sifma

asset management group

May 24, 2024

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

Re: ***SEC "Notice of Filing of Proposed Rule Change, as Modified by Partial Amendment No. 1, To Modify the GSD Rules To Facilitate Access to Clearance and Settlement Services of All Eligible Secondary Market Transactions in U.S. Treasury Securities" [Release No. 34-99817; File No. SR-FICC-2024-005] and "Notice of Filing of Proposed Rule Change To Modify the GSD Rules (i) Regarding the Separate Calculation, Collection and Holding of Margin for Proprietary Transactions and That for Indirect Participant Transactions, and (ii) To Address the Conditions of Note H to Rule 15c3-3a" [Release No. 34-99844; File No. SR-FICC-2024-007]***

Dear Ms. Countryman:

The Asset Management Group of the Securities Industry and Financial Markets Association ("SIFMA AMG")[1] appreciates the opportunity to provide comments to the Securities and Exchange Commission (the "Commission") in response to the above referenced rule changes (the "Proposed Rules") proposed by the Fixed Income Clearing Corporation ("FICC"). The Proposed Rules have been issued by FICC to operationalize and implement the Commission's recently adopted rules requiring the central clearing of transactions involving U.S. Treasury securities (the "Treasury Clearing Rules")[2].

Introduction

SIFMA AMG's members are active participants in the market for U.S. Treasury securities. For this reason, we have a strong interest in promoting stability in that market and ensuring that the implementation of the Treasury Clearing Rules will protect the interests of the investor community. While we support the objectives of improving the resilience and integrity of the U.S. Treasury securities market, we continue to be concerned about the potential negative impact that the implementation of the Treasury Clearing Rules may have on the liquidity, resilience, and overall functioning of the Treasury securities market absent meaningful enhancements to the SEC's ruleset and the FICC operating model.

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1 SIFMA AMG brings the asset management community together to provide views on U.S. and global policy and to create industry best practices. SIFMA AMG's members represent U.S. and global asset management firms whose combined assets under management exceed $45 trillion. The clients of SIFMA AMG member firms include, among others, tens of millions of individual investors, registered investment companies, endowments, public and private pension funds, UCITS and private funds such as hedge funds and private equity funds.

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

The impact of the Treasury Clearing Rules will depend in large measure on how FICC amends its rulebook. The Treasury Clearing Rules achieve the clearing mandate by requiring "covered clearing agencies" ("CAAs") to modify their policies and procedures, and FICC is currently the only CCA. The Proposed Rules are FICC's response to the Commission's directive to CAAs to (i) increase the number of ways market participants can access central clearing of covered treasury security transactions and (ii) specify how margin will be calculated, collected and held, including where a direct participant deposits the margin of an indirect participant in a "segregated account".

While we appreciate the effort that went into developing the Proposed Rules, we believe that they fall short of the objectives established by the Commission and are either incomplete, or insufficient, in many respects. In our view, FICC should either revise substantial portions of its Proposed Rules or provide further information to the market regarding its proposals, including its access models. A discussion of these considerations, as well as our recommendations to update and clarify the Proposed Rules is presented below.[3]

Executive Summary

The approach in our letter can be summarized as follows:

1. ***FICC Must Ensure That its Proposals Facilitate "Done-Away" Trading in a Manner that Fulfills the Access Requirements Mandated under the Final Rule***. We urge FICC to revise the Proposed Rules to properly incentivize Netting Members to facilitate done away trading in the manner envisioned in the Treasury Clearing Rules.

2. ***FICC Should Provide a Mechanism for Indirect Participants to Designate Segregation of Margin.*** We recommend that FICC revise the Proposed Rules to give indirect participants the ability to elect segregation of margin held at FICC. Relatedly, we also ask that FICC confirm that indirect participants can post as margin, and elect segregation of, collateral obtained from margin lending transactions.

3. ***FICC should allow Indirect Participants to Close Out their Positions with Defaulting Netting Members and, in Lieu Thereof, Elect to Receive Payments Directly From FICC.*** We recommend that FICC provide a mechanism for indirect participants to liquidate their positions executed with defaulting Netting Members. To the extent this is not feasible, indirect participants should then have the ability to elect to receive payment directly from FICC, with FICC using any customer[4] funds held at FICC to satisfy such amounts owed. Additionally, we urge FICC to provide a framework for allowing Executing Firm Customers under the Agent Clearing Model to close out their trades with defaulting Netting Members.

