Via Electronic Submission: baselcommittee@bis.org

Basel Committee on Banking Supervision
Bank for International Settlements
Centralbahnplatz 2,
CH-4002 Basel
SWITZERLAND

Re: Treatment of Segregated Initial Margin in the Calculation of Centrally Cleared Derivatives Exposures under the Basel III Leverage Ratio Framework

Dear Sir or Madam:

Managed Funds Association\(^1\) welcomes the opportunity to provide comments to the Basel Committee on Banking Supervision (“BCBS”) to express our concerns with the treatment of segregated initial margin (“IM”) for centrally cleared derivatives exposure under the supplementary leverage ratio (“SLR”) set out in the BCBS document entitled “Basel III leverage ratio framework and disclosure requirements” (the “SLR Framework”).\(^2\) MFA members support central clearing and are substantial users of central counterparty (“CCP”) clearing services for both exchange-traded and cleared over-the-counter (OTC) derivative contracts, and their demand for such services will increase as different regulators fully implement their respective mandatory clearing initiatives. As buy-side market participants, MFA members access CCPs as clients of clearing members under contractual relationships with clearing members that enable them to clear derivative contracts indirectly with the relevant CCP.

MFA generally endorses a number of recent comment letters submitted to the BCBS and other regulatory bodies from a broad range of stakeholders in the cleared derivatives markets expressing serious concerns with the SLR calculation for cleared derivatives.\(^3\) Each of these

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1. Managed Funds Association (“MFA”) represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent and fair capital markets. MFA, based in Washington, DC, is an advocacy, education and communications organization established to enable hedge fund and managed futures firms in the alternative investment industry to participate in public policy discourse, share best practices and learn from peers, and communicate the industry’s contributions to the global economy. MFA members help pension plans, university endowments, charitable organizations, qualified individuals and other institutional investors to diversify their investments, manage risk and generate attractive returns. MFA has cultivated a global membership and actively engages with regulators and policy makers in Asia, Europe, the Americas, Australia and many other regions where MFA members are market participants.


3. See Letter from Timothy W. Cameron Esq., Managing Director, Asset Management Group – Head, Securities Industry and Financial Markets Association, and Matthew J. Nevins Esq., Managing Director and Associate General Counsel, Asset Management Group, Securities Industry and Financial Markets Association, to the BCBS, November 18, 2014; see also the following submissions: Letter from Walter Lukken, President and Chief Executive Officer, FIA Global; Siddharta Roy, Chairman, CCP12; Terrence A. Duffy, Executive Chairman and President, CME Group; Scott A. Hill, Chief Financial Officer, Intercontinental Exchange; Andreas Preuss, Chief
letters explains particular concerns and recommended solutions that align with the views of MFA members. Accordingly, we express our support of the industry positions and recommendations in these letters.

In particular, MFA is very concerned that the SLR does not account for the fact that segregated customer IM for centrally cleared derivatives cannot be used to lever the customer’s clearing member firm. Customers post IM to their clearing firms for the benefit of CCPs to secure customer performance under cleared derivative transactions. Customer IM thus reduces the clearing firm’s exposure to guarantee the customer’s performance to the CCP. Clearing firms may not use these funds for any other purpose. But without any capital recognition for such reduced exposure, clearing firms may face unnecessarily high capital costs that do not appropriately reflect their exposure reduction from segregated customer IM for cleared derivatives. We also understand that this regulatory treatment is compounded by applicable accounting standards that require clearing member banking organizations to treat segregated cash IM as a balance sheet item that must be separately added as an exposure to the clearing member. This accounting treatment would subject clearing member banks to increased capital costs, and will likely incentivize them to accept only non-cash IM from customers.

Buy-side market participants, including MFA members, fear that unnecessarily high capital requirements are not commercially sustainable for clearing firms, and that they will likely be passed onto clearing customers in the form of higher clearing fees or other charges. We believe that if only a few clearing firms can meet these higher capital requirements on an ongoing basis, it could result in a smaller pool of firms offering client clearing services, which would reduce customer choice and harm competition in the market for client clearing services. Fewer clearing firms could reduce competition, resulting in higher fees. Moreover, many hedge funds have sought to use multiple clearing firms in the wake of the failure of Lehman Brothers. In our view, none of these outcomes serves the G-20 policy objectives to incentivize central clearing of derivatives and to reduce systemic risk in the financial markets. We respectfully urge the BCBS to reconsider the effects of the SLR on cleared derivatives in light of these policy objectives, and to modify the SLR Framework to avert the adverse market consequences for the cleared derivatives markets.

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January 8, 2015
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We would welcome the opportunity to discuss our responses and views in greater detail. Please do not hesitate to contact Laura Harper Powell or the undersigned at +1 (202) 730-2600 with any questions the BCBS might have regarding this letter.

Respectfully submitted,

Stuart J. Kaswell

Stuart J. Kaswell
Executive Vice President & Managing Director, General Counsel

cc: Norah Barger, Senior Advisor, Board of Governors of the Federal Reserve System
Sviatlana Phelan, Board of Governors of the Federal Reserve System

The Hon. Timothy G. Massad, Chairman, U.S. Commodity Futures Trading Commission
The Hon. Mark P. Wetjen, Commissioner
The Hon. Sharon Y. Bowen, Commissioner
The Hon. J. Christopher Giancarlo, Commissioner

Bobby R. Bean, Associate Director – Capital Markets Branch, Federal Deposit Insurance Corporation
Karl Reitz, Chief – Capital Markets Strategies, Federal Deposit Insurance Corporation

Barbara Graf, Financial Markets Supervisory Authority (FINMA)

Amrit P. Sekhon, Director – Capital Policy, Office of the Comptroller of the Currency
Margot Schwadron, Office of the Comptroller of the Currency

Amias Gerety, Deputy Assistant Secretary for Financial Institutions, United States
Department of Treasury