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July 17, 2023

VIA ELECTRONIC TRANSMISSION
rule-comments@sec.gov

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

Re: Covered Clearing Agency Resilience and Recovery and Wind-Down Plans (Release No. 34-97516; File Number S7-10-23)

Dear Ms. Countryman:

The Depository Trust & Clearing Corporation ("DTCC"), together with its registered clearing agency subsidiaries, The Depository Trust Company ("DTC"), Fixed Income Clearing Corporation ("FICC"), and National Securities Clearing Corporation ("NSCC"), appreciate the opportunity to provide comments to the U.S. Securities and Exchange Commission ("Commission") regarding proposed amendments and new rules for registered clearing agency resilience and recovery and wind-down plans ("Proposal").[1] Given the critical role registered clearing agencies play for the U.S. securities markets and financial markets more broadly, DTCC appreciates the importance of promoting strong risk management practices and maintaining effective recovery and orderly wind-down plans ("RWP") for such entities.

Introduction

DTCC's common stock is owned by the financial institutions that are participants of its registered clearing agency subsidiaries: DTC, FICC, and NSCC (collectively, the "Clearing Agencies"). NSCC and FICC provide central counterparty ("CCP") services for multiple asset classes, including U.S. equities, corporate and municipal bonds, and government and mortgage-backed securities. The Government Securities Division of FICC is the leading provider of trade comparison, netting and settlement for the U.S. Government securities marketplace. The other division of FICC is the Mortgage-Backed Securities Division, which provides CCP services for mortgage-backed securities, including To-Be-Announced securities. NSCC provides clearing, settlement, risk management, and CCP services for trades involving equities, corporate and municipal debt, exchange-traded funds, and unit investment trusts in the U.S. As a central securities depository, DTC provides settlement services for virtually all equity, corporate and municipal debt trades, and money market instruments in the U.S. Each of these registered Clearing Agencies has been designated as a systemically important financial market utility ("SIFMU") by the U.S. Financial Stability Oversight Council pursuant to Title VIII of the Dodd-Frank Wall Street

[1] See proposed Securities Exchange Act Release No. 34-97516; File No. S7-10-23 (May 17, 2023), available at https://www.sec.gov/rules/proposed/2023/34-97516.pdf ("Proposing Release").

Reform and Consumer Protection Act of 2010.[2] In addition, each of these Clearing Agencies is a covered clearing agency ("CCA") that maintains RWPs pursuant to Commission regulations.[3]

All participant owners of DTCC's registered Clearing Agencies commit capital as owners, pay fees for services and ultimately benefit from the safeguards, efficiencies, and risk mitigation that the Clearing Agencies provide. This ownership model effectively aligns interests among users, owners, the board of directors and management, while fostering capital efficiency and delivering cost-effective operating and processing solutions.

Executive Summary

Overall, DTCC is broadly supportive of the Proposal, which builds upon certain aspects of CCAs' margin systems and specifies certain elements that CCAs should include in their RWPs. As a threshold matter, DTCC believes that its CCAs currently employ many practices that already align with those in the Proposal. At the same time, there are instances where we find that the Proposal either goes too far in prescribing certain processes or outcomes a CCA must realize to observe the new requirements (such as in our discussion of the requirements around intraday margin collection and pricing vendor substitution), or falls short in explaining how a particular concept or standard must be followed (such when a CCA reaches a state of considering initiating its RWP). Therefore, our letter offers recommendations around ways the Commission can provide additional clarity for these particular aspects of the Proposal. As a more significant comment to the Proposal, we also raise concerns regarding the Proposal's conception of "service providers" and offer our views regarding how the Commission should consider this topic more holistically across the various clearing agency proposals issued in the last twelve months.[4]

DTCC continues to stress, as it has in prior comment letters to the Commission, that CCAs must be afforded the discretion and flexibility to interpret and implement rules based on the risk profiles, markets, and products that respective CCAs serve. Aspects from the Proposal that would benefit from this discretion include intraday monitoring and margin collections; the scope of participation of participants and third parties in the annual RWP testing; and the proposed requirement to include contractual terms and conditions that would prevent automatic termination by service providers in the event of a recovery or orderly wind-down.

As indicated above, DTCC also has concerns regarding certain proposed defined terms set forth in the Proposal. For example, we believe that clarification is needed for the proposed definition of "orderly wind-down" to make clear that, notwithstanding a CCA's good faith efforts in preparing its RWP to avoid doing so, CCAs cannot guarantee that their orderly wind-down will not cause contagion within the financial system or that the stability of the U.S. financial system will not be impacted. In addition, and with reference to 17Ad-22(e)(6)(iv), we request clarification of the term "substantive" as it

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[2] The Clearing Agencies are registered clearing agencies under the Securities Exchanges Act of 1934, as amended, and, as such, are supervised by the Commission.

[3] See 17 CFR 240.17Ad-22(e); Release Nos. 34-78961 (Sept. 28, 2016), 81 FR 70785 (Oct. 13, 2016); 34-88616 (Apr. 9, 2020) 85 FR 28853 (May 14, 2020).

