

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-92501; File No. SR-LCH SA-2021-001)

July 26, 2021

Self-Regulatory Organizations; LCH SA; Order Approving Proposed Rule Change Relating to the Clearing of Single-Name Credit Default Swaps by U.S. Customers

I. Introduction

On April 13, 2021, Banque Centrale de Compensation, which conducts business under the name LCH SA (“LCH SA”), filed with the Securities and Exchange Commission (“Commission” or “SEC”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”),¹ and Rule 19b-4,² a proposed rule change to amend LCH SA’s (i) CDS Clearing Rule Book (the “Rule Book”); (ii) CDS Clearing Supplement (the “Clearing Supplement”); (iii) CDS Clearing Procedures (the “Procedures”); and (iv) FCM Clearing Regulations (“Clearing Regulations”) to allow LCH SA to offer clearing services in respect of single-name CDS that are security-based swaps (“SBS”) submitted by Clearing Members on behalf of their U.S. clients.³ The proposed rule change was published for comment in the Federal Register on May 3, 2021.⁴ On June 10, 2021, the Commission designated a longer period within which to take action on the

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ Capitalized terms used but not defined herein have the meanings specified in the Rule Book, the Clearing Supplement, the Procedures, and the Clearing Regulations, as applicable.

⁴ Self-Regulatory Organizations; LCH SA; Notice of Filing of Proposed Rule Change Relating to the Clearing of Single-Name Credit Default Swaps by U.S. Customers, Exchange Act Release No. 34-91676 (April 26, 2021); 86 Fed. Reg. 23445 (May 3, 2021) (SR-LCH SA-2021-001) (“Notice”).

proposed rule change, until August 1, 2021.⁵ The Commission did not receive comments regarding the proposed rule change. For the reasons discussed below, the Commission is approving the proposed rule change.

II. Description of the Proposed Rule Change

Currently, LCH SA's Clearing Members are permitted to submit for clearing swaps on behalf of their U.S. clients. The proposed rule change would amend the LCH SA documents mentioned above to permit LCH SA's Clearing Members also to submit for clearing SBS on behalf of their U.S. clients. Thus, after the proposed rule change becomes effective, LCH SA would permit its Clearing Members to submit for clearing both swaps and SBS on behalf of their U.S. clients.

In addition to this initiative, the proposed rule change would also make certain other confirming and clarifying changes, as discussed further below in Part II.E.

A. Rule Book

To facilitate this initiative, the proposed rule change would amend the Rule Book to, among other things, (i) modify existing and adopt new defined terms; (ii) modify the membership requirements applicable to Clearing Members; (iii) remove provisions that prohibit Clearing Members from offering clearing services to U.S. clients with respect to SBS; (iv) establish the account structure for Clearing Members clearing SBS on behalf of U.S. clients; (v)

⁵ Self-Regulatory Organizations; LCH SA; Notice of Designation of Longer Period for Commission Action on Proposed Rule Change Relating to the Clearing of Single-Name Credit Default Swaps by U.S. Customers, Exchange Act Release No. 34-92142 (June 10, 2021); 86 Fed. Reg. 32079 (June 16, 2021) (SR-LCH SA-2021-001).

update provisions to apply them to Clearing Members that are broker-dealers; and (vi) amend the Appendix to apply relevant provisions of the CDS Default Management Process to SBS. These amendments are discussed below according to the different titles of the Rule Book.

i. Title I

The proposed rule change would add new, and modify existing, defined terms related to Clearing Members and Clients found in Title I of the Rule Book. These changes would facilitate registered broker-dealers becoming Clearing Members for the purpose of clearing SBS on behalf of U.S. clients. For example, the proposed rule change would add a definition for “BD,” to mean a legal entity that is a “broker” or “dealer” as defined in Section 3(a)(4) or 3(a)(5) of the Act, respectively, and is registered in such capacity with the Commission and a member in good standing of FINRA. Similarly, the proposed rule change would amend the defined term “FCM Clearing Member” to be “FCM/BD Clearing Member.” As amended, the term “FCM/BD Clearing Member” would mean any FCM, BD, or legal entity that is both an FCM and BD that has been admitted to LCH SA as a clearing member. The proposed rule change would make a similar modification to the defined term “FCM Client,” which would become “FCM/BD Client.”

Similarly, the proposed rule change would modify a number of defined terms and add new defined terms that relate to the account structure in which transactions would be recorded and collateral for Cleared Swaps and SBS would be held. Among other changes, the proposed rule change would add a new defined term for “Cleared Swap,” which would be used to differentiate between “swaps” and “SBS” and their different account structures and add new defined terms for “Cleared Swaps Customer” and “Cleared Swaps Customer Collateral.”

Overall, these changes would establish three account structures: (i) a separate account structure

for Cleared Swaps; (ii) a separate account structure for SBS; and (iii) an account structure in which an FCM/BD Clearing Member that is both an FCM and a BD may elect to clear and hold margin for FCM/BD Cleared Transactions that are SBS for FCM/BD Clients on a commingled basis with Cleared Swaps.⁶

Moreover, the proposed rule change would amend certain terms with respect to legal jurisdictions to reflect the availability of clearing SBS for U.S. clients. Specifically, the proposed rule change would modify the term “Non-U.S. CCM” to mean, when used in the context of an Original Transaction, a CCM that has its residence in, is organized under the laws of, or has its principal place of business located in, a jurisdiction other than the United States, its territories or possessions and is not a registered BD or FCM. Similarly, the proposed rule change would modify the term “U.S. CCM Client” to mean a Client of an FCM or a BD or any Client that has its residence in, is organized under the laws of, or has its principal place of business located in the United States, its territories or possessions.

Finally, the proposed rule change would make clarifying and conforming changes to other defined terms, and other Articles of Title I of the Rule Book, to reflect these changes. These changes would update references to Clearing Members to apply them to FCM/BD Clearing Members instead of just FCM Clearing Members.