4. ***The Proposed Rules should Provide a Mechanism Allowing Customers to "Port," or Transfer, Transactions from One Netting Member to another Netting Member.*** We urge FICC to adopt a

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[3] Terms used but not defined herein shall have the meaning given to such terms in the Proposed Rules or the Treasury Clearing Rules, as applicable.

[4] For the purposes of this letter, we refer to "indirect participants" and "customers" interchangeably for the convenience of the reader.

mechanism by which indirect participants can port their trades from one Netting Member to another Netting Member, especially with respect to any term repo positions**.**

5. ***FICC Should Not Require a Minimum Deposit of $1 million.*** We recommend that FICC reject the $1 million minimum deposit requirement for each Segregated Indirect Participant Account and instead require Netting Members to determine a properly calibrated margin requirement for each customer based on its risk management policies and procedures.

6. ***FICC Should Detail and Explain How its Rules Will be Adapted to Facilitate Access to Cross-Margining Solutions for both Direct Participants and Indirect Participants.*** We ask that FICC supplement the Proposed Rules with a proposal for cross-margining U.S. Treasury transactions cleared at FICC with transactions cleared through other clearinghouses and fully address how such cross-margining would be handled in the event of a Netting Member and/or clearing member bankruptcy.

7. ***The Proposed Rules should not Preclude Netting Members From Satisfying the Clearing Mandate by Clearing Through Other Clearing Venues.*** We request that FICC revisit and, if necessary, revise, the portions of the Proposed Rules that appear to mandate clearing through FICC.

8. ***FICC Should Clarify, and Potentially Further Limit, the Circumstances under Which "Fellow-Customer Risk" Could Arise under the Proposed Rules.*** Our members would like clarity as to when FICC would exercise any right that could introduce an element of fellow customer risk and adopt reasonable limits to FICC's ability to withhold Excess Segregated Customer Margin.

9. ***The Commission Should Not Approve the Proposed Rules until FICC Publishes a Robust Legal Enforceability Analysis and Otherwise Addresses Indirect Participants' Ability to Close-out Netting Members.*** FICC should provide market participants with the required legal analysis regarding the enforceability of the Proposed Rules. In doing so, FICC can draw from the extensive analysis conducted by the industry over the years, for example, when implementing the segregation model for cleared swaps under the CFTC's LSOC model.

10. ***FICC should Better Articulate the Use Cases for Each Proposed Access Model and, if Necessary, Simplify or Reduce the Number of Proposed Access Models.*** We request that FICC better articulate the relative benefits of each proposed access model and why one market participant would elect to adopt one model over another. It should also provide the industry with information supporting the position that it can accommodate a vast array of new accounts. To the extent it cannot do these things, FICC should consider reducing the number of proposed access models and rethink how it is responding to requirements imposed on it by the Treasury Clearing Rules.

11. ***FICC Should Consider the Cross-Border Application of its Proposed Rules and Provide a Framework for Foreign Netting Members' and Indirect Participants' Compliance with the Proposed Rules.*** We request that FICC collect information on how its Proposed Rules may impact market participants of varying types in the Cross-Border context and, as necessary, provide a workable framework for how such market participants – specifically indirect

participants subject to limitations on the ability to post margin – can comply with the Proposed Rules.

Discussion

1. ***FICC Must Ensure That its Proposals Facilitate "Done-Away" Trading in a Manner that Fulfills the Access Requirements Mandated under the Final Rule.***

SIFMA AMG wants to emphasize that a workable "done away" model is crucial to accommodating the dramatically increased volume of clearing that will be required as a result of the Treasury Clearing Rules.

