A. Introduction

Deutsche Börse Group (DBG) welcomes the opportunity to comment on BCBS consultative document "Revised Basel III leverage ratio framework and disclosure requirements" issued in June 2013.

DBG is operating in the area of financial markets along the complete chain of trading, clearing, settlement and custody for securities, derivatives and other financial instruments and as such mainly active with regulated Financial Market Infrastructure providers.

Among others, Clearstream Banking S.A., Luxembourg (CBL) and Clearstream Banking AG, Frankfurt/Main (CBF), who act as (I)CSD[1] as well as Eurex Clearing AG as the leading European Central Counterparty (CCP), are classified as credit institutions and are therefore within the scope of the European Capital Requirements Directive (CRD) and Capital Requirements Regulation (CRR) which transpose i.a. the Basel III rules into European law. Clearstream subgroup is supervised on a consolidated level as a financial holding group.

However, all our group entities in scope of CRD/CRR and therefore Basel III rules (including the leverage ratio) are offering limited banking activities ancillary to their function as Financial Market Infrastructure (FMI). In order to operate as a Financial Market Infrastructure and in line with the dedicated regulatory framework (e.g. CPSS-IOSCO principles for financial market infrastructures as of April 2012) as well as generally recognised business practices, the business model of our group entities is risk averse, does not include a trading book / proprietary trading, allows loan business only in connection with clearing, settlement and custody activities for very short durations and in general on a collateralised basis and does not lead to intended financial leverage. Cash received out of the functions of our companies is based on the sole discretion of the clients[2]. It is invested with low credit risk and to a large degree without maturity transformation. Existing maturity transformation (strictly limited for CCPs) is done based on proper liquidity management principles and not driven by intention to gear net interest income. Contrary, interest paid on clients' deposits is very limited independent of the level of interest rates. For the CCP

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[1] (International) Central Securities Depository

[2] Margin/collateral requirements may be fulfilled by either cash or securities to the discretion of the client.

business collateral taken is the consequence of the general political preference for CCP cleared business especially for financial derivatives. In order to secure sufficient liquidity for the CCP function at any time a preference for cash collateral received in comparison to other forms of collateral (e.g. securities) is inherent in the business model. In addition due to highly automated processes operational risk is limited to the extent possible.

On the base of our dedicated business we see the need to reflect this adequately in the leverage ratio framework to the extent applicable to businesses like ours (e.g. for CCPs and/or CSDs with ancillary banking business being as legal entity in scope of the Basel rules).

In addition the G20 decided in their Pittsburgh meeting in 2009 to propagate central clearing and move as many OTC derivatives as possible to CCPs. In order to support this, clear rules to incentive centrally cleared transactions have been initiated, these include:

- Clear regulatory framework for central counterparties including proper supervision;
- Mandatory margining and even more stringent risk (position) management requirements for CCP transactions including default funds and lines of defense;
- Clearing obligations via CCPs for standardized OTC derivatives;
- Reduced capital charge for CCP cleared transactions compared to OTC cleared transactions;
- Additional capital charge (CVA) for non-centrally cleared derivatives;

The proposed approach of the treatment of derivatives business for leverage ratio dis-incentivises CCP usage in comparison to OTC cleared business and is therefore not in line with the general political target.

Our response to the consultation below is reflecting the dedicated business of our group entities and the adequate treatment of CCP business in particular. Moreover we raise a couple of comments related to unclear provisions or dedicated topics where we have a different view.

The document at hand contains a management summary in part B and specific explanatory notes in part C.

B. Management Summary

We have generally doubts that the non-risk sensitive leverage ratio with simple calculation basics and unique treatments will add benefits in limiting possible bank failures.

However we strongly support rather simple than complex rules for any kind of regulatory measures as the possibility to fulfil requirements and control the compliance is given to a higher degree of certainty. A flat and unique leverage ratio of e.g. 3% will unintentionally dis-incentivise low risk business and most likely harm risk reducing businesses / activities. As such we see the need to at least calibrate the ratio calculation in further areas which contradicts the general approach of simple and unique calculation.

