



Federated Hermes, Inc.
1001 Liberty Avenue
Pittsburgh, PA 15222-3779

August 30, 2021

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

Via email to rule-comments@sec.gov

Re: Self-Regulatory Organizations; Fixed Income Clearing Corporation; Notice of Filing of Proposed Rule Change To Add the Sponsored GC Service and Make Other Changes, Release No. 34-92014; File No. SR-FICC-2021-003 (the “FICC Proposal”)

Dear Ms. Countryman:

I. Introduction

We are writing on behalf of Federated Hermes, Inc. and its subsidiaries (“Federated Hermes”) to offer our views on the above-referenced proposal for the Fixed Income Clearing Corporation (“FICC”) to amend its rules in order to add the Sponsored GC Service.¹ Repurchase agreement (“repo”) transactions are an important investment for money market funds (“MMFs”). As of May 2021, government and treasury MMFs engaged in repo transactions in the amount of \$804.9 billion with repo counterparties, the majority of which are banks or bank-related entities.

As a leading manager of MMFs and investor in the repurchase agreement market, Federated Hermes supports the FICC Proposal to add the Sponsored GC Service. We also desire to call attention to a structural lack of a liquidity mechanism in the FICC’s recent proposals. The absence of such a mechanism will in our view constrain the amount of term repo transactions that MMFs may enter into.

Federated Hermes has been in business since 1955 and has more than 45 years of experience managing MMFs. During that period, Federated Hermes has participated actively in the money market as it developed over the years.² MMFs managed by Federated Hermes in the

¹ Self-Regulatory Organizations; Fixed Income Clearing Corporation; Notice of Filing of Proposed Rule Change To Add the Sponsored GC Service and Make Other Changes, 86 Fed. Reg. 29,334 (June 1, 2021) (the “FICC Proposal”), available at <https://www.govinfo.gov/content/pkg/FR-2021-06-01/pdf/2021-11407.pdf>.

² The registration statement for Federated Hermes’ Money Market Management fund first became effective on January 16, 1974, making it one of the two longest continuously operating MMFs.

United States include U.S. government MMFs, municipal MMFs and prime MMFs. As of year-end 2020, slightly over two-thirds of the MMF assets managed by Federated Hermes are U.S. government securities. Federated Hermes also manages MMFs and other investment funds and accounts in Canada, Europe and Asia. In addition to MMFs, Federated Hermes manages accounts for institutional customers that invest in money market instruments, as well as state government-sponsored local government investment pools (“LGIPs”) that invest in money market instruments. In all, Federated Hermes manages more than \$400 billion in money market assets.

II. The Repurchase Agreement Market and FICC Repo

A. Background on the Types of Repos

Repo Transactions³ can be settled and cleared in a number of manners and may also encompass different time periods. “Term repos” are Repo Transactions that have a maturity of greater than one business day,⁴ whereas “overnight repos” are Repo Transactions that have a repurchase date on the following business day.⁵ Repo Transactions can take the form of tri-party repo or bilateral repo. A “tri-party repo” is a Repo Transaction where a third party, the tri-party agent,⁶ provides operational and other related services that are used to facilitate settlement of the repo transaction. Alternatively, a “bilateral repo” is a Repo Transaction in which the parties to the repo directly exchange money and securities, absent a clearing bank. Bilateral repos can either allow for general security types or impose restrictions on eligible securities.⁷

B. Sponsored Repo

“Sponsored repo” is an additional form of repo offered by FICC in which a bank or dealer, who is a member of FICC (i.e., Sponsoring Members), sponsors non-member counterparties, such as MMFs, (i.e., Sponsored Members) onto the FICC’s Sponsoring U.S. Member/Sponsored Member Service (the “Service”).⁸ Through its Service, FICC intermediates

³ Capitalized terms not defined herein are defined in the FICC Proposal or the FICC Government Securities Division Rulebook (the “Rulebook”), available at

https://www.dtcc.com/~media/Files/Downloads/legal/rules/ficc_gov_rules.pdf.

⁴ DTCC, REPO SERVICES (last visited August 30, 2021), <https://www.dtcc.com/clearing-services/ficc-gov/repo>. Per the Rulebook, on any particular business day, a “Term Repo Transaction” is a Repo Transaction for which settlement of the End Leg is scheduled to occur two or more Business Days after the scheduled settlement of the Start Leg. Rulebook, *supra* note 3, at 68.

⁵ DTCC, *supra* note 4.

⁶ The tri-party agent facilitates transactions by providing operation services, custody of securities, settlement of cash and securities, valuation of collateral, and optimization tools to allocate collateral efficiently.

⁷ SIFMA, US REPO FACT SHEET (2021), available at <https://www.sifma.org/wp-content/uploads/2020/04/2021-US-Repo-Fact-Sheet.pdf>.

