

April 17, 2024

Submitted Electronically

Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: SEC “Notice of Filing of Proposed Rule Change, as Modified by Partial Amendment No. 1, To Modify the GSD Rules To Facilitate Access to Clearance and Settlement Services of All Eligible Secondary Market Transactions in U.S. Treasury Securities” [Release No. 34-99817; File No. SR-FICC-2024-005]; “Self-Regulatory Organizations; Fixed Income Clearing Corporation; Notice of Filing of Proposed Rule Change To Modify the GSD Rules (i) Regarding the Separate Calculation, Collection and Holding of Margin for Proprietary Transactions and That for Indirect Participant Transactions, and (ii) To Address the Conditions of Note H to Rule 15c3-3a” [Release No. 34-99844; File No. SR-FICC-20240007]; and “Notice of Filing and Extension of Review Period of Advance Notice To Modify the GSD Rules (i) Regarding the Separate Calculation, Collection and Holding of Margin for Proprietary Transactions and That for Indirect Participant Transactions, and (ii) To Address the Conditions of Note H to Rule 15c3-3a” [Release No. 34-99845; File No. SR-FICC-2024-802]

Dear Ms. Countryman:

The International Swaps and Derivatives Association, Inc. (“ISDA”)¹ respectfully submits this comment letter to the Securities and Exchange Commission (the “**Commission**” or the “**SEC**”) in response to the Fixed Income Clearing Corporation’s (“**FICC**”) recently published proposed rule changes. This comment letter will address (1) FICC’s proposed rule change published by the SEC

¹ Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has over 1,000 member institutions from 77 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 ISDA’s website: www.isda.org. Follow us on [Twitter](#), [LinkedIn](#), [Facebook](#) and [YouTube](#).

on March 27, 2024 to modify its Government Securities Division Rulebook (“**GSD Rules**” or “**Rules**”)² such that FICC may facilitate access to clearance and settlement services of all eligible secondary market trades in U.S. Treasury securities in accordance with the Securities Exchange Act of 1934 (“**Exchange Act**”) (the “**Access Proposal**”³); and (2) FICC’s advance notice to amend its GSD Rules and proposed rule change published by the SEC on March 28, 2024 regarding separate and independent calculation, collection, and holding of margin supporting Proprietary Transactions by a FICC Netting Member or that a Netting Member submits on behalf of indirect participants (the “**Segregation Proposal**”,⁴ and together with Access Proposal, the “**FICC Proposals**”). These FICC Proposals arise out of operationalizing and implementing the SEC’s Treasury clearing rules (the “**Treasury Clearing Rules**”).⁵ Terms used but not defined have the meaning in the FICC Rules or in the FICC Proposals.

In addition to its comments on the FICC Proposals, ISDA provides at the end of this letter a brief discussion of concerns relevant to FICC’s anticipated rule in June on the clearing mandate.

I. FICC Should Establish a Rule for Its Agent Clearing Service Addressing How to Close Out a Client’s Positions as It Provides for Under the Sponsored Service

The FICC Proposals are silent with respect to whether an Agent Clearing Member may close out an Executing Firm Customer’s positions. In contrast, the Sponsored Service explicitly provides for the liquidation of a Sponsored Member’s positions under Section 18 of FICC Rule 3A which a Sponsoring Member may invoke to exercise its remedies if the Sponsored Member defaults under it, to offset with the Sponsoring Member.⁶ An Executing Firm Customer, however, could similarly experience an event of default or other triggering condition just as a Sponsored Member may experience. The FICC Proposals do not provide for liquidation of an Executing Firm Customer’s positions presumably because in the Sponsored Service, the Sponsored Member is an actual

² See FIXED INCOME CLEARING CORPORATION, Fixed Income Clearing Corporation Government Securities Division Rulebook, <https://www.dtcc.com/~media/Files/Downloads/legal/rules/ficcgovrules.pdf> (effective as of Dec. 4, 2023) [hereinafter GSD Rules].