Having said this we in general agree to the proposed treatment for on-balance sheet exposures and SFT businesses. Nevertheless we see the need for some adjustments with regards to the proposed SFT treatments.

Contrary we disagree to the proposal of the treatment of derivatives exposures. Moreover the dedicated role of centrally cleared derivatives as well as CCP business performed by a credit institution needs to be properly reflected. In addition we disagree to differing capital and consolidation approaches for the leverage ratio compared to the solvency regime.

All in all we have remarks with regards to the following topics:

- We support the idea of a flexible approach taking into account specific business models, as well as national characteristics;
- The capital base for the leverage ratio should be total regulatory capital instead of (Common Equity) Tier 1 capital;
- We see no good reason to create a completely new consolidation framework only for the purpose of the leverage ratio. There exists a regulatory framework which is used for various other regulatory ratios and we see no justification why this regulatory scope should not be applied to the leverage ratio as well. It is to be noted though the regulatory scope of consolidation is already diverting from the accounting scope of consolidation. We clearly disagree to define a third consolidation framework;

- The equal treatment of derivative positions regardless whether CCP cleared or not is clearly against the general political will to promote centrally cleared derivatives instead of bilaterally cleared OTC derivatives. The definition of a necessary adequate treatment demonstrates the difficulty to define a simple leverage ratio;
- Derivatives positions cleared with a CCP must be treated appropriately. Cross product netting should be possible for CCP cleared derivatives;
- There exist solutions for the CCP clearing which transfer any transaction on an item by item basis (gross transfer) or on a netted basis (net transfer). Therefore it should be secured that the treatment of CCP positions is done equally regardless of the underlying CCP concept if no economical difference exists;
- The treatment of derivatives positions cleared via a CCP should also be applied for such transactions which are originating from clients and are "passed through";
- In order to reflect the role of a CCP being itself in scope of the leverage ratio requirements, CCP positions of that CCP towards it's CMs clearly need to be excluded from the exposure measure;
- Furthermore the limitation of evaluating derivative exposures via Current Exposure Method (CEM) only is seen critical, therefore we support the proposed evaluation of other methods;
- For derivative transactions of Clearing Members (CM) on behalf of their clients via a CCP in a segregated model collateral passed through should be ignored for the exposure measure;
- For collaterals received by a CCP in scope of the leverage ratio rules require a specific treatment in order to allow such CCPs proper operations and should reduce in general the overall exposure value;
- We agree to treat Securities Financing Transactions (SFTs) equally regardless of the applicable accounting standard, otherwise the leverage ratio lacks on comparability. Nevertheless we see several details where adjustments are required;

- While we agree not to consider exposure reduction by collateral received, we disagree to increase exposures by the amount of any potential collateral value gap for SFT transactions. Uncollateralised transactions (i.e. uncollateralised placements) should not have a lower exposure value (E) than partially collateralised exposures (E + (E-C));
- The treatment of banks operating as agents in SFT transactions need refinement (e.g. treatment of guarantees which are fully collateralised, banks acting as agent without any financial guarantee, etc.);
- Disclosure of the leverage ratio should not be strictly on a quarterly basis. It should be in line with the disclosure of financial statements. Therefore national discretion on that topic must be possible to prevent the burden of the leverage ratio disclosure for smaller banks which are not listed and not required to prepare financial statements on a quarterly basis.

We cover these aspects, beside others, in part C below.

C. Specific explanatory notes sections

1. <u>Definition and minimum requirement:</u>

The continuing testing of the 3% minimum requirement for the leverage ratio is supported. A strict fixation of 3% as a Pillar I limit starting in 2018 might impact various business models to an unintended degree. Per se a more differentiated approach seems to be sound with less negative implications on the financial system.

Further, institutions with a balance sheet value that experiences high volatilities due to the specific businesses (volatilities must not be a source of additional risk) might suffer from a fix 3% limit. For example the balance sheet volume of our companies is depending on the cash behaviour of our clients which varies sharply within short timeframes depending on their settlement activities or cash collateral supply.