[4] We note that our discussion of the Proposal's approach to service providers makes specific reference to how the Commission has approached this same concept in its recent proposals about clearing agency governance (Securities Exchange Act Release No. 95431 (August 8, 2022), 87 FR 51812 (August 23, 2022) (S7-21-22)) (the "CA Governance Proposal"), amendments to Regulation Systems Compliance and Integrity (Securities and Exchange Act Release No. 34-97143 (March 15, 2023), 88 FR 23146 (April 14, 2023) (S7-07-23)) (the "Regulation SCI Proposed Amendments"), and Rule 10 (Securities and Exchange Act Release No. 34-97142 (March 15, 2023), 88 FR 20212 (April 5, 2023) (S7-06-23)) (the "Rule 10 Proposal"). We respectfully request that the Commission consider the relevant discussion in this comment letter as a comment of equal applicability to those proposals.

relates to any inputs used by a CCA that are necessary for the risk-based system. Specifically, we request that the determination of what is considered to be "necessary" for the risk-based system to calculate margin and which inputs it deems are not "consequential" be determined by the CCA. We also offer a recommendation that the Commission provide a CCA with the necessary discretion to establish when it is considering initiating a recovery or orderly wind-down, and include in its RWP the means of communication to be used to inform the Commission.

We also have specific comments and concerns around how the Proposal defines and applies the concept of a "service provider" in the context of an RWP, as well as how that defined term and overall concept interacts with similar terms and the same concept across recent Commission and other relevant regulatory agencies' proposed and final rules. Specific points of emphasis include clarifying the scope and definition of a "service provider." In addition, we seek to demonstrate in the discussion below that this is a term that has been utilized by the Commission in multiple clearing agency rulemakings with varying scopes and definitions. In looking holistically across all of these different, but closely linked, proposals, we are concerned that the Commission is taking an overly fragmented approach that will inevitably lead to confusion, redundancy, and overcomplexity in its overall regulatory regime for clearing agencies.

Discussion

A. **Proposed Amendments to Rule 17Ad-22(e)(6)(ii) and (iv)**

1. *DTCC recognizes the critical importance of the margin requirements set forth in Exchange Act Rule 17Ad-22(e)(6). With respect to the proposed amendments to Rule 17Ad-22(e)(6)(ii), we believe that it is important for the Commission to continue to allow CCAs the appropriate flexibility to balance the requirement to monitor intraday exposures with the CCAs' discretion to determine the frequency of margin collection.*

The Proposal calls for amendments to Rule 17Ad-22(e)(6)(ii) (Intraday Monitoring and Margin Calls) that will require CCAs to monitor intraday exposures on an ongoing basis. The Commission specifically states that it is not prescribing a particular time period or frequency for monitoring, and acknowledges that CCAs should have flexibility regarding monitoring frequency. DTCC agrees with the Commission that regular intraday monitoring is an important tool for monitoring credit exposure to participants and allows for effective usage of intraday margin calls. While ongoing monitoring and the operational ability to make intraday margin calls is important, DTCC continues to believe that flexibility is necessary with regards to not only monitoring of intraday exposures, but also to CCA determinations as to the frequency of collection of margin outside of normally scheduled margin calls. In this regard, we believe that such a position is consistent with the Proposal's discussion of the term "ongoing".

Our view above is reinforced by our reading of the Proposal's description[5] of how NSCC tracks intra-day market price and position changes at 15-minute intervals. Further, NSCC retains the authority to impose intra-day mark-to-market charges. Generally, NSCC elects to collect additional margin if the difference between the most recent mark-to-market price of the participant's net positions and the most recent observed market price exceed thresholds established in NSCC's policies and procedures. However, in these circumstances and pursuant to current procedures, NSCC maintains pre-established thresholds amounts, giving NSCC the ability to process margin calls based on numerous factors, such as

[5] See Proposing Release at page 85.

elevated volatility across the market or persistent exposure for any participant during normal market conditions.

In considering this aspect of the Proposal, we wish to stress that it remains imperative for CCAs to retain in any final Commission requirement, the discretion and flexibility to determine whether additional intraday margin calls are in fact needed based on the totality of all circumstances the CCA may consider relevant and appropriate, and not simply based on whether specified risk thresholds have been breached or where the markets served, or products cleared display elevated volatility. This is because even where a risk threshold may have been breached by a participant, this factor alone may not necessitate the collection of additional margin. Instead, actual collection triggers are based on various factors, such as persistent exposure to a participant during normal market conditions, general market conditions, and any possible procyclical effects a margin collection may trigger. It is for these reasons that NSCC has retained flexible and multi-faceted discretion in determining whether a margin call is warranted and if so, when.