³ *Self-Regulatory Organizations; Fixed Income Clearing Corporation; Notice of Filing of Proposed Rule Change, as Modified by Partial Amendment No. 1, To Modify the GSD Rules to Facilitate Access to Clearance and Settlement Services of All Eligible Secondary Market Transactions in U.S. Treasury Securities*, 89 Fed. Reg. 21,362 (Mar. 27, 2024) [hereinafter Access Proposal].

⁴ *Self-Regulatory Organizations; Fixed Income Clearing Corporation; Notice of Filing and Extension of Review Period of Advance Notice To Modify the GSD Rules (i) Regarding the Separate Calculation, Collection and Holding of Margin for Proprietary Transactions and That for Indirect Participant Transactions, and (ii) to Address the Conditions of Note H to Rule 15c3-3a*, 89 Fed. Reg. 21,586 (Mar. 28, 2024) [hereinafter Segregation Proposal].

⁵ Standards for Covered Clearing Agencies for U.S. Treasury Securities and Application of the Broker-Dealer Customer Protection Rule with Respect to U.S. Treasury Securities, Exchange Act Release No. 99149 (Dec. 13, 2023), 89 Fed. Reg. 2,714 (Jan. 16, 2024) [hereinafter Treasury Clearing Rules].

⁶ See GSD Rules, *supra* note 2.

member of FICC,⁷ but that is not the case in the Agent Clearing Service, where the position is entered into by the Agent Clearing Member on behalf of the Executing Firm Customer.⁸ ISDA is unaware of any regulatory reason for the lack of a similar rule under the Agent Clearing Service.

FICC should provide in its Rules that an Agent Clearing Member may liquidate an Executing Firm Customer's positions by transferring the positions to its proprietary/house account or by transferring positions into the Agent Clearing Member Omnibus Account to flatten open positions of the Executing Firm Customer. Failure to provide a mechanism for closing out a defaulting client's positions under the Agent Clearing Service will necessitate an Agent Clearing Member's having to keep the positions open at FICC for the positions' entire duration, even if they are term trades. Without being able to take the obvious step to liquidate the client's positions, an Agent Clearing Member will have to develop alternative methods for reducing any resulting exposure and determine how to claim associated costs, including in the client's bankruptcy. The cleared derivatives model allows a clearing member to transfer a defaulting client's positions to the clearing member's house account or to close out client positions or restore the client's account balance when a client fails to satisfy a margin call, leaving the decision on the appropriate action to take with the clearing member.⁹ Accordingly, ISDA asks that FICC incorporate a rule under the Agent Clearing Service to allow an Agent Clearing Member to transfer and close out the positions of a defaulting Executing Firm Customer.

ISDA understands that the legal analysis regarding closing out positions is more complex for trades done by a client with an executing broker that are given up to the client's Sponsoring Member or Agent Clearing Member for novation to FICC ("done-away" trades), as opposed to "done-with" trades that are initially entered into by the client with its own Sponsoring Member or Agent Clearing Member for novation to FICC. ISDA is willing to engage with FICC to ensure that any close-out provision or right to terminate added to the FICC Proposals covering done-away trades is evaluated under all relevant jurisdictions. In the meantime, however, including a liquidation provision for done-with trading under the Agent Clearing Service is warranted.

⁷ See Access Proposal, *supra* note 3 at 21,364 ("The Sponsored Service permits Netting Members, approved by FICC as 'Sponsoring Members,' to sponsor certain institutional firms, referred to as 'Sponsored Members,' into GSD Membership.").

⁸ See *id.* at 21,365 ("Unlike the Sponsored Service, FICC has no relationship with the Executing Firm and all obligations (i.e., margin and settlement) under the Rules remain with the Submitting Member.").

⁹ See, e.g., CME Rule 930.K ("If an account holder fails to comply with a performance bond call within a reasonable time (the clearing member may deem one hour to be a reasonable time), the clearing member may close out the account holder's trades or sufficient contracts thereof to restore the account holder's account to required performance bond status. Clearing members shall maintain full discretion to determine when and under what circumstances positions in any account shall be liquidated."), <https://www.cmegroup.com/content/dam/cmegroup/rulebook/CME/1/9/9.pdf>. In the event of a client default, LCH Limited permits an FCM clearing member to request the transfer of client swaps to its proprietary account. See LCH Limited FCM Regulation 13(d); LCH Limited FCM Procedure 2.1.14(a).