As qualitative criteria to be used to define the different levels of the limit we propose the business model (e.g. investment bank, retail bank, wholesale bank, CCP, CSD, etc.), the size of an institution, etc.

2. Capital base

We are in favour of the usage of total regulatory capital as capital base. From our perspective the coverage of assets is given by any component of the total regulatory capital. To exclude Tier 2 does not seem reasonable.

Nevertheless we support the further collection of data for quantitative impact studies to perform further calibration.

In case the capital base will be extended and Tier 2 instruments might be included as well, institutions which rely to a large extend or even fully on common equity tier 1 may not be dis-incentivised by increasing the overall limit or not reducing the limit for these institutions.

3. Scope of Consolidation

We see no justification to create another consolidation framework for the purpose of the leverage ratio only beside the already existing regulatory- and accounting consolidation. Therefore, we propose to use the regulatory consolidation which is already used for the solvency and the liquidity framework.

As this framework is focusing on the "financial" activities of any given group it seems also to be appropriate for leverage ratio purposes. "Financial" participations being not consolidated in line with the general regulatory consolidation framework are in principle deducted from equity. Participations outside the regulatory consolidation are on-balance sheet exposures and therefore included in the exposure measure of the leverage ratio. The proposed "look-through" of these investments to include additional "leverage" does not seem appropriate.

The scope of consolidation has implications on the capital base and the exposure measure.

The overall target to keep the leverage ratio framework simple should be followed to the extend possible. The creation of another scope of consolidation contradicts that approach in our view without material benefit.

If the regulatory scope of consolidation is deemed as being inadequate, the adjustment on the scope of consolidation should be done throughout the complete

regulatory framework and not only for leverage ratio purposes. However we do not see the need for such adjustments

Further, it should be considered that with the proposed scope of consolidation various subsidiaries must be included, e.g. insurance companies, which are excluded in regulatory consolidation for good reason. The inclusion of these subsidiaries leads to a situation where the leverage ratio is not a meaningful measure anymore as comparability is not given. The aggregation of these different exposures results in a misleading ratio, which could only be prevented if different exposures are treated differently with varying weights. This approach would be highly complex which contradicts once more a simple approach. Therefore including all these items in the scope of consolidation is not meaningful.

4. Exposure measure

a. General measurement principle:

In paragraph 16, bullet 2 it is stated that netting of loans and deposits is not allowed. For the sake of clarification we propose a clear statement that payables and receivables against the same counterparty in the same currency which are due (and can be settled net are shown net) in line with the accounting standard.

b. On-balance sheet exposures:

As the paragraph 19 is referring to assets we assume that provided collaterals still shown in the balance sheet are targeted for. However it is unclear whether the counter-position of received collaterals (which are liabilities) on the asset side are also meant. We ask to clarify the intended treatment in the final text.

Items which are deducted from Tier 1 capital are also deducted from the on-balance sheet exposure measure. We ask the Committee to exclude items which are deducted from Tier 2 capital from the exposure measure as well as these items are already covered by capital and the leverage ratio framework should not contradict the solvency regime.

In addition in case a CCP is in (consolidated) scope of the leverage ratio received cash collateral for initial margins and received contributions to the default fund should be deducted from the total assets as long as they are invested in line with the CPSS IOSCO recommendations for CCPs or their national implementations (for details see section 4.c).

c. **Derivatives:**

For derivative instruments it is stated in paragraph 22 that derivatives create two types of exposure: An exposure arising from the underlying of the contract and a counterparty credit risk exposure.

However, not all derivatives have an exposure towards the underlying of the contract, e.g. long CDS or long put. In these cases banks have even a "negative" exposure on these underlying as they gain profits if the market prices of the underlying are decreasing. We therefore kindly ask to clarify that the exposure from the underlying of the contract might be zero and therefore not existing.

From our perspective paragraph 25 should be amended as follows: In case derivatives are cleared via a CCP which is compliant with the CPSS IOSCO principles, the conditions on bilateral netting as set out in paragraph 8 of Annex I can be assumed as being fulfilled.