Unlike the "done with" clearing model that is predominant in the Sponsored Service under which an indirect participant generally executes and clears with its Sponsoring Member, a "done away" clearing model allows indirect participants to execute trades with, and potentially obtain better pricing from, any number of executing brokers who in turn will "give up" the trades to the indirect participant's clearing broker. While the Commission has acknowledged the importance of having the increased scale a "done away" model of clearing can facilitate, it stopped short of mandating that CCAs require their direct participants to accept "done away" trades under the Treasury Clearing Rules. Instead, the Commission charged CCAs with "taking all appropriate steps" to accommodate done away trades. CCAs are also expected, pursuant to their obligations under new Rule 17ad-22(e)(18)(iv)(C), to consider "whether to establish policies and procedures that enable direct members to submit to the U.S. Treasury securities CCA eligible transactions for clearance and settlement that have been executed by two indirect participants of the U.S. Treasury securities CCA."[5]

However, we have grave concerns that the access models offered up in the Proposed Rules will not be enough to facilitate the scale of done away trading envisioned by the Commission to fully transition the Treasury market to clearing.

By FICC's own admission, one of the key reasons a successful done away access model has failed to take root is that the prime broker / correspondent clearing access model in effect today is rarely used and not well understood.[6] Yet, the only discernable changes that FICC made to this access model in the Proposed Rules were to rename it the "Agent Clearing Service" and make conforming, technical amendments to the FICC Government Securities Division's Rulebook (the "FICC Rulebook") in hopes that customers "recognize the similarities between FICC's indirect access model and FCM agent clearing models" and therefore start to use it.[7]

These superficial changes alone will be insufficient to significantly increase the availability of done away trading, especially given that it is unclear to us how the proposed indirect access model

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5 Treasury Clearing Adopting Release at 2760.

6 See "Self-Regulatory Organizations; Fixed Income Clearing Corporation; Notice of Filing of Proposed Rule Change, as Modified by Partial Amendment No. 1, To Modify the GSD Rules To Facilitate Access to Clearance and Settlement Services of All Eligible Secondary Market Transactions in U.S. Treasury Securities", 89 Fed. Reg. 21363 (Mar. 27, 2024), at 21363.

7 *Id.*

resembles the FCM agent clearing models in the way claimed by FICC. Indeed, our members' biggest concerns regarding the implementation of a done away model remain unaddressed by the Proposed Rules.

FICC has also repeatedly explained that "done away" clearing is possible through the Sponsored Service but has failed to grapple with why market participants are not leveraging that service today. In its final rulemaking, the Commission noted that FICC is expected to "consider the volumes and proportion of the market that are being centrally cleared through different access models as part of [FICC's] consideration of whether its access models are meeting the needs of the market."[8] Notwithstanding this mandate from the Commission, industry experience makes clear that FICC's existing models are not fit to facilitate "done away" clearing. Without additional changes to FICC's access models, many market participants may be shut out of this market, which could have significant negative effects on liquidity.

The most significant impediment to a successful done away model is that under current FICC rules, Netting Members can force indirect participants to bundle execution and clearing services making it practically impossible for an indirect participant to execute trades with another broker – the key indicia of a done-away model. Absent a requirement in the FICC Rulebook compelling Netting Members to accept for clearing trades executed with other brokers, SIFMA AMG does not expect Netting Members to offer done-away trading via the Agent Clearing Model (which would effectively result in clearing members surrendering potentially lucrative commissions from trade execution to other brokers). The Proposed Rules do not address this issue or otherwise provide any other mechanism to properly align Netting Members' incentives with the goal of facilitating done-away trading.

Another issue is that the no-action relief granted under the Treasury Clearing Rules for registered funds from enforcement under Section 17(f) of the Investment Company Act only appears to extend to registered funds trading through the Sponsored Service. It does not extend to the "Agent Clearing Service." Absent any separate no action relief or guidance from the Commission, registered funds will be hesitant to use an Agent Clearing Service done away model. Our registered investment company members are concerned that the unavailability of the Agent Clearing Service model to their funds, and in turn their funds' investors, will leave them at a disadvantage in terms of pricing and liquidity as compared to other market participants who will have access to the benefits of the done away model.

Accordingly, SIFMA AMG urges FICC to revise the Proposed Rules to properly incentivize Netting Members to facilitate done away trading in the manner envisioned in the Treasury Clearing Rules. If FICC determines that there is no feasible way to indirectly create such incentives through the way the clearing models are designed, FICC should consider imposing in the FICC Rulebook an explicit requirement for its Netting Members to offer done away trading to indirect participants. Furthermore, FICC should consult with the Commission to provide a mechanism – which may include further no-action relief -- by which registered funds can use the Agent Clearing Service on terms no less advantageous than other market participants.

[8] Treasury Clearing Adopting Release at 2760.