II. FICC Needs to Support Its Minimum Clearing Fund Deposit Requirement Under the Agency Clearing Model

Under the FICC Proposals, each indirect participant that wishes to open a segregated account with a Netting Member must deposit at least \$1 million in cash in the segregated account.¹⁰ ISDA urges FICC to reconsider this minimum amount and establish a minimum account based on a client's actual risk profile. FICC has supported this minimum requirement with nothing more than the existing rule applicable to Margin Portfolios offered under the Sponsored Service that also requires a \$1 million minimum deposit and the fact that FICC is restricted from using these funds for loss mutualization purposes.¹¹

ISDA believes that the existing requirement for Margin Portfolios is not appropriate substantiation for the indirect participant segregated account requirement. First, Margin Portfolios are available for Direct Participants, who are the largest participants on FICC and can easily afford the \$1 million requirement. In contrast here, there likely will be a range of indirect participants that desire segregated accounts. Second, FICC admits that it is not able to predict how many indirect participants may select a segregated account or the size and volume of their activity.¹² FICC does not appear to have conducted any study of what that activity could look like and whether it supports a \$1 million minimum deposit. Any required minimum deposit should be determined by the individual client and the risk such client presents to FICC and other market participants.

Third, the \$1 million cash requirement may discourage or make small firms unable to select the segregation model and leave only the general omnibus models for access to FICC and clearing. The availability of segregated accounts should not discriminate against certain types of firms, but that is exactly what this requirement may do.

ISDA encourages FICC to review the proposed minimum deposit requirement and consider requiring an amount more commensurate with the risk posed by the client, consistent not only with the goal of providing a liquid, dynamic market for those that are required to clear their U.S. Treasury trades but also with the goal of promoting accessibility to the U.S. Treasury securities market.

¹⁰ See Segregation Proposal, *supra* note 4 at 21,595 (“FICC is proposing to require that the Segregated Margin Requirement be no lower than \$1 million per Segregated Indirect Participant, and that the same form of deposit requirements set forth in Rule 4, Section 3 apply to Segregated Customer Margin such that no less than \$1 million per Segregated Indirect Participant consist of cash.”).

¹¹ See *id.* (“First, this minimum requirement is consistent with the \$1 million minimum cash requirement applicable to each Margin Portfolio of a Netting Member. FICC believes it is appropriate to apply the same minimum cash requirement to each Segregated Indirect Participant that it currently applies to each Margin Portfolio ... Second, because FICC would be restricted from using these funds to address any losses other than losses resulting from the indirect participant for whom these funds are deposited, FICC believes this minimum requirement is appropriate to mitigate the risk exposures presented by this limitation.”).

¹² See *id.* (“FICC is not able to predict how many indirect participants may elect to submit activity to FICC through a Segregated Indirect Participants Account, or the size and volume of that activity.”).

III. The Rules Should Allow Porting of Client Positions in the Ordinary Course

ISDA encourages FICC to explicitly provide a porting mechanism for use in the ordinary course that allows a client to transfer its positions to another Netting Member. As proposed, the Rules do not allow a Sponsored Member or Executing Firm Customer to port its positions at FICC to a different Clearing Member. A Clearing Member’s client desires portability because, if there is an issue with a Clearing Member (short of a bankruptcy), the client wants the ability to port positions away from that member to a different clearing member. In addition, a client may enter into an arrangement with a new Clearing Member and may need the ability to transfer its positions in this scenario.

The ability to port positions exists in the futures clearing model.¹³ As such, many clients are accustomed to their porting rights and use them as an important risk management tool. Of course, the transferee Clearing Member must accept the client’s positions and generally the client must have sufficient margin in the account to effect a transfer. Guardrails such as these are acceptable, and FICC could consider incorporating them into its porting model. ISDA supports the introduction of a porting mechanism and requests FICC to implement this measure.