⁶ See Order Granting Conditional Exemptions Under the Securities Exchange Act of 1934 in Connection With Portfolio Margining of Swaps and Security-Based Swaps, Exchange Act Release No. 68433 (Dec. 14, 2012); 77 Fed. Reg. 75211 (Dec. 19, 2012) (“Portfolio Margining Order”) (setting out certain conditions that dually registered clearing agencies/derivatives clearing organizations and participating BD/FCMs must satisfy when offering a program to commingle and portfolio margin cleared CDS for customer positions).

ii. Title II and Title III

The proposed rule change would next amend Title II and Title III of the Rule Book, which relate to the requirements applicable to LCH SA's Clearing Members and LCH SA's clearing operations. First, the proposed rule change would amend Article 2.1.1.2 of the Rule Book to provide that, without prejudice to the membership requirements set out in the CDS Clearing Rules and applicable law, both FCMs and BDs are eligible to become FCM/BD Clearing Members. Second, the proposed rule change would amend Article 2.2.3.1 to define a BD's "net capital" as its net capital as provided in SEC Rule 15c3-1.

The proposed rule change would also make conforming changes throughout Title II and in Article 3.1.10.9 of Title III to apply them to an FCM/BD Clearing Member instead of just an FCM Clearing Member. These changes would update references to Clearing Members to apply them to FCM/BD Clearing Members instead of just FCM Clearing Members.

iii. Title IV

The proposed rule change would also amend Title IV regarding risk management, specifically, Article 4.2.2.5, which relates to the return of excess collateral. Under Article 4.2.2.5 as revised, if (i) the FCM/BD Margin Balance of an FCM/BD Client Financial Account exceeds the relevant FCM/BD Client Margin Requirement prior to the Morning Call or (ii) the value of the Collateral attributed to the FCM/BD Buffer Financial Account exceeds the FCM/BD Client Collateral Buffer Threshold, then LCH SA would treat the excess as follows. If the excess is related to Cleared Swaps, it would be reclassified as FCM/BD Swaps Unallocated Client Excess Collateral, and thereafter may be returned to the FCM/BD Clearing Member upon request in the conditions set out in Section 3 of the Procedures, subject to Article 6.2.5 of the Rule Book. If the

excess is related to SBS (excluding SBS that are held in the FCM/BD Swaps Client Account Structure as Cleared Swaps, as described below), it would be reclassified as FCM/BD SBS Client Excess Collateral, and thereafter may be returned to the FCM/BD Clearing Member upon request in the conditions set out in Section 3 of the Procedures, subject to Article 6.2.5 of the Rule Book.

The proposed rule change would also make conforming changes throughout Title IV to apply the articles to an FCM/BD Clearing Member instead of just an FCM Clearing Member. These changes would update references to Clearing Members to apply them to FCM/BD Clearing Members instead of just FCM Clearing Members.

iv. Title V

The proposed rule change next would amend Title V, regarding CDS Client Clearing Services provided by a CCM. Here the proposed rule change would amend Article 5.1.1.2 to permit LCH SA's Clearing Members to submit for clearing SBS on behalf of their U.S. clients. Currently, Article 5.1.1.2 prohibits a Non-U.S. Clearing Member from offering client clearing services to any U.S. client with respect to SBS and any U.S. Clearing Member from offering client clearing services to any client with respect to SBS. The proposed rule change would delete this provision.

The proposed rule change also would amend another provision of Article 5.1.1.2 that currently prohibits a Clearing Member from offering clearing services to any U.S. client (other than an affiliate of the Clearing Member) with respect to an Original Transaction that is not SBS, unless the Clearing Member meets the specified conditions. As amended, this provision would prohibit a Clearing Member from offering clearing services to any U.S. client, other than an

affiliate of the Clearing Member, with respect to swaps and SBS, unless the Clearing Member (i) is an FCM/BD and (ii) has provided LCH SA with an opinion of counsel confirming that the provision of clearing services would not be contrary to applicable law.

v. Title VI

The proposed rule change would amend Title VI, regarding FCM/BD client clearing. First, Article 6.1.1.2(vi) currently prohibits an FCM Clearing Member from providing CDS Client Clearing Services (defined as clearing services in respect of CDS and/or Index Swaptions provided by a Clearing Member to its Clients) to any client. The proposed rule change would delete this prohibition.

The proposed rule change next would amend Article 6.2.1.1, which currently specifies the account structure that LCH SA must open and maintain for each FCM Clearing Member that provides client clearing services for swaps. The proposed rule change would amend this article so that it specifies the client account structure for an FCM/BD Clearing Member providing client clearing services for swaps and SBS. Thus, the proposed rule change would add a new subsection (ii) that specifies the accounts that would make up the FCM/BD SBS Client Account Structure. This structure would mirror the structure applicable to swaps.

Thus, under the proposed rule change, Article 6.2.1.1(i) would set forth the required account structure for an FCM (which may also be a BD) with respect to any Cleared Swaps, which would include:

- An FCM/BD Swaps Client Trade Account for each Cleared Swaps Customer;
- An FCM/BD Swaps Client Margin Account for each Cleared Swaps Customer;
- An FCM/BD Swaps Client Financial Account for each Cleared Swaps Customer;

- An FCM/BD Swaps Unallocated Client Collateral Financial Account;
- An FCM/BD Swaps Buffer Financial Account; and
- An FCM/BD Swaps Client Collateral Account.

Likewise, Article 6.2.1.1(ii) would set forth the required account structure for a BD (which may also be an FCM) with respect to any SBS (excluding SBS that are permitted to be held in an account with Cleared Swaps), which would include:

- An FCM/BD SBS Client Trade Account for each SBS Customer;⁷
- An FCM/BD SBS Client Margin Account for each SBS Customer;⁸
- An FCM/BD SBS Client Financial Account for each SBS Customer;⁹

⁷ In furtherance of this change, the proposed rule change also would amend Article 6.2.2.1, which relates to the establishment of trade accounts, to require LCH SA to open FCM/BD SBS Client Trade Accounts for SBS Customers.

⁸ In furtherance of this change, the proposed rule change also would amend Article 6.2.3.1, which relates to the establishment of client margin accounts, to require LCH SA to open FCM/BD SBS Client Margin Accounts for SBS Customers. Similarly, the proposed rule change would amend Article 6.2.3.2 to provide that FCM/BD Cleared Transactions (i) registered in an FCM/BD Swaps Client Trade Account for a Cleared Swaps Customer will be allocated to the corresponding FCM/BD Cleared Swaps Client Margin Account and (ii) registered in an FCM/BD SBS Client Trade Account for an SBS Customer will be allocated to the corresponding FCM/BD SBS Client Margin Account, for the purpose of the determination of the Open Positions and NPV Payment Requirements attributable to such FCM/BD Client.