In addition the risk and leverage reducing role of a CCP should be taken into account by cross product netting with a CCP or indirectly via a Clearing Member of a CCP. It is important to note, that there exist various legal means on how CCPs step into a derivative (or other kind of) transaction: There are solutions which transfer (in different legal ways) any transaction on an item by item basis (gross transfer). Other soluttions only transfer net positions once a day (net transfer).

As the transfer is the legal basis for accounting, already the starting point for the exposure determination is different. As such, it needs to be secured that the treatment of CCP positions is done equally regardless of the underlying CCP concept if economically no difference exist.

While we agree to the purpose of paragraph 28 which lead to an alignment across different accounting standards we nevertheless want to point out the consequence of different presentation of same items. While under accounting standards which require continued presentation of collaterals given as on-balance sheet asset will result in a presentation of such items as on-balance sheet exposure, the same item as corrected by paragraph 28 will be shown in the derivative exposure caption. We therefore propose to align presentation in the same caption (a similar argument is true for corrections made for SFT exposures). We would prefer to show derivatives (and SFT transactions) together with the related collateral instead of showing collateral as an on-balance sheet item and the exposure in a different caption.

With regards to the indicated re-use possibility of collateral received (paragraph 26 second bullet) we want to point out that re-use of collateral might be limited or even not possible at all. Especially securities collateral received is often not available for re-use (e.g. collateral pledged). We therefore kindly ask to take this various options into account when phrasing the final rules.

With regards to CCP related client business collateral received from clients and placed with the CCP under a segregated model should not be part of the exposure measure. We therefore ask to include a correction measure to take that collateral independent from the relevant accounting standard and whether cash or non-cash collateral out of the exposure measure. In case our proposal would not be followed, derivatives transactions cleared indirectly with a CCP would receive in our view a double counting unintended (correctly at client level but in addition at clearing member level where it should be corrected).

For a CCP being itself in scope of the leverage ratio, received collateral to cover the CCP risk (initial margin and contributions to the default fund) are the consequence of the general set-up of that CCP. As derivative clearing via a CCP is the political preference such collateral should not increase the exposure measure of a CCP. This is in particular true for CCPs being compliant with the CPSS IOSCO principles are not allowed to place such received (cash) collateral with a material maturity mismatch (see principle 5 of the CPSS IOSCO principles for financial market infrastructures). We therefore propose to deduct the amount of collateral received and shown in the balance sheet from the exposure measure. Furthermore no grossing up should occur in case the collateral received is not shown in the balance sheet. As a consequence of the proposed above, equal treatment for CCP collateral of any kind is reached.

d. Securities financing transaction (SFT) exposures

Bank acting as a principal:

Our understanding regarding the treatment of securities received in an SFT transaction is described in paragraph 35 (ii) and should be red as followed: "…and recognised as an asset by the ~~transferor~~ transferee if the transferee has the right…". If our understanding is correct we are in principle fine with this correction. However the removal of the recognised asset should be done for collateral received and recognised in the balance sheet regardless if hypothecation is possible or not.

Uncollateralised placements are taken into account with their on-balance sheet value only. While we agree that in line with the concept of the leverage ratio collaterals received are not reducing the exposure value we however strongly disagree to increase the exposure value of SFT transactions by any portion which is not collateralised. This would not only dis-incentivise collateralised SFT transactions especially with regards to cash placements but also economically overstate the risk while in practise the risk is lower. This effect results out of the potentially add-on of the value difference of exposure versus collateral, i.e. the exposure value of an SFT may be E + (E-C) whereas the exposure value of an uncollateralised placement would be E only. Therefore we strongly disagree with the treatment of paragraph 35 (ii).

In addition we kindly ask to include in the final paper a clarification what is meant with E (Exposure) and C (Collateral) including the treatment of the valuation i.e. market value.

The proposed treatment of master netting agreements (in the following MNA) seems to be too restrictive for such kind of arrangements. It is quite common for SFT business and in particular for the securities lending market to collateralise a variety of loans (loan portfolio) with a pool of collaterals. Such collateralisation has various legal concepts and is not necessarily an MNA. As such the Committee should ensure that all kinds of similar agreements, which are legally enforceable in case of a borrower default, are treated the same. An artificial allocation of collateral is only the second best solution.