IV. Liability for LEI Accuracy Should Be Nuanced

FICC’s indemnification requirement for legal entity identifiers (“LEIs”) must be more nuanced. Under the Agent Clearing Service, Agent Clearing Members are responsible for submitting the LEIs of their respective Executing Firm Customers to FICC and ensuring continued accuracy of LEI information.¹⁴ Section 3(d) of Proposed Rule 8 of FICC’s Rules requires Agent Clearing Members to indemnify FICC, *and FICC’s employees, officers, directors, shareholders, agents, and Members*, “for any and all losses, liabilities, expenses and Legal Actions suffered or incurred by these parties arising from an Agent Clearing Member’s failure to have the current LEIs of its Executing Firm Customers on file with [FICC].”¹⁵

LEIs must be renewed on an annual basis. In some instances, the person renewing the LEI does not do so in a timely manner, meaning that an LEI may be lapsed for a period before ultimately being renewed. A person’s trading activity should not be halted by virtue of this sort of lapse. In addition, an Agent Clearing Member would not be aware of any lapse without itself verifying on any number of LEI service provider websites that its Executing Firm Customers have in fact renewed their LEIs. It is unclear why FICC needs this indemnification, particularly where other information identifying Executing Firm Customers will be submitted with each trade. There is no

¹³ See, e.g., CME Rule 853.A.

¹⁴ See Access Proposal, *supra* note 3 at 21,366 (“The proposed requirement that Agent Clearing Members both provide and maintain a current LEI on file with FICC for each of its Executing Firm Customers and provide an indemnification related to this”).

¹⁵ See *id.*; See also Securities Exchange Act Release No. 34-99817, File No. SR-FICC-2024-005, Ex. 5, at 138 (Mar. 21, 2024) [hereinafter SEC Access Proposal Release].

regulatory requirement that ISDA is aware of requiring LEIs for U.S. Treasury cash and repurchase or reverse repurchase (collectively, “repo”) trades.

For these reasons, ISDA believes that the indemnification should be narrowly tailored to cover “losses, liabilities, and expenses arising out of any Legal Action... arising from an Agent Clearing Member’s failure to have the current LEIs of its Executing Firm Customers on file with [FICC] where such failure is the result of the Agent Clearing Member’s gross negligence, willful misconduct or fraudulent conduct.” ISDA respectfully requests FICC to reconsider the proposed indemnification provision and tailor it more appropriately.

V. The FICC Proposals Should Clarify That Funds-Only Settlement Amounts Are Settlement Payments Rather Than Margin

ISDA members request assurance from FICC that funds-only settlement amounts will be treated as settlement payments rather than cash margin so that upon the client’s payment or receipt, the settlement resets or reprices the trade to an agreed-upon level. FICC’s guidance on this matter is necessary for market participants to accurately gauge their obligations and to ensure compliance with FICC’s applicable segregation rules. While the FICC Proposals do not appear to treat funds-only settlement amounts as client-delivered margin subject to segregation,¹⁶ the absence of an explicit carve-out necessitates further clarification. Accordingly, ISDA asks FICC to clarify that funds-only settlement payments are not considered margin and will not be subject to segregation requirements.

VI. FICC Should Confirm Whether Branches of a Bank or a Netting Member’s Affiliates Have the Ability to Access FICC by the Bank’s or Netting Member’s Direct Membership

The Access Proposal does not address whether a U.S. Treasury repo entered into by a bank branch or an affiliate of a Direct Participant of FICC may be cleared in the Direct Participant’s account at FICC. ISDA believes that in this instance the bank’s branches and Netting Member’s affiliates should be able to establish a separate Margin Portfolio within the Direct Participant’s account that would be separately netted and margined, such that they would not have to establish indirect access to FICC. This type of arrangement currently exists under the futures clearing model, where a Clearing Member may clear certain affiliates’ positions in its house account.¹⁷ ISDA understands that FICC has separate legal requirements applicable to foreign branches and that the branches

¹⁶ See Securities Exchange Act Release No. 34-99844, File No. SR-FICC-2024-007, Ex. 5, at 133 (Mar. 22, 2024) [hereinafter SEC Segregation Proposal Release] (funds-only settlement amounts are missing from proposed Rule 4’s description of the calculation and collection of segregated margin).