⁹ In furtherance of this change, the proposed rule change also would amend Article 6.2.4.1, which relates to the establishment of Client Financial Accounts and related accounts, to require LCH SA to open FCM/BD SBS Client Financial Accounts for SBS Customers, in which LCH SA will record the value of Collateral provided by the FCM/BD Clearing Member in respect of each such SBS Customer's Open Positions in SBS.

- An FCM/BD SBS Client Excess Collateral Financial Account;¹⁰
- An FCM/BD SBS Buffer Financial Account;¹¹ and
- An FCM/BD SBS Client Collateral Account.¹²

Moreover, the proposed rule change would add a new Article 6.2.1.1(iii) to provide that an FCM/BD Clearing Member that is both an FCM and a BD may elect to clear and hold margin for FCM/BD Cleared Transactions that are SBS for FCM/BD Clients in the FCM/BD Swaps Client Account Structure on a commingled basis with Cleared Swaps, and margin such combined positions on a portfolio basis in compliance with Applicable Laws.¹³ This provision would be subject to the condition that each FCM/BD Client participating in the portfolio margining must be an eligible contract participant as defined in Section 1a(18) of the Commodity Exchange

¹⁰ In furtherance of this change, the proposed rule change also would amend Article 6.2.4.1, which relates to the establishment of Client Financial Accounts and related accounts, to require LCH SA to open an FCM/BD SBS Client Excess Collateral Financial Account for SBS Customers, in which LCH SA will record the value of FCM/BD SBS Client Excess Collateral.

¹¹ In furtherance of this change, the proposed rule change also would amend Article 6.2.4.1, which relates to the establishment of Client Financial Accounts and related accounts, to require LCH SA to open an FCM/BD SBS Buffer Financial Account for SBS Customers, in which LCH SA will record the value of Collateral provided by the FCM/BD Clearing Member as FCM/BD SBS Client Collateral Buffer.

¹² In furtherance of this change, the proposed rule change also would amend Article 6.2.4.1, which relates to the establishment of Client Financial Accounts and related accounts, to require LCH SA to open FCM/BD SBS Client Collateral Accounts for SBS Customers, in which LCH SA will record the value of Collateral held by LCH SA in the other accounts listed in Article 6.2.1.1(ii) (such as the FCM/BD SBS Client Financial Account and FCM/BD SBS Client Excess Collateral Financial Account).

¹³ See Portfolio Margin Order, 77 Fed. Reg. 75211.

Act.¹⁴ Upon such election, FCM/BD Cleared Transactions that are SBS would be included as Cleared Swaps and maintained in the FCM/BD Swaps Client Account Structure.

The proposed rule change also would add a new article regarding the return of excess collateral. Under new Article 6.2.5.2, an FCM/BD Clearing Member is not permitted to maintain any FCM/BD Client Excess Collateral on a day-to-day basis with respect to SBS, but may hold FCM/BD Client Excess Collateral on an intraday basis. LCH SA would be required to transfer the value of any FCM/BD Client Excess Collateral that is reflected in any FCM/BD SBS Client Financial Account of the FCM/BD Clearing Member prior to the Morning Call to the FCM/BD Clearing Member's FCM/BD SBS Client Excess Collateral Financial Account. In addition, new Article 6.2.5.2(iv) would require, among other things, that LCH SA hold FCM/BD SBS Client Excess Collateral in the FCM/BD SBS Client Excess Collateral Financial Account for the benefit of FCM/BD Clearing Member's FCM/BD Clients that are SBS customers as a class in accordance with SEC regulations and Applicable Law and that upon the request of an FCM/BD Clearing Member, LCH SA would return FCM/BD SBS Client Excess Collateral to such FCM/BD Clearing Member.

The proposed rule change also would amend Article 6.2.6.1, which currently requires an FCM Clearing Member to collect collateral from each client in respect of such client's open positions in an amount at least equal to the greater of (i) the amount required by LCH SA for the FCM Client Margin Account for such client or (ii) such higher amount as required in Section 2 of the Procedures. The proposed rule change would amend this Article to apply it to FCM/BD

¹⁴ 7 U.S.C. 1a(18).

Clearing Members and to add a corresponding provision for client open positions in SBS in an amount at least equal to the amount required by LCH SA for the FCM/BD SBS Client Margin Accounts.

Finally, the proposed rule change would make conforming changes throughout Title VI by updating references to Clearing Members to ensure that the articles apply to an FCM/BD Clearing Member instead of just an FCM Clearing Member.

vi. Appendix

Appendix 1 of the Rule Book describes LCH SA's CDS Default Management Process. The proposed rule change would amend the defined term "Transaction Categories," which currently sets out the different categories of transactions that LCH SA clears. The proposed rule change would amend the definition of "Transaction Categories" to include "Single Name Cleared Transactions." This change would help ensure that LCH SA's default management process applies to SBS.

The proposed rule change also would amend Clause 3.3 of Appendix 1, which sets out the applicable U.S. law and regulation that LCH SA would act in accordance with in carrying out the CDS Default Management Process, such as the Exchange Act and SEC regulations. The proposed rule change would add to Clause 3.3 a reference to the new defined term "SIPC" in Section 1.1.1 of the Rule Book, such that LCH SA would act in accordance with SIPC in carrying out the CDS Default Management Process, in addition to the other U.S. laws and regulations currently listed in Clause 3.3. Under the proposed rule change, "SIPC" would be defined as the Securities Investor Protection Corporation or any successor thereto.

The proposed rule change would revise Clause 5.4, which relates to competitive bidding in a default auction. Currently under Clause 5.4, all Non-Defaulting Clearing Members are required to participate in Competitive Bidding for each Auction Package notwithstanding that any Non-Defaulting Clearing Member may not have registered within its Account Structure a Cleared Transaction of the type included in the relevant Transaction Category for an Auction Package, subject to certain exceptions. As proposed to be revised, under Clause 5.4 a Non-Defaulting Clearing Member that is a BD but not an FCM would not be required to participate in Competitive Bidding for an Auction Package containing any Cleared Swaps and a Non-Defaulting Clearing Member that is an FCM but not a BD would not be required to participate in Competitive Bidding for an Auction Package containing any SBS.

