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By Electronic Mail (rule-comments@sec.gov)

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

Re: File No. SR-FICC-2018-013; Self-Regulatory Organizations; Fixed Income Clearing Corporation; Order Approving a Proposed Rule Change to Expand Sponsoring Member Eligibility in the Government Securities Division Rulebook and Make Other Changes

Dear Mr. Fields:

Fixed Income Clearing Corporation ("FICC")[1] appreciates the opportunity to respond to the concerns raised in the latest comment letter submitted by the Independent Dealer and Trader Association ("IDTA")[2] to the Commission's Order Approving FICC's Proposed Rule Change to Expand Sponsoring Member Eligibility in the Government Securities Division Rulebook and Make Other Changes.[3]

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1 FICC is a clearing agency registered with the U.S. Securities and Exchange Commission ("Commission") pursuant to the Securities Exchange Act of 1934, as amended (the "Exchange Act"). FICC is comprised of two Divisions — the Government Securities Division ("GSD") and the Mortgage-Backed Securities Division ("MBSD"). GSD provides central counterparty services to its customers with respect to the U.S. government securities market, and MBSD provides such services to the U.S. mortgage-backed securities market. FICC has been designated as a systemically important financial market utility ("SIFMU") by the Financial Stability Oversight Counsel pursuant to Section 805 of Title VIII of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank") in recognition of FICC's critical role in the national financial infrastructure. FICC is a subsidiary of The Depository Trust & Clearing Corporation ("DTCC"), which is a user-owned, user-governed holding company for FICC, two other registered clearing agencies and SIFMUs regulated by the Commission, and a number of other companies that provide a variety of post-trade processing and information services. FICC and DTCC's other registered clearing agencies provide critical infrastructure for the clearance and settlement of securities transactions in the U.S.

2 Letter from James Tabacchi, Chairman, IDTA to Christian Sabella, Deputy Director, U.S. Securities and Exchange Commission (April 16, 2019) ("IDTA April 16, 2019 Letter"). IDTA also submitted a comment letter on FICC's rule filing SR-FICC-2018-013 dated January 22, 2019. See Letter from James Tabacchi, Chairman, IDTA to Brent J. Fields, Secretary, U.S. Securities and Exchange Commission (January 22, 2019) ("IDTA January 22, 2019 Letter"). FICC responded to the IDTA January 22, 2019 Letter on February 4, 2019. See Letter from Murray Pozmanter, Managing Director, DTCC to Brent J. Fields, Secretary, U.S. Securities and Exchange Commission (February 4, 2019) ("DTCC February 4, 2019 Letter").

3 Securities Exchange Act Release No. 85470 (March 29, 2019), 84 FR 13328 (April 4, 2019) (SR-FICC-2018-013) ("Approval Order").

I. Background.

On March 29, 2019, the Commission approved FICC's rule filing SR-FICC-2018-013 (the "Rule Filing"),[4] which expanded sponsoring member eligibility and made certain other changes ("Rule Change").[5] The Rule Change consisted of amendments to the Government Securities Division Rulebook ("GSD Rules")[6] that (i) allow a broader group of Netting Members to participate in FICC as Sponsoring Members and (ii) allow a Sponsoring Member to establish a Sponsoring Member Omnibus Account that may contain transactions between a Sponsored Member and a Netting Member other than the Sponsoring Member, which Sponsoring Member Omnibus Account could be in addition to or in lieu of a Sponsoring Member Omnibus Account in which only transactions between a Sponsored Member and its Sponsoring Member are permitted.

II. IDTA Concerns

IDTA raises certain concerns regarding how the expansion of the Sponsoring Member/Sponsored Member Program may increase concentration risk and impair the repo market, which are unfounded and rebutted by FICC below:

A. First, IDTA asserts that the "crux" of their concern is that "the expanded Sponsored Membership Program is likely to increase systemic concentration risk in the market generally, and to FICC in particular."[7]

   While it is true that this expansion of the Sponsoring Member/Sponsored Member Program could potentially increase the overall volume of transactions that are centrally cleared by FICC in that a Sponsored Member's transactions in eligible securities that were previously bilaterally settled may be submitted to FICC by its Sponsoring Member for clearing, as the Commission notes in its Approval Order, the independent risk management of FICC is designed to mitigate any concentration risk associated with such a potential increase in cleared volume.[8] Moreover, IDTA fails to acknowledge the fact that the Rule Change *materially reduces the counterparty concentration risk* that FICC previously faced by being able to admit only well-capitalized banks as Sponsoring Members. As a result of the Rule Change, FICC is now allowed to admit, and is currently in the process of onboarding, a much broader array of Netting Members to participate in the program as Category 2 Sponsoring Members, thereby diversifying the pool of firms facilitating Sponsored Member activity in clearing.