2. ***FICC Should Provide a Mechanism for Indirect Participants to Designate Segregation of Margin.***

The Treasury Clearing Rules require FICC to establish a clearing model that enables margin of indirect participants to be held in segregated accounts. The segregation of customer margin, coupled with the corresponding amendment to Rule 15c3-3a enabling broker-dealers to record any customer margin posted to a segregated account as a "debit" in its reserve formula, offer additional protections and benefits to market participants. In our view, the amendment to the customer protection rule also provides a strong incentive to broker-dealers to collect margin from their customers and then deposit this margin at FICC. However, the current proposal has several major shortcomings.

First, while the Proposed Rules give Netting Members the ability to "designate" an indirect participant's account as a "segregated" account, they are silent on whether or not indirect participants themselves have any right to direct their Netting Member to segregate their margin. Such a right for indirect participants is highly desirable for a variety of reasons: an indirect participant may want certainty that margin that it posts receives the protection provided by segregation. Alternatively, an indirect participant may prefer the flexibility of having its Netting Member post margin from its own funds (and reflect this in the pricing of its trades with the Netting Member).

Second, it is not clear how the establishment of Segregated Indirect Participant Accounts will impact indirect participants' trading with Netting Members who are not broker-dealers and who will not benefit from the amendment to the broker-dealer customer protection rule regarding the recording of segregated margin as a "debit." There is no similar incentive for such non-broker-dealer Netting Members to segregate customer margin. This is another reason FICC rules should require Netting Members to give indirect participants the option to designate whether their margin will be placed in a segregated account at FICC.

It cannot be over-emphasized the importance to SIFMA AMG members of the ability to opt into a clearing model that provides protections approximating those offered by the "legally segregated operationally commingled" (LSOC) model that applies to cleared swaps. Quite simply, access to LSOC-like protections is central to the successful adoption of the Treasury clearing mandate.

Therefore, we ask that FICC revise the Proposed Rules to give indirect participants the ability to elect segregation of margin held at FICC. Relatedly, we also ask that FICC confirm that indirect participants can post as margin, and elect segregation of, collateral obtained from margin lending transactions.

3. ***FICC should allow Indirect Participants to Close Out their Positions with Defaulting Netting Members and, in Lieu Thereof, Elect to Receive Payments Directly From FICC.***

In addition to the points discussed above, successful adoption of U.S. Treasury clearing will require that indirect participants have adequate close out rights in the event of a Netting Member's default. While we acknowledge the Commission's views that the FICC rules already address bankruptcy-related concerns[9], our members feel strongly that the protections afforded to indirect participants under the FICC rules in the event of a Netting Member's default are far from sufficient in their present form.

Foremost, under the FICC rules, the process for closing out indirect participants' trade positions under the Sponsored Service is driven entirely by FICC, with indirect participants having no "say" in whether their positions are closed out. This means that a Netting Member's customer may need to continue to rely on an insolvent (or near-insolvent) Netting Member to make or receive payments on its behalf.

Then, in the event the Netting Member becomes subject to a bankruptcy or similar proceeding, there could be uncertainty as to an indirect participant's ability (or the timing around its ability) to access margin posted on its behalf at FICC to satisfy any amounts owed to it by the Netting Member[10]. Such delays in the ability to close out positions and apply margin to satisfy claims owed to indirect participants would effectively serve to sap liquidity from the market and would thereby work at cross purposes to the Treasury Clearing Rule's objective of increasing operational efficiency and strengthening the soundness of the overall Treasury securities market.

Moreover, the lack of any rules or guidance addressing indirect participants' close out rights under the Agent Clearing Model is in our view a significant omission from the Proposed Rules. There is no discussion in the Proposed Rules as to Executing Firm Customers' close out rights under the Agent Clearing Model and we call on FICC to clearly address such critical close-out rights in its rules.

Accordingly, we request that FICC provide a mechanism for indirect participants to liquidate their positions executed with defaulting Netting Members. To the extent this is not feasible, indirect participants should then have the ability to elect to receive payment directly from FICC, with FICC using any customer funds held at FICC to satisfy such amounts owed. Additionally, we urge FICC to provide a framework for allowing Executing Firm Customers under the Agent Clearing Model to close out their trades with defaulting Netting Members.