The proposed rule change also would make conforming changes throughout Appendix 1 to apply Appendix 1 to an FCM/BD Clearing Member instead of just an FCM Clearing Member. Specifically, references to Clearing Members would be updated to apply them to FCM/BD Clearing Members instead of just FCM Clearing Members.

B. Clearing Supplement

Similar to some of the changes to the Rule Book discussed above, the proposed rule change would make conforming changes to apply the Clearing Supplement to an FCM/BD Clearing Member instead of just an FCM Clearing Member. These changes would update references to Clearing Members to apply them to FCM/BD Clearing Members instead of just FCM Clearing Members.

C. Procedures

The proposed rule change would amend Sections 2, 3, 4, and 5 of the Procedures.

i. Section 2

Similar to the changes to the Rule Book and Clearing Supplement discussed above, in Section 2 of the Procedures, the proposed rule change would make conforming changes to apply Section 2 to an FCM/BD Clearing Member instead of just an FCM Clearing Member. These changes would update references to Clearing Members to apply them to FCM/BD Clearing Members instead of just FCM Clearing Members.

ii. Section 3

Similar to the changes to the Rule Book and Clearing Supplement discussed above, in Section 3 of the Procedures, the proposed rule change would make conforming changes to apply Section 3 to an FCM/BD Clearing Member instead of just an FCM Clearing Member. These changes would update references to Clearing Members to apply them to FCM/BD Clearing Members instead of just FCM Clearing Members.

In addition, the proposed rule change would amend Section 3.3(b), which relates to the Collateral Account structure, to add a reference to the FCM/BD SBS Client Collateral Account. In this account LCH SA would record the Collateral held by LCH SA for the benefit of an FCM/BD Clearing Member's SBS Customers with respect to SBS. The value in this account would be further divided among and recorded in three separate accounts: (i) the FCM/BD SBS Client Financial Account; (ii) the FCM/BD SBS Buffer Financial Account; and (iii) the FCM/BD SBS Client Excess Collateral Financial Account.

The proposed rule change would amend Section 3.7, which relates to collection of Euro denominated cash collateral. As described in Section 3.7(a), LCH SA performs Collateral Calls using TARGET2 Accounts opened in its name. The proposed rule change would amend Section 3.7(a) to provide that LCH SA will perform Collateral Calls with respect to the Clients of a Clearing Member using a TARGET2 Account. As described in the proposed amendment, LCH SA would use this TARGET2 Account to make Collateral Calls in relation to the Client Margin Requirements with respect to SBS (excluding SBS held in the FCM/BD Swaps Client Account Structure) and FCM/BD Client Collateral Buffer Threshold of each FCM/BD Clearing Member.

Similarly, the proposed rule change would amend Section 3.7(b), which relates to the TARGET2 Accounts that a Clearing Member must hold. Section 3.7(b) currently requires that a Clearing Member hold two TARGET2 Accounts, one related to house margin and the other related to client margin. The proposed rule change would add to these two accounts a third account, relating to client margin with respect to SBS. Thus, as revised, Section 3.7(b) would require that an FCM/BD Clearing Member hold three TARGET2 Accounts for purposes of Collateral Calls in respect of (i) its FCM/BD House Margin Requirement and FCM/BD House Excess Collateral Threshold, (ii) its Client Margin Requirements with respect to Cleared Swaps and FCM/BD Client Collateral Buffer Threshold, and (iii) its Client Margin Requirements with respect to SBS (excluding SBS that are held in the FCM/BD Swaps Client Account Structure) and FCM/BD Client Collateral Buffer Threshold.

The proposed rule change next would amend Section 3.7(g), which relates to the return of Euro denominated cash collateral. Currently, Section 3.7(g)(iv) allows a Clearing Member to request LCH SA to return some or all FCM Unallocated Client Excess Collateral in the form of

Euro denominated Cash Collateral provided that the requested amount does not exceed the FCM Unallocated Client Excess Collateral recorded in its Client Collateral Account. The proposed rule change would amend Section 3.7(g)(iv) to clarify that it applies to FCM/BD Clearing Members, not just FCM Clearing Members. The proposed rule change also would add to Section 3.7(g) a new paragraph (v), which would mirror paragraph (iv) of Section 3.7(g) described above, but it would apply to excess collateral related to SBS. Thus, under new Section 3.7(g)(v), a Clearing Member may also request LCH SA to return some or all FCM/BD SBS Client Excess Collateral in the form of Euro denominated Cash Collateral provided that the requested amount does not exceed the FCM/BD SBS Client Excess Collateral recorded in its FCM/BD SBS Client Collateral Account.

The proposed rule change also would amend Section 3.8, which sets out the multi-currency accounts in which LCH SA holds non-Euro Collateral provided by Clearing Members to meet house and client margin requirements. Currently, Section 3.8(a) requires that LCH SA have two multi-currency accounts for holding non-Euro Cash Collateral provided by Clearing Members in respect of their clients. The proposed rule change would add a third account, requiring that LCH SA have, with respect to Clients of a Clearing Member, a multi-currency account used to credit non-Euro, non-USD Cash Collateral which is transferred by an FCM/BD Clearing Member to be recorded in its FCM/BD SBS Client Collateral Account. This account would form part of the LCH SBS Client Segregated Depository Account for purposes of the FCM/BD CDS Clearing Regulations.

Similarly, Section 3.8(b) currently requires that LCH SA have two USD cash accounts for holding USD Cash Collateral provided by Clearing Members in respect of their clients. The

proposed rule change would add a third account, requiring that LCH SA have, with respect to Clients of a Clearing Member, an account used to credit USD Cash Collateral which is transferred by FCM/BD Clearing Members to be recorded in their FCM/BD SBS Client Collateral Account. This account would form part of the LCH SBS Client Segregated Depository Account for purposes of the FCM/BD CDS Clearing Regulations.

With respect to the return of excess collateral, the proposed rule change would amend Section 3.8(h) and (i), to provide for the return of excess collateral in respect of SBS. These amendments would mirror the provisions currently applicable to swaps.