⁸ See FICC, SPONSORED SERVICE (last visited August 30, 2021), <https://www.dtcc.com/clearing-services/ficc-gov/sponsored-membership>.

both sides of the Repo Transaction, allowing Sponsoring Members to offset on their balance sheets their obligations to FICC on Sponsored Member Trades with their Sponsored Members against their obligations to FICC on other eligible FICC-cleared activity, including trades with other Netting Members.⁹ In addition, the Service permits Sponsoring Members to take lesser capital charges for Repo Transactions with Sponsored Members than would be required were such transactions uncleared.¹⁰ For MMFs, as Sponsored Members, it permits access to repo whereby the settlement leg of the transaction becomes an obligation of FICC.

III. FICC Proposal for a Sponsored GC Service

A. The FICC Proposal

The FICC Proposal would amend the Rulebook to add the Sponsored GC Service, which would allow Sponsoring Members and their Sponsored Member clients to execute Repo Transactions with each other on a general collateral basis in the same asset classes as are currently eligible for Netting Members to transact in through FICC/GSD's existing GCF Repo® Service.¹¹ Per the FICC Proposal, such Repo Transactions would be allowed to settle on the tri-party repo platform of a Sponsored GC Clearing Agent Bank¹² similar to the manner in which dealers and MMFs settle tri-party Repo Transactions with each other outside of central clearing.¹³

As explained by the FICC, any accrued repo interest on Sponsored GC Trades would be paid and collected by FICC on a daily basis.¹⁴ If on any Business Day the market value of the specific Eligible Securities that were delivered in the settlement of the Start Leg of the Sponsored GC Trade (the "Purchased GC Repo Securities") is less than the GC Start Leg Market Value, then the Sponsoring Member or Sponsored Member that transferred the securities in the Start Leg (the "GC Funds Borrower") would be required to deliver to FICC (and FICC would be required to deliver to the GC Funds Borrower's pre-Novation counterparty) additional Eligible Securities that are represented by the same Generic CUSIP Number as the Purchased GC Repo

⁹ 86 Fed. Reg. 29,335.

¹⁰ *Id.*

¹¹ *Id.* at 29,336. These asset classes include (i) U.S. Treasury Securities maturing in ten years or less, (ii) U.S. Treasury Securities maturing in thirty years or less, (iii) Non-Mortgage-Backed U.S. Agency Securities, (iv) Federal National Mortgage Association ("Fannie Mae") and Federal Home Loan Mortgage Corporation ("Freddie Mac") Fixed Rate Mortgage-Backed Securities, (v) Fannie Mae and Freddie Mac Adjustable Rate Mortgage-Backed Securities, (vi) Government National Mortgage Association ("Ginnie Mae") Fixed Rate Mortgage-Backed Securities, (vii) Ginnie Mae Adjustable Rate Mortgage-Backed Securities, (viii) U.S. Treasury Inflation-Protected Securities and (ix) U.S. Treasury Separate Trading of Registered Interest and Principal of Securities.

¹² The FICC Proposal defines "Sponsored GC Clearing Agent Bank" as "a Clearing Agent Bank that has agreed to provide FICC, upon request, under mutually agreeable terms, with clearing services for Sponsored GC Trades." *Id.* at 29,339.

¹³ *Id.* at 29,336.

¹⁴ *Id.* at 29,337.

Securities (“GC Comparable Securities”) and/or cash, such that the market value of the Purchased GC Repo Securities (inclusive of the newly transferred securities and cash) is at least equal to the GC Start Leg Market Value. If on any Business Day the market value of the Purchased GC Repo Securities is greater than the GC Start Leg Market Value, the Sponsoring Member or Sponsored Member that received the securities in the start leg (the “GC Funds Lender”) would be required to return to FICC (and FICC would be required to return to the relevant GC Funds Borrower) Purchased GC Repo Securities such that the market value of the remaining Purchased GC Repo Securities remains at least equal to the GC Start Leg Market Value. Such security transactions would occur utilizing tri-party infrastructure under the Proposal.

B. Federated Hermes’ Support for the FICC Proposal

We support the FICC Proposal and FICC’s view that the FICC Proposal, as well as other recent FICC proposals,¹⁵ are likely to increase the amount of term Repo Transactions. Additional term Repo Transaction volumes can in turn serve to help reduce repo rate volatility in the market particularly around holidays and period closings such as quarterly and monthly ends. We believe the operational and portfolio management challenges of complying with the margin requirements under the FICC rules is currently a significant impediment to the broader use of FICC’s term repo offering.