2. *DTCC disagrees with the Commission's proposal requiring CCAs to use alternate data sources or alternate risk-based margin systems in the event their primary pricing data sources or other substantive inputs to its margin system are not available or are unreliable. As an alternative to this overly prescriptive aspect of the Proposal, DTCC recommends that CCAs be allowed to implement reasonably designed policies and procedures that provide CCAs with more flexibility in developing and implementing back-up procedures. Such policies and procedures could include, depending on such factors as the relevant cleared product and market structure, a variety of contingencies determined by the CCA.*

The Commission has proposed amendments to Rule 17Ad-22(e)(6)(iv) (Alternative Data Sources) that would require, with respect to both price data and other substantive inputs, that CCAs' procedures address circumstances in which price data or substantive inputs are not readily available or reliable.[6] Specifically, the Commission proposes to require that such procedures include the use of price data or substantive inputs from an alternate source or use of an alternate risk-based system that does not rely on the same unavailable or unreliable information.[7] However, as we demonstrate below, the retention of a secondary source of price information or maintenance of an alternate system vendor is not always the most practical or effective means for CCAs to ensure that they are able to meet their obligations under Rule 17Ad-22(e). Rather, CCAs should have the flexibility to develop reasonable back-up procedures and contingency plans for these types of circumstances, which will depend on the cleared products and market structure at issue, and may not in all cases include the use of third-party secondary vendors or data sources.

As a practical matter, use of a secondary third-party source of pricing data is not available in all circumstances. Based on DTCC's experience and industry observations, there has been a considerable amount of consolidation among securities pricing data providers over the past few years.[8] This has made it even more challenging to retain multiple vendors for each of the asset classes in which the Clearing

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[6] See Proposing Release at page 25.

[7] Supra note 1, page 27-28.

[8] Some recent examples of industry consolidation include S&P's pricing business being acquired by ICE (formerly Interactive Data pricing) in 2016, and Markit Partners being merged with S&P in 2020, effectively eliminating two pricing vendors. See: https://www.businesswire.com/news/home/20161004005472/en/Intercontinental-Exchange-Completes-Acquisition-of-SP-Global%E2%80%99s-Standard-and-Poor%E2%80%99s-Securities-Evaluations-and-Credit-Market-Analysis; https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/s-p-global-ihs-markit-merger-2020-s-largest-deal-shows-value-of-financial-data-61516189.

Agencies require coverage, which includes almost every cash and bond trade effected in the U.S. and Canadian markets. Although the DTCC CCAs maintain relationships with more than one pricing vendor for the majority of their products, this may not be the case in all circumstances. In addition, there can be instances where the Clearing Agencies may find it more effective to use the inputs provided by one pricing vendor for certain cleared products to other, albeit similar products, as opposed to contracting with multiple vendors across multiple products. Finally, and as set forth in the recent updates to the Clearing Agencies' Securities Valuation Framework,[9] certain updates were made to reflect that backup pricing more accurately may be sourced from an alternative pricing vendor, where applicable, or may also be determined, in the absence of an alternative pricing vendor, pursuant to the CCA' applicable policies and procedures to ensure that timely pricing data is applied. Such procedures include, for example, that with respect to end-of-day and intraday pricing, if pricing vendor data is unavailable, unreliable, or otherwise unusable for a CUSIP, the last available price would be recorded in the CCAs' pricing database, which price is consumable to applicable participants. Therefore, rather than mandating as a sole means of contingency the use of alternate providers, we suggest that the Commission adopt the practical approach described immediately above, which provides CCAs with discretion to determine a variety of approaches to how best to address vendor issues, whether for pricing data or other substantive inputs to its margin systems.

Finally, we note that the proposed amendment to Rule 17Ad-22(e)(6)(iv) would require a CCA to address circumstances and develop procedures addressing the use of substantive third-party inputs in their margin calculation processes.[10] In considering this aspect of the Proposal, DTCC recommends that the term "substantive" as used in this context be further refined so as to avoid confusion over the difference between inputs that are "necessary" and those that are "non-consequential." To avoid this risk, we believe that the term "substantive", as it relates to inputs used by the CCA for a risk-based system, should be based solely upon the respective CCA's expert determination of what it considers to be "necessary" for the risk-based system to calculate margin, and which inputs it deems are "non-consequential."

B. <u>Proposed Rule 17Ad-26</u>

1. *The current drafting of the requirements of Proposed Rule 17Ad-26(a)(2) and the related definition of "Service Providers" in Proposed Rule 17Ad-26(b) is circular in nature, and is overly broad, and as a result it embraces numerous service providers that are not necessary to the critical services provided by the Clearing Agencies. This outcome results in many of the Proposal's service requirements being overly burdensome, particularly in the case of the requirement to map service providers.*

As a threshold observation, DTCC notes that the language used in the definition of a "Service Provider" that includes, "...in any way related to the provision of critical services, as identified by the covered clearing agency in 17 CFR 240.17ad-26(a)(1)" [11] is superfluous and unnecessary as the language of Proposed Rule 17 Ad-26(a)(2) specifically references services, "...upon which the covered clearing agency relies to provide the services identified in paragraph (a)(1) of this section." As both the definition and the proposed rule itself refer to the critical services of section (a)(1)[12], both are not needed.

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[9] See Securities Exchange Act Release Nos. 97284 (April 11, 2023), (SR-DTC-2023-003); 97283 (April 11, 2023), (SR-FICC-2023-004), and 97280 (April 11, 2023), (SR-NSCC-2023-003).
[10] See Proposing Release at page 25.
[11] See Proposing Release at page 130.
[12] See Proposing Release at page 127.