Finally, the proposed rule change would amend Section 3.18, relating to cash payments and variation margin transfers. Currently, Section 3.18(c) lists the accounts that LCH SA uses when making or receiving Cash Payments and/or Variation Margin Collateral Transfer obligations in USD. The proposed rule change would add to this list a cash account used to debit or credit USD to satisfy Cash Payments and/or Variation Margin Collateral Transfer obligations in USD with respect to all relevant Client Cleared Transactions of each FCM/BD Clearing Member that are SBS (excluding SBS that are held in the FCM/BD Swaps Client Account Structure).

iii. Section 4

Section 4 sets out certain requirements that a transaction must satisfy to be eligible for clearing at LCH SA. Currently, Section 4.1 provides that (i) in respect of an FCM Client, a U.S. CCM Client of a Non-U.S. CCM or a CCM Client of a U.S. CCM, the Original Transaction may not be a Single Name CDS or any other SBS identified as such in a Clearing Notice; and (ii) in respect of a Non-U.S. CCM Client, the Original Transaction may not be a Single Name CDS or

any other SBS identified as such in a Clearing Notice unless such transaction is cleared through a Non-U.S. CCM. The proposed rule change would delete Section 4.1, thus permitting Clearing Members to submit SBS to LCH SA for clearing on behalf of U.S. Clients.

iv. Section 5

Section 5 of the Procedures specifies LCH SA's CDS Clearing Operations Procedures and includes numerous references to "FCM Clearing Members." Similar to the changes to the Rule Book and Clearing Supplement discussed above, the proposed rule change would change these references from "FCM Clearing Members" to "FCM/BD Clearing Members." This would help ensure that the Clearing Operations Procedures in Section 5 apply to FCM/BD Clearing Members instead of just FCM Clearing Members.

D. Clearing Regulations

The proposed rule change also would amend LCH SA's CDS Clearing Regulations, which impose certain obligations on LCH SA's Clearing Members and is divided into Regulations 1 through 6, as well as a Definitions section appearing before Regulation 1. The proposed rule change would first update certain of the defined terms found in the Definitions section to reflect some of the changes discussed above. For example, the proposed rule change would amend a number of defined terms to use the term "Cleared Swaps Customer," which, as discussed above, the proposed rule change would add to the Rule Book. The proposed rule change would also add the defined term "LCH SBS Client Segregated Depository Account," which, as discussed above, the proposed rule change would reference in Section 3 of the Procedures.

In Regulation 2 (Depository Accounts), the proposed rule change would set out the relevant account structure for SBS. Under Regulation 2 as revised, each FCM/BD Clearing Member would be required to establish and maintain an FCM/BD SBS Client Segregated Depository Account on behalf of its SBS Customers in accordance with applicable provisions of the Exchange Act and SEC regulations. An FCM/BD Clearing Member would be required to maintain the FCM/BD SBS Client Segregated Depository Account with a Bank in accordance with the Exchange Act and SEC Regulations and the FCM/BD Clearing Member would be allowed to commingle assets of all of its SBS Customers held in that account in a single omnibus account established and maintained in accordance with SEC regulations. LCH SA would designate the FCM/BD SBS Client Segregated Depository Account maintained by each FCM/BD Clearing Member as a “Special Reserve Bank Account for the Exclusive Benefit of the Cleared Security-Based Swap Customers” of the FCM/BD Clearing Member as provided in Exchange Act Rule 15c3-3(p).¹⁵

Similarly, under Regulation 2 as revised, LCH SA would be required to establish and maintain a LCH SBS Client Segregated Depository Account on behalf of the SBS Customers of FCM/BD Clearing Members, in accordance with applicable provisions of the Exchange Act and SEC regulations. LCH SA would be required to maintain the LCH SBS Client Segregated Depository Account with a Bank in accordance with the Exchange Act and SEC regulations and LCH SA would be allowed to commingle assets of all of the SBS Customers in that account in a single omnibus account established and maintained in accordance with SEC regulations.

¹⁵ 17 CFR 240.15c3-3(p).

Regulation 2 would further require that LCH SA hold in the LCH SBS Client Segregated Depository Account all Collateral that is deposited by FCM/BD Clearing Members in connection with SBS cleared on behalf of SBS Customers (other than Collateral provided to satisfy the Contribution Requirement of such FCM/BD Clearing Members). Moreover, Regulation 2 would require that LCH SA maintain the LCH SBS Client Segregated Depository Account separately from any and all assets of the FCM/BD Clearing Members, or any other assets that LCH SA is holding for clients (other than SBS Customers) and that the account contain no assets other than Collateral deposited by FCM/BD Clearing Members in connection with the clearing of SBS on behalf of their SBS Customers. Finally, LCH SA would designate the LCH SBS Client Segregated Depository Account as a “Special Clearing Account for the Exclusive Benefit of the Cleared Security-Based Swaps Customers” of the FCM/BD Clearing Member for purposes of the Exchange Act and SEC Regulations.

The proposed rule change also would update Regulation 3 of the CDS Clearing Regulations (Collateral), to apply to the LCH SBS Client Segregated Depository Account. Under Regulation 3 as revised, securities or cash held in the LCH SBS Client Segregated Depository Account would be subject to a security interest in accordance with Regulation 5 and no collateral deposited in the LCH SBS Client Segregated Depository Account may be applied on or in respect of payment or satisfaction of the FCM/BD Clearing Member’s liabilities to LCH SA.

Similarly, the proposed rule change would update Regulation 4 (Transfer) to apply to BDs, SBS, and SBS Customers. Currently, Regulation 4 requires that, if an FCM Clearing Member is a Defaulting Clearing Member, any action by LCH SA pursuant to the Rule Book (including the CDS Default Management Process) must be taken in compliance with the

Commodity Exchange Act and CFTC regulations and applicable bankruptcy laws regarding the liquidation or transfer of FCM Cleared Transactions carried by an FCM on behalf of its clients. Under Regulation 4 as revised, if an FCM/BD Clearing Member is a Defaulting Clearing Member, any action taken by LCH SA pursuant to the Rule Book (including the CDS Default Management Process) must be taken in compliance with the Commodity Exchange Act and CFTC regulations or the Exchange Act and SEC regulations, as applicable, and applicable bankruptcy laws regarding the liquidation or transfer of Cleared Swaps carried by an FCM on behalf of its clients or SBS carried by a BD on behalf of its SBS Customers. Moreover, under Regulation 4 as revised, to the extent any transfer by an FCM/BD Clearing Member of open contracts between its Proprietary Account and accounts of its FCM/BD Clients, upon an FCM/BD Client default, is permitted pursuant to the Rule Book (including the CDS Default Management Process) and the Procedures, such transfer must be made subject to applicable provisions of the Commodity Exchange Act and CFTC regulations or the Exchange Act and SEC regulations, as applicable, regarding segregation of assets. Currently, this provision only applies to the Commodity Exchange Act and CFTC regulations.