B. Second, IDTA claims that the Rule Change increases the ability of Sponsoring Members to "net positions of its Sponsored Members – even those positions that are not directly facing the

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4 Securities Exchange Act Release No. 84951 (December 21, 2018), 83 FR 67801 (December 31, 2018) (SR-FICC-2018-013) ("Notice of Rule Filing").

5 Approval Order, supra note 3, at 13328.

6 Capitalized terms not defined herein are defined in the GSD Rules, available at http://www.dtcc.com/legal/rules-and-procedures.

7 IDTA April 16, 2019 Letter, supra note 2, at 1.

8 See Approval Order, supra note 3, at 13331.

Sponsoring Member" and that such netting "can lead to dramatic increases in concentration" and increases in "settlement risk exposures to FICC."[9]

FICC believes that these claims reflect a misunderstanding of the Sponsoring Member/Sponsored Member Program. The Rule Change, including the amendments to allow a Sponsoring Member to establish a Sponsoring Member Omnibus Account that may contain transactions between a Sponsored Member and a Netting Member other than the Sponsoring Member, has *no impact* on the manner in which either the Clearing Fund obligations or the Capped Contingent Liquidity Facility ("CCLF") obligations of a Sponsoring Member are calculated by FICC.

As described in the Rule Filing and in GSD Rule 3A, FICC mitigates the market risk associated with Sponsored Member activity through the collection of Clearing Fund from the Sponsoring Member.[10] In light of the fact that FICC novates and guarantees the settlement of each Sponsored Member's position in the Sponsoring Member Omnibus Account, each Sponsored Member's activity is assigned a separate VaR Charge, and, as such, the Unadjusted GSD Margin Portfolio Amount for the Sponsoring Member Omnibus Account is *not reduced* by any netting of positions as between different Sponsored Members within that Sponsoring Member Omnibus Account, *irrespective* of whether the Sponsored Members' cleared positions reflect transactions with its Sponsoring Member or with another Netting Member.

Moreover, as described in the Rule Filing, a Sponsoring Member is responsible for the CCLF obligation of its Sponsoring Member Omnibus Account.[11] While it is true that for purposes of determining the CCLF obligation of a Sponsoring Member's Omnibus Account, FICC calculates such obligation based on the net settlement obligation of that Omnibus Account (as it does for any other Netting Member Account), and such net settlement obligation can reflect the netting of offsetting positions as between two Sponsored Members within that Omnibus Account, none of the amendments under the Rule Change have any impact on that calculation methodology. For example, if a Sponsoring Member has only two Sponsored Members in its Sponsoring Member Omnibus Account, and those two Sponsored Members each have one FICC-cleared position, and those positions offset (i.e., one long and the other short in the same CUSIP for the same tenor), then the Sponsoring Member's CCLF obligation should be zero because FICC does not have a settlement obligation to the Omnibus Account. This will be the case *irrespective* of whether the Sponsored Members' cleared positions reflect transactions with its Sponsoring Member or with another Netting Member.

Likewise, the Rule Change has no impact on how either the Clearing Fund or CCLF obligations of a Sponsoring Member's proprietary Netting Member Account are calculated, *irrespective* of whether the Sponsored Members' cleared positions reflect transactions with its Sponsoring Member or with another Netting Member. For Clearing Fund calculation purposes, no netting or offset is permitted as between the activity in a Sponsoring Member's Omnibus Account and the activity in its proprietary Netting Member Account.[12] Similarly, the CCLF obligations of a

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[9] IDTA April 16, 2019 Letter, supra note 2, at 1-2.

[10] Notice of Rule Filing, supra note 4, at 67802; GSD Rule 3A, Section 10, supra note 6.

[11] Notice of Rule Filing, supra note 4, at 67803-04.