4. ***The Proposed Rules should Provide a Mechanism Allowing Customers to "Port," or Transfer, Transactions from One Netting Member to another Netting Member.***

The Proposed Rules do not currently provide a mechanism to allow indirect participants to "port," or transfer, their transactions from one Netting Member to another. An indirect participant may desire such an ability to transfer its positions in the event it is experiencing issues with a Netting Member, including where such Netting Member is approaching insolvency or simply where the indirect participant is dissatisfied with the pricing or level of service provided by such Netting Member.

The absence of any ability to transfer cleared positions may result in market participants being less likely to trade, either because they are uncomfortable with the risk profile of having to clear through a limited number of Netting Members, or because they feel constrained to clear through their existing Netting Member. The inability to port could also exacerbate risks to a systemic level by effectively

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9 See the Treasury Clearing Adopting Release at 2731.

10 A Netting Member may, for instance, still owe a customer funds or delivery of securities under the "on-leg" of a repurchase transaction that has not been novated to FICC.

trapping customer positions and thereby reducing overall Treasury market liquidity in the event of a Netting Member insolvency.

It is worth noting that the ability to port positions is an important feature of the cleared swaps and futures market, and one that our members have expressed a strong desire in seeing implemented for U.S. Treasury clearing. Underscoring the importance of the ability of customers to port their positions is the fact that it is stated as a policy preference of the Commodity Futures Trading Commission ("CFTC") in the event of a futures commission merchant's insolvency.[11]

Accordingly, SIFMA AMG urges FICC to adopt a mechanism by which indirect participants can port their trades from one Netting Member to another Netting Member, especially with respect to any term repo positions. Furthermore, we ask that such mechanism allow indirect participants to affect the transfer of their positions from one Netting Member to another by sending porting instructions directly to FICC, as there may be instances in which the Netting Members experiencing distress are not responsive to their customers' instructions.

5. ***FICC Should Not Require a Minimum Deposit of $1 million.***

FICC's proposal to require Netting Members to deposit margin of at least $1 million in each Segregated Indirect Participant's Account will create an arbitrary barrier to the market that will reduce liquidity and is not tailored to reduce risk in the market. FICC's reasoning for proposing the $1 million minimum deposit is that it is the same minimum amount currently applicable to Netting Members for their own accounts, and furthermore, that it aligns with findings from back testing of the Clearing Fund showing that a $1 million per customer minimum deposit would provide sufficient protection to Netting Members against intraday swings in their exposures.

However, FICC's reasoning is flawed, even if well-intentioned, for a few reasons. First, from a purely practical perspective, using the $1 million minimum margin deposit Netting Member requirement as a benchmark draws an unfair comparison between Netting Members – who are generally much larger and can more easily "afford" $1 million – and indirect participants, who are generally much smaller in size than Netting Members. Such smaller indirect participants may refrain from, or reduce their trading in, U.S. Treasury securities if faced with the requirement to post $1 million in cash to cover their minimum deposit requirement. They may also choose not to elect segregation, which would erode the customer protection benefit and thereby increase downstream risk should a Netting Member fail.

Moreover, the proposed $1 million minimum contradicts the Commission's expectations with regard to access of registered investment companies. Registered investment companies are required to segregate margin and would therefore be subject to the $1 million minimum. In its final rulemaking, the Commission explained that registered funds are important participants in the repo market[12], and that "facilitating the ability for a registered fund's margin to be posted at FICC as an alternative to the sponsoring member posting the margin and passing the cost of doing so through to the registered fund may lower the cost of trading for the fund…"[13] The Commission clearly understands, therefore, that

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[11] See Part 190.00(c)(4) of the CFTC's Rules.

[12] See the Treasury Clearing Adopting Release at 2726.

[13] *Id.* at 2809.

registered investment companies are important sources of liquidity in the repo market, that they are required to segregate margin posted to clearing agencies, and that allowing them to post margin would lower costs and increase participation and liquidity in the repo market. Yet, FICC has proposed an arbitrary $1 million minimum that would likely preclude many smaller registered funds from posting margin. As a result, as the Commission inferred, the costs of trading for such funds will likely increase and liquidity may suffer.