DTCC agrees with the Commission that in a recovery or orderly wind-down plan, the continued performance of a service provider would remain essential.[13] However, as currently drafted, the definition of a "service provider", and the language "...upon which the covered clearing agency relies..." in (a)(2), are too broad and would capture large numbers of service providers to DTCC that are not immediately necessary to the ongoing operations of the critical services of DTCC's CCAs. We believe that this would result in a significant burden upon our CCAs (and likely other CCAs) with minimal benefit to the development of effective RWPs.

As currently proposed, the definition of a service provider in Proposed Rule 17Ad-26(a)(2) (Identification of Service Providers) is "any person, including an affiliate or a third-party, that is contractually obligated to the CCA *in any way related* to the provision of critical services" (emphasis added).[14] The Proposal then goes on to require that the CCA identify any service providers upon which the CCA relies to provide the critical services identified in its RWP and specify what services the identified service providers provide to which critical services of the CCA. By including the term "in any way" as well as "relies" in these two sections, the Commission has broadened the scope of a service provider in this Proposal, to a point that renders the term functionally useless in identifying the nexus and necessity of these service providers to the critical business operations of a CCA.

By way of example, there are numerous service providers that are in some way related to the provision of critical services by the clearing agencies but would not result in the inability of the Clearing Agencies to perform their critical services in the event of a recovery or orderly wind-down. Just a few examples of these would be internet service providers or security services at DTCC facilities. Despite the fact that these services are related *in some way* to, and that DTCC *relies* on these for the provision of, critical services identified under the RWPs, these service providers are clearly not necessary to be identified and mapped to the critical services included in the RWPs.

Given the broad scope of the Commission's definition and usage of the term "service providers", as discussed above, the level of services that must be mapped to a CCA's critical services can be massive and a significant burden for CCAs. This is because CCAs would be forced to spend significant resources reviewing all services to determine which are in any way related to, or relied upon for the provision of critical services, and then mapping these services procured to the critical services provided by CCAs. To ensure that the purpose of the proposed rule is best served, DTCC requests that the Commission clarify that CCAs will only be required to map service providers to a CCAs' critical services in the RWP if the service provider directly supports and is necessary to the performance of the critical service.

2. *The definition of "service provider" has become an expanding and increasingly confusing policy concept across multiple varying Commission proposals relating to clearing agencies, and we believe that it is imperative for the Commission to resolve the ambiguities and variances of this concept across the different proposals so that clearing agencies may, for the purposes of RWPs and otherwise, appropriately focus on critical third-party relationships. (Responsive to questions 18 and 20 of the Proposal.)*

DTCC believes that the Commission's use of multiple terms in the various recently proposed rulemakings (including this Proposal, the CA Governance Proposal[15], the Regulation SCI Proposed

[13] See Proposing Release at page 45.
[14] See Proposing Release at page 130.
[15] https://www.sec.gov/rules/proposed/2022/34-95431.pdf

Amendments[16], and the Rule 10 Proposal[17]) to describe the same service provider risk concepts will undermine the ability of clearing agencies to understand and implement each of the interrelated proposed requirements in a manner that supports effective risk management and resilience. To this end, in lieu of establishing different variations of the same concept across disparate rulemakings and thereby creating regulatory uncertainty, DTCC recommends that the Commission (1) choose either "service provider" or "third-party provider" as the defined term; (2) provide a streamlined and baseline definition of the chosen term; (3) provide a clear definition of what it would mean to be a "critical" provider; and (4) apply this tiered definitional structure to the services or systems, as appropriate, in the aforementioned rulemakings.

With respect to the baseline definition of a "service provider" or "third-party provider", DTCC believes that the definition we submitted to the Commission for consideration in our CA Governance Proposal comment letter to be appropriate across the various aforementioned rulemakings. We propose the following definition: "any mutual understanding or agreement between a registered clearing agency and third-party entity by which the third-party entity is required or commits to provide ongoing goods or services to the [registered or covered, as appropriate] clearing agency pursuant to a written contract." These third-party entities can be external, or they can be affiliates.[18] Importantly, we believe explicitly acknowledging the existence of a written contract would address instances where the third-party may pose a risk to the clearing agency but there is no mutuality by which the clearing agency may exercise any control over the third-party and its actions. It is also the written contract that provides the clearing agency with the legal authority to direct the third-party to comply with third-party risk management lifecycle practices as well as processes and procedures established under the recovery and orderly wind-down plans. Further, the written contract would make clear that local police, fire, and other municipal services are explicitly out of scope. The proposed definition of service provider should also include an "ongoing basis" element. Without this element, a one-time receipt of a good or a one-time service may be included within the scope of the any of the aforementioned Commission rulemakings that implicate service provider obligations, and trigger application of the full risk management lifecycle in the same way that a recurring arrangement does. The "ongoing basis" element also works in the RWP context, as the recovery or orderly wind-down plans are designed to ensure the continuation of existing critical payment, clearing, or settlement services through the recovery or orderly wind-down.

With respect to establishing a clear and appropriate definition for "critical" providers, we build on our recommendation from the CA Governance Proposal letter[19], and recommend that the Commission define a "critical" provider as a service provider that is fundamental to the delivery of in-scope services with no readily available substitutes. DTCC believes that the underlined elements are important thresholds to set for "critical" providers. The availability of substitutes is self-explanatory. Additionally, there can be a number of ancillary service providers that are not essential to the delivery of critical services or systems (i.e., nice-to-haves; bells and whistles for a given clearing and settlement service).