[12] GSD Rule 3A, Section 10(c), supra note 6.

Sponsoring Member's Omnibus Account and its proprietary Netting Member Account are calculated *separately* and are reflective of activity in each of those accounts, respectively, without netting or offset between them.

C. Third, IDTA discusses CCLF and claims that "the incremental costs to Netting Members from [the] top line growth of liquidity risk to FICC is intensifying concentration risks" (i.e., smaller firms are forced to manage their books to stay below the $15 billion liquidity threshold to avoid being assessed an Individual Supplemental Amount), and that the expansion of the Sponsoring Member/Sponsored Member Program exacerbates that problem.[13] IDTA also claims that the increase in FICC's Cover 1 liquidity need[14] is causing Netting Members who exceed the $15 billion liquidity threshold to bear a disproportionate burden to the risks they present to FICC.[15]

With respect to these concerns, FICC notes that a Netting Member's CCLF obligation is based a variety of factors, including, among other things, FICC's Cover 1 liquidity need and the aggregate activity of Netting Members in a firm's respective CCLF tier, and is irrespective of whether that activity represents Sponsored Member transactions or other types of proprietary transactions. For example, the table below illustrates the CCLF allocations of Netting Members in the $15-$20 billion tier compared to the CCLF Aggregate Total Amount over the past 2 years. As the table below depicts, increases in FICC's Cover 1 liquidity need do not necessarily correlate to increases in the CCLF obligations of Netting Members in a particular CCLF tier. Likewise, such firms' CCLF obligations could potentially increase as a result of increased activity, notwithstanding a reduction in the CCLF Aggregate Total Amount.

CCLF Reset Date	CCLF Allocation Per Occurrence in the $15-20 billion tier	CCLF Aggregate Total Amount[16]
Jan 1, 2017	$16.6 million	$73.8 billion
July 1, 2017	$21.6 million	$70.5 billion
Jan 1, 2018	$15.5 million	$69.7 billion
May 1, 2018	$20.9 million	$73.3 billion
Nov 15, 2018	$24.3 million	$72.6 billion
Jan 1, 2019	$29.4 million	$82.2 billion
Feb 8, 2019	$34.9 million	$105.1 billion

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13 IDTA April 16, 2019 Letter, supra note 2, at 4.

14 Cover 1 liquidity need is defined as the liquidity resources required to withstand a default by the Netting Member and its affiliates to which GSD has the largest exposure in extreme but plausible market conditions.

15 IDTA April 16, 2019 Letter, supra note 2, at 4.

16 It should be noted that the figures cited by IDTA for the CCLF Aggregate Total Amount are incorrect. IDTA April 16, 2019 Letter, supra note 2, at 3. The correct figures are included in the above table.

It should also be noted that FICC's Cover 1 liquidity needs in 2019 reflect liquidity reductions from position offsets across the Cover 1 Netting Member affiliates under the assumption that all affiliates default simultaneously. These offsets are currently calculated manually and are not reflected on Netting Members' automated CCLF reports. FICC plans to enhance CCLF reports on May 6, 2019 to reflect the correct CCLF Aggregate Total Amount.

Moreover, with respect to Sponsored Member activity specifically, it should be noted that if a Sponsoring Member were to submit to FICC "matched-book" type Sponsored Member activity (i.e., offsetting positions as between its Sponsored Members), its CCLF obligation to FICC should not increase and, in fact, could potentially decrease, depending on whether one leg of that "matched-book" was already in clearing at FICC. In light of the foregoing, FICC does not believe that the need to manage their CCLF obligations should impair the ability of a broad array of Netting Members to participate in the expanded Sponsoring Member/Sponsored Member Program as Sponsoring Members.

D. Fourth, IDTA claims that the benefits of the expansion of the Sponsoring Member/Sponsored Member service to the repo market are "speculative or conclusory"[17] and makes veiled references to the program impairing liquidity in the repo market.[18]

In terms of the benefits of the expansion to the repo market, IDTA refers to the data FICC and the Commission cited with respect to the exponential growth of money market fund ("MMF") participation in the Sponsoring Member/Sponsored Member program since 2017.[19] IDTA then goes on to misquote FICC as having characterized that benefit solely in terms of increased income for firms.[20] FICC's actual statement refers to the exponential growth proving the value of the program to MMFs in terms of *increasing their lending capacity*, which then results in increased income for them.[21] This ability for MMFs to maintain lending capacity in the market, including at times when dealers' balance sheets are constrained, was deemed so important to the health of the repo market that the Federal Reserve established the Overnight Reverse Repurchase ("RRP") Agreement Program in 2013.[22] Along those lines, it should be noted that the RRP program activity

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17 IDTA April 16, 2019 Letter, supra note 2, at 4.