As noted in the FICC Proposal, the FICC has recently taken steps to enable participating members to submit term (rather than overnight) Repo Transactions for clearing.¹⁶ For instance, in the FICC 2020 Proposal, the FICC amended its rules to add a new close-out mechanism and adjusted the calculation of certain funds-only settlement amounts for Sponsored Member Trades that include haircuts.¹⁷ However, there are practical limitations for MMFs under the FICC’s recent proposals. For instance, the current requirement that all Sponsored Member Trades be margined exclusively in cash through FICC’s Funds-Only Settlement Process is not conducive for the MMFs to be able to transact term Repo Transactions with their Sponsoring Members in central clearing.

Although cash margin payments required by the FICC’s current term repo rules should be small under normal market conditions, they are fundamentally at odds with the investment objective of a term repo from the perspective of a MMF. A MMF uses a term repo to invest a specific amount of its cash balances with a specific counterparty. The FICC Funds-Only- U.S.

¹⁵ See, e.g., Self-Regulatory Organizations; Fixed Income Clearing Corporation; Order Approving a Proposed Rule Change Regarding the Close-Out and Funds-Only Settlement Processes Associated With the Sponsoring Member/Sponsored Member Service, Exchange Act Release No. 88262, 85 Fed. Reg. 11,401 (February 27, 2020), available at <https://www.govinfo.gov/content/pkg/FR-2020-02-27/pdf/2020-03914.pdf> (“FICC 2020 Proposal,” and together with the FICC Proposal, “FICC’s recent proposals”).

¹⁶ 86 Fed. Reg. 29,336.

¹⁷ 85 Fed. Reg. at 11,401.

Settlement Process would have the effect of increasing or decreasing this amount of cash. A MMF may be required to maintain higher uninvested cash balances to cover a potential cash margin reconciliation, and could find itself with uninvested cash (on which payment of interest could be required) if it receives cash margin. In addition, managing the Funds-Only-Settlement Process would increase the expense of managing a MMF, with no corresponding benefit to the MMF.

In addition, there is a structural lack of a liquidity mechanism in the FICC's recent proposals. For instance, the FICC's recent proposals do not include a seven-day put option that would allow investors to return the collateral to a financial intermediary at par with seven days' notice. As noted by the Investment Company Institute ("ICI") in a recent 2020 report, "[i]t is this put feature at par that allows these transactions to be considered liquid investments and therefore not limited for purchase by US money market funds."¹⁸ The lack of such a put mechanism will constrain the amount of term Repo Transactions with maturities in excess of seven days that MMFs may enter into. Accordingly, Federated Hermes requests that the SEC and FICC give further thought to how the liquidity needs of MMFs can be addressed.

IV. Tri-Party Repo

While it may not be an intended effect of the FICC Proposal, we note that FICC proposes to leverage the operational infrastructure of tri-party repo for the new Sponsored GC Service. Federated Hermes and other MMF sponsors widely utilize and support the tri-party clearing settlement model. For example, our operations are a product of the traditional term repo tri-party clearing settlement infrastructure in which cash is typically not exchanged between the MMF and the counterparty to the repo between the purchase date and repurchase date of the repurchase transaction. The MMFs managed by Federated Hermes depend on transfers of securities to maintain required margin, and heavily rely on a tri-party repo clearing bank to administer the margin management on such trades. The tri-party repo clearing bank calculates the mark-to-market change in value of the securities underlying each Repo Transaction and facilitates the transfer of securities necessary to ensure the value of the securities equals a specified percentage of the outstanding principal amount of the Repo Transaction. Therefore, in our experience, tri-party Repo Transactions are operationally more efficient than executing delivery-versus-payment transactions and it allows Federated Hermes to engage in Repo Transactions with additional security types since the use of cash collateral is generally minimized. For these reasons Federated Hermes supports FICC's utilization of the tri-party infrastructure to support the Sponsored GC Service.

¹⁸ ICI, EXPERIENCES OF US MONEY MARKET FUNDS DURING THE COVID-19 CRISIS 42 (2020), available at <https://www.sec.gov/comments/credit-market-interconnectedness/c1110-8026117-225527.pdf>.

Securities and Exchange Commission
August 30, 2021
Page Six



V. Conclusion

Thank you for the opportunity to offer our comments on this FICC Proposal. As noted above, we believe that the FICC Proposal would be a beneficial change and allow more MMFs to clear term repos through the FICC.

Sincerely,

A handwritten signature in black ink, appearing to read "Peter J. Germain".

Peter J. Germain
Chief Legal Officer
Executive Vice President

cc: The Honorable Gary Gensler, Chair, SEC
The Honorable Allison Herren Lee, Commissioner, SEC
The Honorable Hester M. Pierce, Commissioner, SEC
The Honorable Elad L. Roisman, Commissioner, SEC
The Honorable Caroline A. Crenshaw, Commissioner, SEC