Bank acting as an agent:

Paragraph 37 assumes that in SFT transactions where a bank acting as an agent is generally providing an indemnity or guarantee for any difference between the securities or cash and the value of the related collateral. However to our knowledge at least two other models are frequently used:

1. The bank is only acting operationally as an agent and is not guaranteeing at all the value of any collateral or exposure;
2. The bank is guaranteeing the full amount of the transaction while being collateralised to 100% plus an adequate haircut.

While we do not see any need to include "exposures" out of models as described in number 1 we expect equal treatment of the economical subsense of exposures out of

models as described in number 2 with the proposed treatment of items as described (i.a. treatment in accordance with paragraph 38) in paragraph 37. In consequence only a remaining exposure value after deduction of the received collateral should be taken into account. Consequently the context of paragraph 39 needs to be adjusted.

Similar to our argumentation in the derivative exposure section we are also proposing a specific treatment for CCPs acting in the SFT business. In case such CCP itself has to achieve the leverage ratio the SFT position as such should not be included in the exposure measure at the CCP regardless of the accounting treatment. Furthermore any collateral received by such CCP should also be excluded from the exposure measure as described in the derivative section above.

e. Other off-balance sheet exposures

On other off-balance sheet items described in paragraph 40 to paragraph 42 shall be applied a 100% Credit Conversion Factor (CCF), with an exceptional treatment of 10% CCF for any commitments that are unconditionally cancellable at any time by the bank without prior notice (see paragraph 42). These unconditionally cancellable commitments are included in paragraph 41 as an off-balance sheet item. Paragraph 41 required for all off-balance sheet items a 100% CCF. Contrary paragraph 42 allows for a 10% CCF for "commitments that are unconditionally cancellable at any time". We see a potential conflict of the wording of these paragraphs and kindly ask to clarify the treatment precisely in the final text.

5. Disclosure requirements

For disclosure requirements we support a consistent and common disclosure of the main leverage ratio components and a common template for internationally-active banks.

In paragraph 48 the frequency of disclosure is set with the same frequency as the publication of financial statements. It is assumed in that paragraph that the frequency is quarterly or half yearly. However the majority of smaller banks, especially those which are not publicly listed and which do not issue publicly traded debt instruments are publishing financial statements only on an annual basis. It should be therefore clearly stated that in such cases an annual publication is seen sufficient. Else an

indirect obligation to publish financial statements more frequently would be the consequence which is outside of the authority of the banking regulatory framework.

With regards to the introduced disclosure rules in paragraph 49 we agree to the alignment of the disclosure of the different leverage ratio elements with the other Pillar 3 disclosures. However this needs to be limited as under the current Pillar 3 framework for the large (Basel) banks only.

Concerning paragraph 53 we repeat our position that the regulatory consolidation framework only should be used for leverage ratio purposes.

Another issue that shall be mentioned is the requirement to reconcile with public financial statements. Due to national accounting standards regulated (sub) groups of larger mixed groups might not be obliged to publish sub consolidated accounting figures (financial statements). As such no published accounting statements are available to compare leverage ratio data with. For such situation a description is needed for the respective treatment.

6. Transitional arrangements

We strongly support the Committee's intention to assess whether the proposed design and calibration of the minimum Pillar 1 leverage ratio of 3% is appropriate over a full credit cycle and for different types of business models. Moreover the assessment should also be used to derive the general benefit of the ratio as such. We clearly encourage the Basel Committee to consider also not proposing the leverage ratio becoming a Pillar 1 limit in case the on-going assessment does not give clear evidence for the benefit of such limit. In turn the assessment should not only answer the question on the "how" but also on the "if" related to the possible Pillar 1 limit as of 2018.

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We hope that our comments given are useful in the further process and are taken up going forward. We are happy to discuss any question related to the comments made.

Eschborn

20 September 2013

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