By the same logic, DTCC believes the same tiered definitions of "service provider" and "critical service provider" applicable to the Proposal and the CA Governance Proposal can also be used for purposes of Regulation SCI and Rule 10. DTCC recognizes that the Regulation SCI and Rule 10 requirements apply at a "systems" level, which, from DTCC's perspective, would generally be a level more granular than a clearing agency's "services." In other words, the services that a clearing agency provides in support of core market functions (such as clearing and settlement) are generally built and run

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[16] https://www.sec.gov/rules/proposed/2023/34-97143.pdf

[17] https://www.sec.gov/rules/proposed/2023/34-97142.pdf

[18] DTCC notes that this is consistent with the definition of "service provider" under the recent FSB consultation report on third- party risk management and oversight. https://www.fsb.org/2023/06/enhancing-third-party-risk-management-and-oversight-a-toolkit-for-financial-institutions-and-financial-authorities-consultative-document/

[19] https://www.sec.gov/comments/s7-21-22/s72122-20144972-309569.pdf, see page 7.

on a single set or collection of systems (and/or processes and controls). This seems consistent with the Commission's views as well.[20] Identification of service providers at the clearing agency *services* level would therefore entail an understanding of the service providers for the underlying systems that support the delivery of these clearing agency services. To this end, and consistent with DTCC's rationale above with respect to the comparison with CA Governance Proposal, DTCC believes the same "service provider" definition, coupled with a consistent materiality threshold for "critical" service providers (i.e., those that are fundamental to the operational capability of in-scope systems with no readily available substitutes) can be applied to these two rulemakings so long as the scoping at the "systems" level is clear.[21] For Regulation SCI, this would mean the longstanding definitions of "SCI system," "Critical SCI system," and "indirect SCI system". For proposed Rule 10, this would mean the Commission's proposed definition of "information" and "information systems" (though DTCC believes these definitions, as proposed, may be too broad particularly for certain aspects of the Rule 10 Proposal requirements, as noted in our Rule 10 Proposal comment letter).[22]

Although the aforementioned rulemakings ostensibly serve different purposes (e.g., board of directors responsibilities, operational risk management, recovery and orderly wind-down planning), when collectively applied to one entity, the requirements would apply to the same underlying set of systems, processes, and controls (and the service providers upon which they rely) on which a CCA's clearing and settlement services are built and run. Therefore, DTCC believes that our proposed tiered approach to defining "service providers" and what it would mean to be a "critical" service provider, coupled with clear definitions and tiering of the services or systems applicable for purposes of each of the aforementioned rulemaking, would serve to avoid the regulatory uncertainty that would otherwise arise from establishing bespoke terms for each rulemaking applied to the same underlying service provider risk concepts that would be applicable to the same underlying set of systems or services.

3. *DTCC disagrees that CCAs can reasonably "ensure" that there will be continuation of services by service providers and recommends that the Commission instead adopt a standard that provides CCAs flexibility in developing policies and procedures to facilitate the continuity of services during a recovery or orderly wind-down.*

Recognizing the importance of critical service providers to CCAs' RWPs, the Proposal calls for a RWP to address how the CCA would ensure that a service provider could continue to perform during a recovery or orderly wind-down of a CCA.[23] DTCC disagrees that CCAs can reasonably "ensure" that there will be continuation of services by service providers, particularly external service providers, in the case of a recovery or orderly wind-down. This proposed requirement overestimates the negotiating leverage that CCAs have when entering contracts with service providers or assumes that CCAs would be able to unilaterally require service providers to continue performance during a recovery or orderly wind-down. Federal banking agencies encountered similar concerns regarding lack of negotiating leverage for

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[20] See Proposing Release page 44 that states: "As stated above in section III.B.2.b, a covered clearing agency's critical services, for purposes of inclusion in an RWP, would encompass its critical payment, clearing, and settlement services. Thus, those services could be supported by the covered clearing agency's Critical SCI systems, as defined in Regulation SCI."

[21] As the Commission stated in the CA Governance Proposal on page 93 (and reiterated in its Reg SCI proposal FN 288), investment advisors (for purposes of default management processes) are expected to fall in scope of the CA Governance Proposal but not under Reg SCI. DTCC's suggested formulation would accommodate this difference, as investment advisors would naturally not be identified as a service provider of an SCI system, but would be identified as a service provider of one of a clearing agency's critical services. Again, the key is clear definition of which "systems" or "services" fall within scope of each rulemaking.

[22] https://www.sec.gov/comments/s7-06-23/s70623-199519-399522.pdf

[23] See Proposing Release at page 39.

banking organizations in the final version of the *Final Interagency Guidance on Managing Risks Associated with Third-Party Relationships*.[24] There, commentators noted that "banking organizations may lack sufficient leverage in negotiations with larger third parties and may struggle to get certain "typical" provisions into the contract.[25] The federal banking agencies, acknowledged these limitations, noting that a banking organization may have limited negotiating power in certain instances.