Secondly, and more importantly, the proposed minimum deposit ignores the actual risk profile of individual indirect participants, which can vary greatly. For instance, an indirect participant who trades infrequently, and in small quantities, poses an entirely different risk to the market than one that trades frequently, and/or in large quantities. Therefore, applying the same minimum deposit requirement irrespective of indirect participants' level of clearing activity at FICC unfairly forces smaller market participants to bear a cost, and effectively pay a premium to insure, the losses that could be borne by larger market participants.

Our members are not aware of any other clearing model, such as those for futures and cleared swaps, which have a fixed minimum margin deposit requirement for indirect participants. In other robust clearing models – which have demonstrated their effectiveness for years and through multiple market shocks - it is the clearing member that is required to post margin which is calibrated to the risk of its customers. The clearing member is effectively charged with the task of monitoring the credit and risk profile of its participants and collecting any add-on margin to address such assessed risks. We see no reason the Treasury clearing model – drawing from the experience of other established models – should be any different.

Accordingly, FICC should reject the $1 million minimum deposit requirement for each Segregated Indirect Participant Account and instead require Netting Members to determine a properly calibrated margin requirement for each customer based on its risk management policies and procedures.

6. ***FICC Should Detail and Explain How its Rules Will be Adapted to Facilitate Access to Cross-Margining Solutions for both Direct Participants and Indirect Participants.***

The ability to cross-margin cleared trades is of paramount importance to our members. Cross-margining programs significantly lower the cost of clearing to indirect participants by permitting them to calculate risk-based margin requirements against positions in different financial products that may be cleared at different clearinghouses. Our members already rely heavily on such cross-margining programs available under different regulatory regimes and would expect to have similar flexibility to cross-margin transactions involving U.S. Treasury securities that will be cleared at FICC and other clearinghouses.

The Proposed Rules, however, do not address whether any cross-margining programs would be available to indirect participants and how current proposals to separately account for house and customer margin would be affected by them, including with respect to the applicable bankruptcy implications. For instance, we are aware that FICC and the CME have proposed a cross-margining program that would allow a customer to trade U.S. Treasury securities out of a futures account. However, this proposal has not been formalized and, when it is, it will likely have a dramatic impact on the way Netting Members calculate, collect, and hold customer margin requiring FICC to revisit the rules it is now presently proposing.

In light of this, we ask that FICC supplement the Proposed Rules with a proposal for cross-margining U.S. Treasury transactions cleared at FICC with transactions cleared through other clearinghouses and fully address how such cross-margining would be handled in the event of a Netting Member and/or clearing member bankruptcy.

7. *The Proposed Rules should not Preclude Netting Members From Satisfying the Clearing Mandate by Clearing Through Other Clearing Venues.*

Currently, FICC is the only CCA for U.S. Treasury securities. This poses obvious "concentration risk," or the risk that any operational, technical, or other failure experienced by FICC could disrupt or even completely stall trading in the U.S. Treasuries market. Having one single CCA also raises potential anti-competitive concerns.

These issues have not been lost on the marketplace, and other clearing agencies, notably the CME, are already contemplating an expansion of their cleared product offering. In light of this, FICC needs to confirm or provide clarification that the Proposed Rules will not prohibit or disincentivize Netting Members from clearing transactions through another clearing agency.

We are particularly concerned about language that states, or implies, that a Netting Member ***must*** clear certain transactions with FICC. Accordingly, we request that FICC revisit and, if necessary, revise, the portions of the Proposed Rules that appear to mandate clearing through FICC.

8. *FICC Should Clarify, and Potentially Further Limit, the Circumstances under Which "Fellow-Customer Risk" Could Arise under the Proposed Rules.*

It is of serious concern to SIFMA AMG members that in at least two instances, the Proposed Rules introduce a circumstance in which one indirect participant's margin could be used by a Netting Member to satisfy the margin requirement associated with another indirect participant that is in default, giving rise to "fellow-customer risk."

In its proposed revision to the definition of "Net Settlement Positions", FICC proposes that that any Current Net Settlement Position in a Sponsoring Member Omnibus Account or Segregated Indirect Participant's Account that is not clearly allocable to a particular Sponsored Member or Segregated Indirect Participant (because of settlement failure etc.) will be allocated, for the purposes of calculating the margin requirement, pro rata across all Sponsored Members or Segregated Indirect Participants that had, as of the end of the preceding Business Day, net positions in the same direction and CUSIP as the un-allocable Current Net Unsettled Position. Our members have raised concerns that this could result in fellow-customer risk to the extent one customer's positions are aggregated together with those of other customers for the purpose of calculating a margin requirement.