The proposed rule change also would update Regulation 5 of the CDS Clearing Regulations (Security Interest) to apply to BDs, SBS, and SBS Customers. Currently, Regulation 5 provides that each FCM Clearing Member grants LCH SA a first security interest in and a first priority and unencumbered first lien upon any and all cash, securities, receivables, rights and intangibles and any other Collateral or assets deposited with or transferred to LCH SA, or otherwise held by LCH SA, including all property deposited in an LCH Proprietary Depository Account and in an LCH Cleared Swaps Client Segregated Depository Account, as security for

unconditional payment and satisfaction of the obligations and liabilities of the FCM Clearing Member to LCH SA. The proposed rule change would amend this provision so that it applies to FCM/BD Clearing Members and the LCH SBS Client Segregated Depository Account. The proposed rule change also would clarify that in no event shall LCH SA's security interest in the Collateral in an LCH Cleared Swaps Client Segregated Depository Account or an LCH SBS Client Segregated Depository Account held on behalf of the FCM/BD Clearing Member's Clients be exercised to satisfy any obligations or liabilities of such FCM/BD Clearing Member other than in connection with obligations or liabilities relating to Cleared Swaps cleared by such FCM/BD Clearing Member on behalf of its Cleared Swaps Customers or relating to SBS cleared by such FCM/BD Clearing Member on behalf of its SBS Customers. Currently, this provision only applies to LCH Cleared Swaps Client Segregated Depository Account and swaps clients.

Finally, similar to the changes to the Rule Book, Clearing Supplement, and Procedures discussed above, throughout the Clearing Regulations the proposed rule change would make conforming changes to apply the Clearing Regulations to an FCM/BD Clearing Member instead of just an FCM Clearing Member. These changes would update references to Clearing Members to apply them to FCM/BD Clearing Members instead of just FCM Clearing Members, including changing the title of the document to the "FCM/BD CDS Clearing Regulations." The proposed rule change would similarly add references to the Exchange Act when discussing applicable law.

E. Additional Changes Unrelated to U.S. Client Clearing

In addition to the changes discussed above related to U.S. client clearing, the proposed rule change would make certain other changes not directly related to that initiative. First, the proposed rule change would amend Appendix 1 of the Rule Book (CDS Default Management

Process). As discussed above, Appendix 1 of the Rule Book describes LCH SA's CDS Default Management Process. In Clause 5.4.4 (Minimum Bid Size), the amendment would revise the current formula for LCH SA's calculation of the Minimum Bid Size for each Non-Defaulting Clearing Member by incorporating a 100% maximum cap, thus clarifying that a Non-Defaulting Clearing Member would never be required to bid for more than 100% of the relevant Auction Package in a default auction. This proposed change would also be consistent with existing Clause 5.4.6 (Bids in excess of the Minimum Bid Size), which prohibits a Non-Defaulting Clearing Member from submitting Bid(s) whose Bid Size(s), alone or in aggregate, exceed 100% of the relevant Auction Package. The proposed rule change also would revise Clause 5.9.1 for LCH SA's recalculation of Minimum Bid Sizes for Residual Auction Packages in a potential second round of Competitive Bidding. Under existing Clause 5.9.1(i), LCH SA will reduce a Non-Defaulting Clearing Member's original Minimum Bid Size as calculated in Clause 5.4.4 by an amount equal to the Bid Credit, which is the percentage difference between the Minimum Bid Size and the percentage of the aggregate of the Bid Sizes of the Non-Defaulting Member's Initial Winning Bids. The proposed rule change would provide that such recalculation is "subject to the maximum value for the Bid Credit of the Minimum Bid Size."

In Clause 8.1.1 of Appendix 1 of the Rule Book, the proposed rule change would remove a reference to the Early Termination Trigger Date at the end of the paragraph. Currently, that paragraph provides that upon an Early Termination Trigger Date, other payment and delivery obligations in relation to any Cleared Transactions and any other obligations pursuant to the CDS Clearing Documentation (including Collateral registered in any Collateral Accounts and other Collateral representing a Clearing Member's Contribution Requirement) shall be payable or

deliverable on the Early Termination Trigger Date and in accordance with the provisions of Clause 8.1.1. The proposed rule change would retain this language but delete the reference to the Early Termination Trigger Date at the end of the paragraph such that the obligations shall be payable or deliverable in accordance with the provisions of Clause 8.1.1, rather than on the Early Termination Trigger Date and in accordance with the provisions of Clause 8.1.1. This change would help to ensure consistency in the operation of the Early Termination process since all payment and delivery obligations in the context of the Early Termination process would be made at the date and times as set out in the provisions of Clause 8.1.1. Thus, this change would remove a potential inconsistency between the Early Termination Trigger Date and the provisions of Clause 8.1.1.

Finally, the proposed rule change would amend Regulation 6 of the Clearing Regulations to implement CFTC Letter No. 19-17.¹⁶ Under CFTC Letter No. 19-17, a Derivatives Clearing Organization may permit a Futures Commission Merchant to treat the separate accounts of a customer as accounts of separate entities subject to a number of conditions provided for in that letter. Therefore, the proposed rule change would amend Regulation 6(e) to allow Clearing Members to benefit from this no-action relief regarding the withdrawal of the Cleared Swaps Customer funds by providing that references to “Cleared Swaps Customer” shall include all Cleared Swaps Customers for the same beneficial owner, unless the Clearing Member complies with the relevant conditions set out in CFTC Letter No. 19-17.

¹⁶ CFTC Letter No 19-17 of July 10, 2019 (“Advisory and Time-Limited No-Action Relief with Respect to the Treatment of Separate Accounts by Futures Commission Merchants”).