With respect to DTCC's CCAs, Commission concerns regarding continuation of services are mitigated by a vendor management process that requires, to the extent possible, that contracts entered by the CCAs with service providers are assignable by the CCA in the event of a change in control of the CCA, as well as requiring transitional services for a period of time if the contract is terminated. In addition, we would note that Exchange Act Rule 17Ad-22(e)(15)(ii) already requires CCAs to hold liquid net assets funded by equity equal to the greater of either (x) six months of the CCA's current operating expenses, or (y) the amount determined by the CCA's board of directors to be sufficient to ensure a recovery or orderly wind-down of critical operations and services of the CCA, as contemplated under the CCA's RWP.[26] DTCC has always interpreted this requirement as including sufficient resources to continue to pay service providers through the entirety of the execution of a CCA's RWP (whether in the event of recovery or an orderly wind-down) and therefore submits to the Commission that this existing requirement, combined with the proposed revision to ensure continuation of services, should adequately address the Commission's goals for this aspect of the Proposal. As such, DTCC recommends that the Commission revise the proposed standard in this part of the Proposal by removing any requirement that CCAs "ensure" continuation of services. As an alternative, we request that the Commission adopt a standard that acknowledges these limitations and in which a CCA is required to establish, implement, maintain, and enforce written policies and procedures reasonably designed to facilitate consideration of contractual provisions with service providers that, subject to continued payment by the CCA (or successor), obligates them to continue to perform in the event of a recovery and during an orderly wind-down.

Further, the orderly wind-down strategy for each of the CCAs includes the transfer of the critical services and participation to another legal entity. The transfer of critical services and participation would be effected in connection with proceedings under Chapter 11 of the U.S. Federal Bankruptcy Code and after effectuating this transfer, the clearing agency liquidating any remaining assets in an orderly manner in bankruptcy proceedings.[27] As a practical matter, under the Bankruptcy Code, most service provider contracts with the applicable clearing agency could be assumed and assigned to the other legal entity without regard to any ipso facto provisions, since the Bankruptcy Code generally overrides such provisions, and vendors would be stayed from terminating their agreements, subject to being paid. Thus, effectively, the CCAs' RWPs already serves to address the concerns expressed in the Proposal, without an unnecessary and overly prescriptive rule.

4. *While the Clearing Agencies currently conduct robust default management testing that includes use of their respective recovery tools, we do not believe it is appropriate for the Proposal to prescribe a specified approach for the inclusion of CCA participants and, where practicable, other stakeholders in the testing of its RWPs. Further, DTCC requests that the Commission provide additional guidance regarding how CCAs would test the ability to implement the wind-down portion of their RWPs.*

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[24] https://www.govinfo.gov/content/pkg/FR-2023-06-09/pdf/2023-12340.pdf at page 37925.
[25] *Id.*
[26] https://www.sec.gov/rules/final/2016/34-78961.pdf at page 198.
[27] See Securities Exchange Act Release Nos. 91428 (March 29, 2021), (SR-NSCC-2021-004); 91430 (March 29, 2021), (SR-FICC-2021-002), and 91429 (March 29, 2021), (SR-DTC-2021-004).

Proposed Rule 17Ad-26(a)(8) (Testing) would require testing the RWP at least annually and include participants and, where practicable, other stakeholders in the testing. The Proposal states that "The Commission believes that including participants and, where practicable, stakeholders in periodic testing is appropriate because a successful recovery or orderly wind-down will require coordination among these parties, particularly during periods of market stress."[28] DTCC observes that this proposed approach is similar to language included in the Commission's original proposal of Rule 17Ad-22(e)(13) in the 2014 covered clearing agency standards rule proposal.[29] As DTCC noted in its comment letter to that proposal,[30] inclusion of participants in RWP testing is of particular benefit for CCPs that clear derivative products where market participants are key to the wind-down process as they are part of any close-out auctions by the CCP. In contrast, we noted in 2014 and continue to believe for the purposes of this Proposal, that it is important to recognize that the DTCC CCAs clear cash settled U.S. securities transactions, and any required close out would occur by the DTCC CCA effecting market purchases and sales, as opposed to critical reliance upon participant actions in a close-out auction. In these market purchases and sales, participant action and awareness of the defaulter's portfolio is not needed and, in important contrast to the approach we understand is taken in close-out auctions for cleared derivatives portfolios, would be counterproductive to the cash CCA's need for confidentiality around its market-facing close-out activity. Further, the cash market CCAs have a relatively larger number of participants when compared to other cleared markets, which means a prescriptive mandate around participant engagement in RWP testing will be impractical, cost and resource-intensive and, as noted immediately above, potentially antithetical to the underlying goals of an RWP test. Finally, the cash market CCAs have multiple participant types, such as FICC's sponsored (indirect) participants, and as currently drafted, it is unclear how the Proposal would make each different type of participant participate in the annual testing.