We believe FICC should provide assurances that one Segregated Indirect Participant's margin ***will not be used to satisfy the obligations of, or owed to, another customer***.

For similar reasons, our members seek to better understand and, if possible, limit the circumstances under which FICC may exercise its right to withhold the return of Excess Segregated Customer Margin under proposed Section 10(b) of Rule 4 in the FICC Rulebook. Under this proposed rule change, FICC appears to have the right to elect ***not*** to return Excess Segregated Customer Margin of one indirect participant if the Netting Member through which such indirect participant clears owes an obligation to FICC for ***any*** Segregated Indirect Participant.

Our members would like clarity as to when FICC would exercise this right and, if it does in fact introduce an element of fellow customer risk, adopt reasonable limits to FICC's ability to withhold Excess Segregated Customer Margin.

9. ***The Commission Should Not Approve the Proposed Rules until FICC Publishes a Robust Legal Enforceability Analysis and Otherwise Addresses Indirect Participants' Ability to Close-out Netting Members.***

Section 17A of the Exchange Act and the regulations thereunder require FICC to provide (i) a well-founded, clear, transparent, and enforceable legal basis for each aspect of its activities and (ii) sufficient information to enable market participants to identify and evaluate risks incurred by participating in FICC.

Thus far, FICC has not provided any formal analysis regarding the commercial law and insolvency implications of the Proposed Rules and, of particular importance for our members, regarding the ability of indirect participants to recover funds posted to a Netting Member (or at FICC) in the event of such Member's, or FICC's, failure. Instead, FICC has merely stated that an indirect participant' ability to recover fund will depend on the relevant insolvency regime.[14] As a result, it is difficult for market participants to assess whether the rules truly achieve the enhanced customer protection objectives of the Treasury Clearing Rules.

Accordingly, FICC should provide market participants with the required legal analysis regarding the enforceability of the Proposed Rules. In doing so, FICC can draw from the extensive analysis conducted by the industry over the years, for example, when implementing the segregation model for cleared swaps under the CFTC's LSOC model.

10. ***FICC should Better Articulate the Use Cases for Each Proposed Access Model and, if Necessary, Simplify or Reduce the Number of Proposed Access Models.***

The Proposed Rules provide access to clearing through four account types: (1) Agent Clearing Member Omnibus Accounts, (2) Segregated Agent Clearing Member Omnibus Accounts, (3) Sponsoring Member Omnibus Accounts and (4) Segregated Sponsoring Member Omnibus Accounts. While the Proposed Rules go into detail explaining how each type of account will be established and function, FICC has not explained the relative benefits of each of the account types and models. This makes it difficult for clearing firms to decide on their proposed offerings and for indirect participants to determine which model of clearing to pursue.

For example, while the Proposed Rules tout the establishment of an Agent Clearing Service to replace the existing prime broker / correspondent clearing service, the Proposed Rules do not articulate

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[14] See "Self-Regulatory Organizations; Fixed Income Clearing Corporation; Notice of Filing of Proposed Rule Change To Modify the GSD Rules (i) Regarding the Separate Calculation, Collection and Holding of Margin for Proprietary Transactions and That for Indirect Participant Transactions, and (ii) To Address the Conditions of Note H to Rule 15c3-3a", 89 Fed. Reg. 21603 (Mar. 28, 2024), at 21611, fn. 43.

why market participants would find the Agent Clearing Service preferable to the existing Sponsored Service (or vice versa). FICC should, for instance, specifically address the circumstances under which an indirect participant would execute a "done away" trade through the Agent Clearing Service as opposed to the Sponsored Service.

Market participants also seek to better understand the legal, operational, and administrative complexities of trading through the Agent Clearing Services as opposed to the Sponsored Service, including how involved the onboarding process and documentation will be for each model.

As another example, while we see the benefit to an indirect participant of giving its Netting Member the ability to deposit its initial margin to "segregated" (as opposed to omnibus) accounts at FICC, it is less clear what the benefit would be to indirect participants of having their margin held in omnibus accounts that don't provide for segregation. FICC does not provide an explanation of the rationale and benefits of such an omnibus model.