III. Discussion and Commission Findings

Section 19(b)(2)(C) of the Act directs the Commission to approve a proposed rule change of a self-regulatory organization if it finds that such proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to such organization.¹⁷ For the reasons given below, the Commission finds that the proposed rule change is consistent with Section 17A(b)(3)(F) of the Act¹⁸ and Rules 17Ad-22(e)(1) and (e)(18).¹⁹

A. Consistency with Section 17A(b)(3)(F) of the Act

Section 17A(b)(3)(F) of the Act requires, among other things, that the rules of LCH SA be designed to promote the prompt and accurate clearance and settlement of securities transactions and, to the extent applicable, derivative agreements, contracts, and transactions, as well as to assure the safeguarding of securities and funds which are in the custody or control of LCH SA or for which it is responsible.²⁰ As discussed in more detail below, the Commission finds that the proposed rule change is consistent with Section 17A(b)(3)(F) of the Act.²¹

As described above, the proposed rule change would make a number of changes to the Rule Book, Clearing Supplement, Procedures, and Clearing Regulations to permit LCH SA's Clearing Members to offer client clearing services in respect of SBS to U.S. clients. Specifically,

¹⁷ 15 U.S.C. 78s(b)(2)(C).

¹⁸ 15 U.S.C. 78q-1(b)(3)(F).

¹⁹ 17 CFR 240.17Ad-22(e)(1), (e)(18).

²⁰ 15 U.S.C. 78q-1(b)(3)(F).

²¹ 15 U.S.C. 78q-1(b)(3)(F).

as discussed in Part II.A, the proposed rule change would amend the Rule Book to (i) add and update defined terms; (ii) modify the membership requirements applicable to Clearing Members; (iii) remove provisions that prohibit Clearing Members from offering clearing services to U.S. clients with respect to SBS; (iv) permit broker-dealers to become Clearing Members and update provisions to apply them to Clearing Members that are broker-dealers; (v) establish the account structure for Clearing Members clearing SBS on behalf of U.S. clients, including the treatment of collateral posted by Clearing Members in respect of client positions in SBS; and (vi) amend the Appendix to apply relevant provisions of the CDS Default Management Process to SBS. The Commission believes these changes would facilitate clearing of SBS for U.S. clients by establishing the legal and operational framework for Clearing Members to clear SBS on behalf of U.S. clients, thereby promoting the prompt and accurate clearance and settlement of securities transactions by such clients at LCH SA. Similarly, the changes with respect to collateral posted by Clearing Members in respect of client positions in SBS would help to ensure that such collateral is subject to the provisions of LCH SA's Rule Book regarding the protection of collateral, including the return of excess collateral, thereby helping to assure the safeguarding of securities and funds in LCH SA's custody and control. Because the changes to the Clearing Supplement discussed in Part II.B above would further these changes to the Rule Book by making conforming changes to apply the Clearing Supplement to an FCM/BD Clearing Member instead of just an FCM Clearing Member, the Commission believes the changes to the Clearing Supplement also would promote the prompt and accurate clearance and settlement of securities transactions and assure the safeguarding of securities and funds in LCH SA's custody and control.

As discussed in Part II.C, the proposed changes to the Procedures would (i) make conforming changes to apply them to an FCM/BD Clearing Member instead of just an FCM Clearing Member; (ii) require that LCH SA and Clearing Members establish and use certain accounts to hold and transfer cash and other collateral for satisfying margin requirements in connection with client positions in SBS; (iii) establish procedures for the return of excess collateral related to client positions in SBS; and (iv) remove provisions that currently prohibit LCH SA from accepting SBS transactions in respect of U.S. clients. Like the changes to the Rule Book and Clearing Supplement, the Commission believes these changes would facilitate clearing of SBS for U.S. clients by establishing the financial accounts and operational framework needed for clearing client positions in SBS and removing provisions that currently prohibit LCH SA from accepting SBS transactions in respect of U.S. clients, thereby promoting the prompt and accurate clearance and settlement of those securities transactions at LCH SA. Moreover, in requiring the establishment and use of certain accounts to hold and transfer cash and other collateral for satisfying margin requirements, and in establishing procedures for the return of excess collateral related to client positions in SBS, these proposed changes would help to assure the safeguarding of securities and funds in LCH SA's custody and control.

For similar reasons, the Commission finds the proposed changes to the Clearing Regulations also are consistent with Section 17A(b)(3)(F) of the Act.²² Requiring that Clearing Members and LCH SA establish accounts with a Bank for holding collateral on behalf of SBS Customers and requiring that the accounts be maintained separately from any and all assets of

²² 15 U.S.C. 78q-1(b)(3)(F).

the FCM/BD Clearing Members, or any other assets that LCH SA is holding for clients (other than SBS Customers), should promote the safekeeping of SBS Customers' collateral, thereby assuring safeguarding of securities and funds in LCH SA's custody and control. Similarly, in amending Regulation 3 and Regulation 5 to clarify that the security interest granted to LCH SA applies to FCM/BD Clearing Members and the LCH SBS Client Segregated Depository Account and that no collateral deposited in the LCH SBS Client Segregated Depository Account may be applied on or in respect of payment or satisfaction of any of the FCM/BD Clearing Member's liabilities to LCH SA, the Commission believes the proposed rule change should help to assure that SBS Customers' collateral is not misapplied to satisfy a Clearing Member's liabilities, again assuring the safeguarding of securities and funds in LCH SA's custody and control. Moreover, amending Regulation 4 to require that any action by LCH SA pursuant to the Rule Book (including the CDS Default Management Process) be taken in compliance with the Exchange Act and SEC regulations as well as applicable bankruptcy laws regarding the liquidation or transfer of SBS carried by a BD on behalf of its clients, should help to assure the safekeeping of SBS Customers' collateral after the default of a Clearing Member. Finally, making conforming changes to apply the Clearing Regulations to an FCM/BD Clearing Member instead of just an FCM Clearing Member should help to assure the applicability of these provisions to SBS.