We further note that DTCC's CCAs already engage in a significant amount of testing of their risk management and recovery tools, which happens both on an individual basis as well as part of larger exercises, including: annual default simulations; biennially testing multi-member default, and conducting non-default scenarios that include testing of recovery tools, providing readouts of these simulations to our board (which as the Commission has noted[31], includes participant owner representation), regulators, and certain stakeholders; conducting annual loss allocation simulations to test internal processes; and holding a variety of other default and non-default tabletop exercises with internal and external stakeholders. In each instance, the testing of the risk management and recovery tools is designed to ensure that both the CCAs and other relevant stakeholders have a clear understanding of the relevant operational mechanics, decision-making processes, and governance. DTCC recognizes the importance of participants and the board being educated about the policies and procedures CCAs have in place to manage defaults and RWP, and what their role would be in that process. Specifically, DTCC has developed a series of on demand training sessions for members and participants that explain operational requirements and loss allocations for participants in the event of a default at a CCA. DTCC has also implemented live webinar sessions that have the stated goal to educate participants and members about the recovery and wind-down process at DTCC.

DTCC believes that all of these approaches and measures are of equal value when compared to mandating, prescriptively, a role for participants in a CCA's RWP annual testing. We therefore recommend that CCAs be allowed to consider and implement such approaches in satisfying any final requirement the Commission adopts for RWP testing. Thus, instead of requiring that CCA participants be included in testing in all instances, DTCC recommends that the Commission apply the same guidance to

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[28] See Proposing Release at page 59.
[29] Standards for Covered Clearing Agencies, 79 Fed. Reg. 16,866 (proposed Mar. 26, 2014).
[30] https://www.sec.gov/comments/s7-03-14/s70314-16.pdf
[31] https://www.sec.gov/rules/proposed/2022/34-95431.pdf at page 44.

RWP testing that was provided for the adopted version of Rule 17Ad-22(e)(13). That guidance was that the rule does not specify that participants be included in the testing process, but that some or all participants could be included in some or all of the testing.[32] We also note that the Proposal seems to suggest that the Commission could potentially move to adopt such an approach for RWP testing, given that the cost-benefit analysis section in the Proposal discusses how the annual RWP testing requirement might be implemented in a cost-effective manner if the CCAs are able to leverage existing requirements around default management test.[33] Therefore, DTCC believes that the Commission should move to more closely harmonize its Proposal around RWP testing with the current approach it offers to CCAs in implementing Rule 17Ad-22(e)(13). Such an approach would give CCAs the necessary flexibility to design testing procedures to properly fit the particular markets, cleared products, and participants that they serve.

Lastly, DTCC requests that the Commission clarify that the end-to-end RWP testing obligations in the Proposal do not require the testing of steps related to effectuating required legal processes and related decision making. This is because, as a practical matter for a CCA, other than internal governance requirements necessary to determine whether to trigger the implementation of the orderly wind-down plan, implementation would include preparation of Bankruptcy Court filings, the provisioning of legal advice as a result of the entering into the bankruptcy process, and the entering into various agreements and other processes that are operational in nature and do not lend themselves to standardized testing scripts or protocols.

5. *DTCC believes that additional clarification and guidance from the Commission is needed as to the meaning of "effective" as related to tools utilized by a CCA in its RWP, as well as the definition of an "orderly wind-down." In addition, we caution that any Commission guidance regarding the extent to which CCAs need to consider international standard setting guidance as related to RWPs, as well as other topics, has limits in terms of applicability and scope.*

Proposed Rule 17Ad-26(a)(5) (Rule, Policies, Procedures, and Tools) would require a CCA's RWP to identify and describe the rules, policies, procedures, and other tools that a CCA would rely upon during a recovery or orderly wind-down.[34] When describing the tools that the CCA could rely upon, the Proposal notes that the tools should be "effective" and must, among other things, have a "strong legal basis." While DTCC interprets the inclusion of "strong legal basis" to mean that, at a minimum, the recovery or wind-down tool is subject to effective internal governance and has been included in a self-regulatory organization rule filing, we note that without further clarification this term is ripe for parties to interpret in different ways. We therefore request that the Commission provide clear guidance that the term "strong legal basis" does not mean that a CCA is providing a guarantee that there will be no legal challenges to the recovery and orderly wind-down tool, and rather that this concept means that the CCA believes that the recovery or orderly wind-down tool, if exercised, can reasonably be expected to withstand legal challenges if any are raised.

Proposed Rule 17Ad-26(b) provides a definition for the term "orderly wind-down" and includes that an orderly wind-down would occur, "...in a manner that would not increase the risk of significant liquidity, credit, or operational problems spreading among financial institutions or markets and thereby threaten the stability of the U.S. financial system."[35] DTCC notes that the CCAs' orderly wind-down plans seek to limit the risk of significant liquidity, credit, or operational problems spreading among financial institutions or markets, but as a practical matter it is impossible for either the CCAs or the

[32] https://www.sec.gov/rules/final/2016/34-78961.pdf at page 169.
[33] See Proposing Release at page 99.
[34] See Proposing Release at page 53.
[35] See Proposing Release at page 129.

orderly wind-down plans themselves to ex ante guarantee that contagion will not occur or that stability of the U.S. financial system would not be impacted. As such, DTCC recommends that the Commission introduce a reasonably designed standard to this definition so that the relevant section would read, "...in a manner that is reasonably designed to not increase the risk of significant liquidity, credit, or operational problems spreading among financial institutions or markets and thereby threaten the stability of the U.S. financial system, while seeking the continuity of critical services provided by the covered clearing agency and limiting any related operational disruptions."

