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March 28, 2016

Mr. Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Re: Use of Derivatives by Registered Investment Companies and Business Development Companies (File Number S7-24-15)

Dear Mr. Fields:

LCH.Clearnet Limited, LCH.Clearnet SA and LCH.Clearnet LLC (together "LCH") welcomes the opportunity to respond to this proposed rulemaking[1] published by the Securities and Exchange Commission ("SEC" or "Commission"). We commend the Commission on this initiative to update the regulatory framework governing the use of derivatives by registered investment companies and business development companies through proposed Rule 18f-4 under the Investment Company Act of 1940.

LCH is an international, multi-asset class group of clearing houses, or central counterparties ("CCPs"), that manage risk of many diverse portfolios of cleared derivatives.[2] LCH has supported regulatory reform enhancements to the global structure governing derivatives markets that have resulted in a comprehensive, stronger and more robust risk management framework for CCPs, clearing members and end-users of derivatives. We continue to work with regulators and the industry to strengthen the resiliency of CCPs and the safety and soundness of the broader derivatives industry.

The Commission has proposed three primary components in Rule 18f-4: 1) quantitative limits for derivatives portfolios based on gross notional exposures 2) minimum holding of segregated cash or cash equivalent assets against derivative positions and 3) formalized derivatives risk

[1] Use of Derivatives by Registered Investment Companies and Business Development Companies, 80 Fed. Reg. 80883 (Dec. 28, 2015) ("Proposal").

[2] All three CCPs are registered as Derivatives Clearing Organizations (DCOs) with the Commodity Futures Trading Commission ("CFTC"). The LCH.Clearnet Group is the leading multi-asset class and multi-national group of clearing houses, serving major international exchanges and platforms as well as a range of OTC markets. It clears a broad range of asset classes including securities, exchange-traded derivatives, commodities, energy, freight, foreign exchange derivatives, interest rate swaps, credit default swaps, and euro and sterling denominated bonds and repos. LCH.Clearnet Group Limited is majority owned by the London Stock Exchange Group (LSEG), a diversified international exchange group.

management programs. As explained further in our comments below, LCH provides the following recommendations in response to the proposal:

1) If the Commission ultimately determines that additional portfolio constraints are necessary, we recommend applying a risk-based framework that recognizes the leverage and risk in a fund's portfolio, rather than the proposed measure, which uses a blunt calculation of the total notional amount of the derivatives positions in a fund's portfolio.

2) The scope of "qualifying coverage assets" that a fund would have to hold against derivatives positions should be aligned with similar assets permitted to meet collateral requirements within the broader global derivatives framework.

Portfolio Limitations for Derivative Transactions

The proposed portfolio limits calculate the total notional amount of derivatives in order to cap the risk and leverage in a fund's portfolio.[3] As the Commission observes, simply counting the total notional amount of derivatives in a fund's portfolio is a blunt measure and may not appropriately reflect the risk of a derivatives portfolio.[4] We recognize the importance of having an effective and administrable means of limiting the potential leverage in a fund. However, utilizing a notional based limit could artificially and negatively limit a fund's ability to manage risk. This approach may not take into account either a) the risk-reducing benefits of a derivative transaction entered into as a hedging strategy in conjunction with an underlying asset or other derivative instrument or b) the true value at risk within the entire derivatives portfolio.

Should the Commission pursue additional limits on derivatives portfolios, we believe the framework should focus on identifying and managing the actual amount of risk and leverage taken by a fund. Similar risk-based approaches are broadly utilized in international standards and domestic regulations and are administered by CCPs in their initial margin ("IM") calculations.

Central counterparties calculate IM to manage the amount of risk in a portfolio in order to protect the CCP from its members and clients in the event of a counterparty default. Indeed, IM plays a key risk-reducing role in the derivatives markets to limit risk exposure as well as cap the amount of leverage that can be taken. Policies and procedures for setting IM take into account the total risk in a portfolio, including long and short positions at each point in the curve. CCP risk management programs could serve as a useful foundation should the Commission seek to develop an effective and administrable, risk-based framework for managing derivatives exposures and setting limits.

[3] Proposed rule 18f-4(a)(1).

[4] Proposal at 80903.

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Definition of "Qualifying Coverage Assets"

The Proposal would require funds to hold "qualifying coverage assets" against derivatives positions in cash or cash equivalent instruments.[5] As the Commission recognizes, non-cash collateral is permitted in other regulatory constructs with appropriate safeguards, such as haircutting requirements.[6] The definition of "qualifying coverage assets" should be aligned with similar assets permitted to meet collateral requirements within the broader global derivatives framework.

Pursuant to the relevant regulatory requirements, LCH accepts various government bonds that meet our risk and liquidity requirements. LCH applies haircuts to collateral to take into account the varying degrees of risk and to protect against market movements in extreme but plausible circumstances, irrespective of any correlation to the derivatives portfolio being collateralized. Concentration limits are also used as an effective tool to maintain a well-balanced pool of collateral and to avoid concentration risk of any one collateral type, including cash. Utilizing a broader definition of "qualifying coverage assets" while applying the appropriate framework would allow the Commission to better achieve the stated policy objective.

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LCH is grateful for the opportunity to comment on the proposed rulemaking and would be happy to provide further information related to the issues described in this letter at the Commission's request.

Sincerely,

Jonathan Jachym
Head of North America Regulatory Strategy & Government Relations

[5] Proposed rule 18f-4(c)(8).

[6] *See* Proposal at 80932 "…for cleared OTC transactions with clients, cash represented 59% of initial margin received (with government securities representing an additional 39%)" [citing ISDA Margin Survey 2015 (Aug. 2015)].