¹⁷ See CFTC Regulation 1.3 (defining “proprietary account” to include a trading account carried on the books and records of person for one of the following persons or of which 10% or more is owned by one of the following persons, or an aggregate of 10% or more of which is owned by more than one of the following persons: “[a] business affiliate that directly or indirectly controls such individual, partnership, corporation or association; or [a] business affiliate that, directly or indirectly is controlled by or is under common control with, such individual, partnership, corporation or association...”).

would have to satisfy those before having the ability to access FICC in this manner. ISDA respectfully asks FICC to confirm that bank branches and affiliates of a Direct Participant may enter into a U.S. Treasury repo that may be cleared in the direct participant’s account at FICC.

VII. FICC Should Confirm that Segregation of Margin for Indirect Participants Does Not Magnify Risk on Netting Members

ISDA requests that FICC confirm that FICC’s Required Fund Deposit calculations for a Netting Member adequately consider all of a Netting Member’s activity at FICC, including its activity for indirect participants and, in particular, those who post margin held in Segregated Indirect Participants Accounts. Default fund allocation in clearing agencies is typically based on a stress-loss exposures of each clearing member, including the stress loss-exposures of their client activity. ISDA members would like to better understand how FICC will allocate its Clearing Fund, which in FICC’s case encompasses a default fund component, to consider risks that are brought into the system by indirect participants.

In FICC’s new Margin Component Schedule, which is part of the Segregation Proposal, it is not clear whether the Required Fund Deposit to be posted by Netting Members under Section 2 incorporates any exposure associated with Segregated Indirect Participant Accounts. Required Fund Deposit for those segregated accounts is calculated separately in Section 3.¹⁸ Under Section 4 of the Margin Component Schedule, FICC is able to require additional Required Fund Deposits from Netting Members if necessary to protect FICC from (x) risk arising from laws, rules or regulations that would affect, among other things, access to the Netting Member’s Required Fund Deposit or the netting, closing out or liquidating trades; or (y) market conditions and other financial and operational capabilities of the Netting Member.¹⁹ These factors, however, do not seem to cover any enhanced risk that may arise relating to the Netting Member’s obligations to FICC (including its guarantee to FICC) for its clients who are indirect participants generally or who choose segregation specifically. In particular, in certain instances, Netting Members are permitted to prefund temporarily the margin posting of their segregated indirect participants, but they are not allowed to do so on a permanent basis.²⁰ That puts pressure on the Netting Member’s own Required Fund Deposit, which it seems would still cover the obligations of all of its clients, and generally on the Netting Member and the broader FICC membership, in the event of a failure by any segregated indirect participant.

¹⁸ See Segregation Proposal, *supra* note 4 at 21,593 (“Section 3 of the new Margin Component Schedule ... would provide for FICC to perform substantially the same calculation it currently performs when determining a Netting Member’s Required Fund Deposit ...”).

¹⁹ See SEC Segregation Proposal Release, *supra* note 14, Ex. 5 at 158 (Mar. 22, 2024).

²⁰ See *id.* at 123-124 (“A Netting Member may designate any of its Indirect Participants Accounts as a Segregated Indirect Participants Account. Any such designation of an Account shall constitute a representation to the Corporation by the Netting Member that the Netting Member intends to meet all Segregated Customer Margin Requirements for such Account using cash or securities deposited by Segregated Indirect Participants with the Netting Member, **except to the extent the Netting Member temporarily uses its own securities** in accordance with the conditions set forth in Section (b)(1)(iii) of Note H to SEC Rule 15c3-3a.” (emphasis supplied).