We also submit that some of the proposed rule changes that provide for new account types are too open-ended and ambiguous. For example, new rule 2B of the FICC Rulebook includes a provision at the end thereof that states "[u]nless otherwise expressly stated in the Rules, all references to a Sponsoring Member Omnibus Account and Agent Clearing Member Omnibus Account shall also apply to Segregated Indirect Participants Accounts". It is difficult to discern what substantive effect such a broad statement has on customer segregated accounts. We think FICC should provide a detailed "roadmap" of each rule applicable to omnibus accounts that will now be applicable to segregated accounts to ensure that market participants can fully evaluate the impact of the rulebook proposals.

Finally, it is unclear if FICC has the ability to onboard and account for the potentially vast number of accounts of different types that will need to be established to support the increased volume of clearing activity. One of the core objectives of the Proposed Rules is to facilitate clearing of cash and repo transactions involving U.S. Treasury securities by enabling indirect participants to trade under different access models, including with multiple executing brokers under the Agent Clearing Service model. However, doing so will require that, in addition to setting up omnibus accounts for the Sponsored and Agent Clearing Service models, each Netting Member acting as an "Agent Clearing Member" will also need to set up at FICC individual accounts for each indirect participant for which it is segregating margin. FICC has not demonstrated or confirmed that it has the operational capability of onboarding and accounting for such a large number of accounts.

For these reasons, we request that FICC better articulate the relative benefits of each proposed access model and why one market participant would elect to adopt one model over another. It should also provide the industry with information supporting the position that it can accommodate a vast array of new accounts. To the extent it cannot do these things, FICC should consider reducing the number of proposed access models and rethink how it is responding to requirements imposed on it by the Treasury Clearing Rules.

11. ***FICC Should Consider the Cross-Border Application of its Proposed Rules and Provide a Framework for Foreign Netting Members' and Indirect Participants' Compliance with the Proposed Rules.***

Several of our members have voiced concerns about how the Treasury Clearing Rules and the Proposed Rules that seek to implement these Rules will apply to non-U.S. direct and indirect participants.

Specifically, we are concerned that the U.S. Treasury clearing mandate will adversely impact foreign customers that are limited in their ability, or prohibited entirely, to post margin in connection with transactions involving U.S. Treasury securities. For instance, we understand that Article 15(2) of the European Union's Money Market Fund Regulation prohibits European Money Market Mutual Funds from pledging any assets received under reverse repurchase agreements. We understand that Undertakings for Collective Investment in Transferable Securities (UCITS) and similar investment vehicles may also be subject to restrictions on their ability to post margin that will be held on deposit at FICC.

Accordingly, we request that FICC collect information on how its Proposed Rules may impact market participants of varying types in the Cross-Border context and, as necessary, provide a workable framework for how such market participants – specifically indirect participants subject to limitations on the ability to post margin – can comply with the Proposed Rules.

Conclusion

As stated above, SIFMA AMG has a strong interest in promoting stability in the market for U.S. Treasury securities and ensuring that the implementation of the Treasury Clearing Rules will protect the interests of the investor community. We believe that the rule changes promulgated by FICC to implement and operationalize the Treasury Clearing Rules will ultimately play a central role in determining whether the clearing mandate succeeds in achieving its objectives. Consequently, we urge the Commission to consider our comments and recommendations included in this letter.

On behalf of SIFMA AMG, we appreciate the opportunity to respond to the Proposed Rules and your consideration of our comments and recommendations. If you have any questions or require additional information, please do not hesitate to contact us by calling William Thum at (202) 962-7381.[15]

Sincerely,

William C. Thum
Managing Director and Assistant General Counsel, SIFMA AMG

cc: The Hon. Gary Gensler, SEC Chair
The Hon. Hester M. Peirce, SEC Commissioner
The Hon. Caroline A. Crenshaw, SEC Commissioner
The Hon. Mark T. Uyeda, SEC Commissioner
The Hon. Jaime Lizárraga, SEC Commissioner
Dr. Haoxiang Zhu, Director, Division of Trading and Markets

[15] SIFMA AMG is grateful for the advice and drafting assistance of Darren Littlejohn and Andrew DesRault of Clifford Chance in the preparation of this comment.