18 Id. at 5.

19 Id.

20 Id.

21 DTCC February 4, 2019 Letter, supra note 2, at 8 ("This exponential growth in incremental cash investment from MMFs in FICC through the Sponsoring Member/Sponsored Member Program proves the value of the program to them in terms of their ability to increase their lending capacity and, in turn, their income.").

22 See, e.g., Zeynep Senyuz and Manjola Tase, FEDS Notes, Overnight Reverse Repurchase (ON RRP) Operations and Uncertainty in the Repo Market, https://www.federalreserve.gov/econres/notes/feds-notes/overnight-reverse-repurchase-operations-and-uncertainty-in-the-repo-market-20171019.htm ("Another important factor affecting repo market dynamics is financial reporting requirements of institutions which are major participants in the repo market. One prominent example is the implementation of the Basel III leverage ratio regulations. Most foreign dealers are required to report their leverage ratios based on month-end or quarter-end snapshots of their balance sheets, while domestic dealers ratios are calculated from daily averages. The former calculation incentivizes most foreign dealers to contract their balance sheets on financial reporting days. The withdrawal of primary cash borrowers from the market on financial reporting dates leaves MMFs, the main cash lenders in the repo market, looking for alternatives. The ON RRP operations provide an investment vehicle for MMFs on these days and generally prevents the market repo rate from falling below the offering rate. Therefore, take-up at the ON RRP operations tends to be elevated at month-ends due to increased investments by MMFs." (footnote omitted)).

in Treasury collateral has seen a precipitous drop from $365.2 billion in June 2017 to $0.7 billion in March 2019,[23] which is directly correlated to the increase in MMF participation in the Sponsoring Member/Sponsored Member Program. This suggests that the Sponsoring Member/Sponsored Member Program could potentially supplant the RRP as an important safety valve for lending capacity to the MMFs.

IDTA also discusses concerns regarding impairment in the liquidity of the repo market, citing the dislocations in the overnight repo rate that occurred at year-end 2018,[24] and makes a veiled reference to the expansion of the Sponsoring Member/Sponsored Member program as "further impair[ing] the repo market."[25] As described in the Bloomberg article cited by IDTA, those temporary dislocations in the repo rate at year-end 2018 related primarily to dealers trimming their balance sheets for regulatory reasons, rather than funding stress.[26] In fact, as Ronin pointed out in its comment letter on the Rule Filing, by providing needed capacity at times of balance sheet constraint, FICC's Sponsoring Member/Sponsored Member Program should actually help to temper, rather than exacerbate, volatility in repo rates.[27]

DTCC thanks the Commission for considering our comments. Should you have any questions, please contact me at [redacted] or [redacted].

Very truly yours,

Murray Pozmanter
Managing Director
Head of Clearing Agency Services

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23 Office of Financial Research, U.S. MMFs' investment in the repo market, https://www.financialresearch.gov/money-market-funds/us-mmfs-investments-in-the-repo-market/.

24 IDTA April 16, 2019 Letter, supra note 2, at 5.

25 Id.

26 See Alex Harris, Eye-Popping Surge in Repo Rate Blamed on Rules Instead of Funding Stress, Bloomberg, (January 2, 2019), https://www.bloomberg.com/news/articles/2019-01-02/eye-popping-repo-surge-blamed-on-rules-instead-of-funding-stress.

27 See Letter from Robert E. Pooler, Jr., Chief Financial Officer, Ronin Capital LLC to Brent J. Fields, Secretary, U.S. Securities and Exchange Commission (January 18, 2019), at 3. As the DTCC February 4, 2019 Letter notes, the Office of Financial Research's U.S. Money Market Fund Monitor shows that, as of December 31, 2018, MMF Treasury repo activity with FICC was $136.9 billion. See DTCC February 4, 2019 Letter, supra note 2, at 8.