Finally, the Commission finds the other changes unrelated to U.S. client clearing, discussed in Part II.E above, are also consistent with Section 17A(b)(3)(F) of the Act.²³ Amending Appendix 1 of the Rule Book to provide that each Non-Defaulting Clearing Member

²³ 15 U.S.C. 78q-1(b)(3)(F).

would never be required to bid for more than 100% of the relevant Auction Package and to remove a reference to the Early Termination Trigger Date at the end of the paragraph would correct existing drafting errors in clauses pertaining to the CDS Default Management Process. Correcting these errors should help to ensure that the CDS Default Management Process is applied consistently and correctly, thereby helping to ensure a smooth resolution of Clearing Member defaults. This in turn should help to ensure that LCH SA continues to operate as normal after a Clearing Member default, and thus should promote the prompt and accurate clearance and settlement of transactions. Moreover, in amending Regulation 6 of the Clearing Regulations to implement CFTC Letter No. 19-17, the proposed rule change should allow LCH SA's Clearing Members that are FCMs to take advantage of that relief, thereby promoting the use of LCH SA's clearing services among such members and the prompt and accurate clearance and settlement of derivative transactions.

Therefore, for the reasons discussed above, the Commission finds that the proposed rule change is consistent with the Section 17A(b)(3)(F) of the Act.²⁴

B. Consistency with Rule 17Ad-22(e)(1)

Rule 17Ad-22(e)(1) requires that LCH SA establish, implement, maintain and enforce written policies and procedures reasonably designed to provide for a well-founded, clear, transparent, and enforceable legal basis for each aspect of its activities in all relevant jurisdictions.²⁵ The Commission believes the changes discussed above permitting LCH SA's

²⁴ 15 U.S.C. 78q-1(b)(3)(F).

²⁵ 17 CFR 240.17Ad-22(e)(1).

Clearing Members to submit for clearing SBS on behalf of their U.S. clients would establish a well-founded, clear, transparent, and enforceable legal basis for such client clearing services. In particular, removing current provisions from the Rule Book that prohibit Clearing Members from offering clearing services to U.S. clients with respect to SBS and removing provisions from the Procedures that prohibit LCH SA from accepting SBS transactions in respect of U.S. clients, would help ensure that the legal basis for providing clearing to U.S. clients with respect to SBS is well-founded. Establishing the account structure to be used by Clearing Members clearing SBS on behalf of U.S. clients and requiring that Clearing Members and LCH SA establish accounts for holding and transferring cash and other collateral on behalf of SBS Customers likewise would help ensure that the methods for holding and transferring such collateral are clear and transparent. Amending Appendix 1 of the Rule Book to apply the CDS Default Management Process to SBS would help to ensure the enforceability of the CDS Default Management Process with respect to SBS, while amending Regulation 3 and Regulation 5 of the Clearing Regulations to clarify that the security interest granted to LCH SA applies to FCM/BD Clearing Members and the LCH SBS Client Segregated Depository Account, and that no collateral deposited in the LCH SBS Client Segregated Depository Account may be applied on or in respect of payment or satisfaction of any of the FCM/BD Clearing Member's liabilities to LCH SA, would help to ensure the enforceability of LCH SA's security interest while protecting SBS customer collateral. Finally, amending defined terms and provisions throughout the Rule Book, Clearing Supplement, Procedures, and Clearing Regulations to clarify that they apply to BDs and SBS would help to ensure that the legal bases for applying these provisions to BDs and SBS are similarly well-founded and clear.

The Commission believes that the other changes unrelated to U.S. client clearing, as discussed in Part II.E above, would similarly help to ensure that the legal basis for LCH SA's activities is well-founded and clear. Amending Appendix 1 of the Rule Book to provide that each Non-Defaulting Clearing Member would never be required to bid for more than 100% of the relevant Auction Package and to remove a reference to the Early Termination Trigger Date at the end of the paragraph would correct drafting errors in clauses pertaining to the CDS Default Management Process, thereby helping to ensure the clarity of the CDS Default Management Process. Amending Regulation 6 of the Clearing Regulations to implement CFTC Letter No. 19-17 should help clarify the ability of Clearing Members that are FCMs to rely on the provisions of such letter.

Thus, the Commission finds that these aspects of the proposed rule change are consistent with Rule 17Ad-22(e)(1).²⁶

C. Consistency with Rule 17Ad-22(e)(18)

Rule 17Ad-22(e)(18) requires that LCH SA establish, implement, maintain and enforce written policies and procedures reasonably designed to establish objective, risk-based, and publicly disclosed criteria for participation, which permit fair and open access by direct and, where relevant, indirect participants and other financial market utilities, require participants to have sufficient financial resources and robust operational capacity to meet obligations arising from participation in the clearing agency, and monitor compliance with such participation

²⁶ 17 CFR 240.17Ad-22(e)(1).

requirements on an ongoing basis.²⁷ As discussed above, as part of the proposed changes permitting LCH SA's Clearing Members to submit for clearing SBS on behalf of their U.S. clients, the proposed rule change would impose certain requirements on Clearing Members who wish to offer clearing to U.S. clients. Among other things, Clearing Members would be required to establish accounts for holding and transferring cash and other collateral on behalf of SBS Customers and would be prohibited from offering clearing services to any U.S. Client, other than an affiliate of the clearing member, with respect to swaps and SBS, unless the Clearing Member (i) is an FCM or BD and (ii) has provided LCH SA with an opinion of counsel confirming that the provision of clearing services would not be contrary to applicable law. The Commission believes these changes would establish objective, risk-based, and publicly disclosed criteria for participation by LCH SA's Clearing Members in client clearing for U.S. clients, which should permit fair and open access by Clearing Members directly and U.S. clients indirectly.

Thus, the Commission finds that these aspects of the proposed rule change are consistent with Rule 17Ad-22(e)(18).²⁸

²⁷ 17 CFR 240.17Ad-22(e)(18).

²⁸ 17 CFR 240.17Ad-22(e)(18).

IV. Conclusion

On the basis of the foregoing, the Commission finds that the proposed rule change is consistent with the requirements of the Act, and in particular, with the requirements of Section 17A(b)(3)(F) of the Act²⁹ and Rules 17Ad-22(e)(1) and (e)(18).³⁰

IT IS THEREFORE ORDERED pursuant to Section 19(b)(2) of the Act³¹ that the proposed rule change (SR-LCH SA-2021-001), be, and hereby is, approved.³²

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.³³

J. Matthew DeLesDernier
Assistant Secretary

²⁹ 15 U.S.C. 78q-1(b)(3)(F).

³⁰ 17 CFR 240.17Ad-22(e)(1), (e)(18).

³¹ 15 U.S.C. 78s(b)(2).

³² In approving the proposed rule change, the Commission considered the proposal's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

³³ 17 CFR 200.30-3(a)(12).