VIII. ISDA Requests That FICC Provide Its Rationale for Each Client Access Model to Help Clients Select the Appropriate Access Method and to Avoid Industry Confusion

While ISDA appreciates the trainings and question-and-answer sessions that FICC has held to explain how its clearing models work, FICC should also explain the rationale for and the benefits of each clearing model. We understand that access will be provided through the following account types: (1) Agent Clearing Member Omnibus Account; (2) Segregated Agent Clearing Member Omnibus Account; (3) Sponsoring Member Omnibus Account; and (4) Segregated Sponsoring Member Omnibus Account. Giving market participants a better sense of the use cases for and benefits of each type of access will help them select the most appropriate access model for their businesses. For instance, one area of clarification could center on why a market participant would choose the segregated option under the Sponsored Service as opposed to the segregated option under the Agent Clearing Service. ISDA therefore requests that FICC take additional steps to articulate and outline what might motivate a market participant's selection of one model over another.

IX. ISDA Remains Concerned About the Workability of the Inter-Affiliate Clearing Exemption and the Requirement to Clear Certain Tri-Party Trades

The Treasury Clearing Rules exempt from clearing inter-affiliate trades between a FICC Direct Participant and one of its affiliates only if all of the affiliate's outward-facing trades are cleared.²¹ ISDA members continue to be concerned that the inter-affiliate clearing exemption specified in the Treasury Clearing Rule does not leave sufficient flexibility for a Direct Participant and its affiliates to conduct treasury or liquidity management within their corporate group, which can have little to do with client-facing trades. ISDA encourages FICC to be proactive in issuing, and working with the SEC to provide, guidance and clarification on this exemption and is, itself, happy to assist in any way.

Also, ISDA members who are Direct Participants of FICC continue to be concerned about the requirement to centrally clear tri-party repos that have U.S. Treasuries at the outset of the trade. ISDA requests that FICC consider in its June rulemaking on the clearing mandate confirming that U.S. Treasuries do not have to be cleared if they are initially part of a pool of tri-party repo collateral that contains some non-Eligible Securities (i.e., securities not eligible to be cleared in FICC). ISDA understands that it is not workable to clear the U.S. Treasury portion of that tri-party repo trade. If clearing were nonetheless to be required, market participants would likely substitute cash in lieu of U.S. Treasuries, which could have a liquidity impact on the market that should be evaluated. In addition, there are other instances where it may be appropriate, using a cost-benefit

²¹ See Treasury Clearing Rules, *supra* note 5 at 2,737 (“the definition of an eligible secondary market trades in Rule 17ad-22(a) [shall] conditionally exclude inter-affiliate repurchase and reverse repurchase trades. Specifically, the Commission is excluding from that definition any repurchase or reverse repurchase agreement collateralized by U.S. Treasury securities entered into between a direct participant and an affiliated counterparty, provided that the affiliated counterparty submits for clearance and settlement all other repurchase or reverse repurchase agreements collateralized by U.S. Treasury securities to which the affiliated counterparty is a party.”).

analysis, to exclude tri-party repo trades that contain U.S. Treasuries as part of a pool at the outset (e.g., where U.S. Treasuries are initially only a de minimis part of a tri-party trade). ISDA looks forward to further engaging with FICC and the SEC on these issues.

X. Conclusion

We appreciate the opportunity to submit our comments in response to the FICC Proposals. We welcome FICC's clarification and continued efforts to provide guidance to market participants in advance of the effective date of the clearing mandate. ISDA applauds FICC for hosting forums and office hours to explain the FICC Proposals and respond to questions. The number of questions raised during these events demonstrates that more guidance is needed before the Rules become effective. ISDA supports FICC's efforts and is available to work with FICC on where further guidance or rule changes would be beneficial to market participants and, ultimately, to FICC.

ISDA members are strongly committed to maintaining the safety and efficiency of the U.S. financial markets and ensuring the efficiency of robust and functional derivatives markets. While ISDA supports FICC's efforts to create the access and segregation framework to fulfill the Treasury Clearing Rules' mandate for the clearing of certain cash and all repo secondary market trades in U.S. Treasury securities, we believe that the current FICC Proposals require the adjustments set out in this letter.

We look forward to further engagement with FICC on these important issues. Please do not hesitate to contact Christopher Young, Head of U.S. Public Policy, at (202) 683-9339, should you have any questions.

Sincerely,



Katherine Darras
General Counsel
International Swaps and Derivatives Association (ISDA)