In the Proposal's discussion of Proposed Rule 17ad-26(a)(9) (Periodic Review) the Commission calls on CCAs to consider the extent to which any new policy statements from standard setting bodies, while not binding, might tend to support the updating or revising of a firm's RWP to ensure the CCA's approach to risk management, recovery, and wind-down are effective at maintaining the core functions of the CCAs in a recovery or resolution scenario and mitigating the potential for transmitting systemic risk through the financial system.[36] DTCC recognizes the important work of global standard setting bodies in identifying the various risks faced by CCPs and proposing recommendations around management actions that can be taken to mitigate these risks. As a general matter of practice, the DTCC CCAs review, incorporate, and adopt such recommendations as appropriate and otherwise consistent with the CCA's obligations under U.S. law. At the same time, in analyzing this aspect of the Proposal we hope that the Commission will continue to recognize the limits inherent in referring to international guidance or standards insofar as we understand that such materials lack legal authority in the U.S., unless explicitly implemented by an appropriate regulatory body pursuant to relevant U.S. law. Therefore, we think it would be prudent as matter of both regulatory and supervisory policy for the Commission to reaffirm in any adopted requirements that relevant international policy statements must be recognized as what they are, which is non-binding guidance for CCAs. This is particularly true when the guidance provided is in contrast to the obligations a CCA faces under U.S. law, or when the guidance is not applicable to specific business lines, assets, or markets that a CCA engages in (e.g., as we have noted above the relevant mechanisms around closing out a defaulters portfolio will vary greatly between a derivatives CCA and a cash market CCA and where international guidance speaks to practices relevant to only certain types of cleared markets, that guidance cannot be, as a presumptive matter, considered immediately applicable to the central clearing of other products). As such, DTCC believes that the language of the Proposal should be clarified further in the adopting release to any final rule so as to acknowledge that policy statements from international standard setting bodies are non-binding guidance, and as such, should be considered as appropriate in the reasonable discretion of a CCA.

6. *As timely communication between a CCA considering initiation of a recovery or orderly wind-down and the Commission is vitally important, DTCC recommends that a CCA be permitted to include in its RWP the particular means of communication used to notify the Commission when the CCA is considering initiation of its RWP. At the same time, DTCC believes that each CCA should have the discretion, based on its internal governance and organizational structure, to establish when a CCA is in fact considering initiating a recovery or orderly wind-down.*

During times of stress at CCAs, which may in turn implicate consideration of initiating an RWP, communication between a CCA and the Commission is imperative. Proposed Rule 17ad-26(a)(7) (Notification to the Commission)[37] recognizes the importance of this communication stream in allowing the Commission to assist a CCA as it implements its RWP; as well as allowing regulators the ability to analyze any potential systemic risks, and facilitating inter-regulatory efforts to manage the recovery or orderly wind down. The proposed rule requires a CCA's RWP to include procedures for informing the Commission when a CCA is *considering* initiating a recovery or orderly wind-down. As noted by the

[36] See Proposing Release at page 62.
[37] See Proposing Release at page 57.

Commission in the Proposal, RWPs are often implemented during times of market stress, and often during these times, circumstances are changing, and decisions are being made quickly. Having a defined process for CCAs to communicate with the Commission during stressful and uncertain times ensures effective and timely communications can be made. As such, we recommend that a CCA be permitted under this aspect of the Proposal to include in its RWP the particular means of communication that would be used to notify the Commission when it is considering initiating a recovery or orderly wind-down, which could include dedicated phone numbers, email addresses, or other forms of electronic communications.

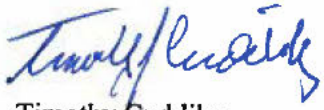
While DTCC believes that there is great utility in having the Commission clarify further the appropriate means of effective communication to the Commission around initiation of an RWP, DTCC also notes that the Proposal does not discuss in any detail what it means for a CCA to "consider" initiating a recovery or orderly wind-down. DTCC believes it would be useful to offer some further guidance around this question and respectfully submits that "consideration" should be understood in this context as having occurred when the necessary governance process as specified in the CCA's RWP and related procedural and governance documentation has commenced. This approach would support effective governance and oversight around how CCAs approach the critical moment of initiating an RWP in a manner that would also help in ensuring the Proposal's goal of making sure a CCA's recovery tools and RWP are effective and have a strong legal basis.

In addition, Proposed Rule 17ad-26(a)(6) (Timely Implementation) calls for CCAs' RWP to address how certain rules, policies, procedures, and other tools would ensure timely implementation of an RWP.[38] Implementation of an RWP involves communication with regulators, and depending on the facts and circumstances at the time, may require approvals from the Commission or other regulators. Given the urgency in these situations, DTCC encourages the Commission to internally prepare and be in a proactive position to receive, consider, and approve any necessary regulatory requests from CCAs in a timely manner when RWPs have been implemented.

Conclusion

DTCC appreciates this opportunity to comment on the Proposal and your consideration of the views expressed in this letter. We look forward to continuing to engage with our members, the Commission, and the broader industry on these important topics. We welcome the opportunity to further discuss any of these comments with you at your convenience. If you have any questions or need further information, please contact me at [redacted].

Sincerely,



Timothy Cuddihy

[38] See Proposing Release at page 56.