SwissLife

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

Zurich, September 27, 2012

<u>Consultation on Margin Requirements for non-centrally-cleared derivatives</u>

Dear Madam

Dear Sir

We appreciate having the opportunity to comment on the consultation paper.

General Remarks

Swiss Life Ltd. is an important life and pension insurance company domiciled in Switzerland with major business activities in Europe managing assets of more than CHF 120 billion. When managing these assets we carefully watch the counterparty risk. This was the reason why we substituted our former ISDA Agreements with threshold amounts against ISDA and CSA Agreements with full collateralisation on a mutual basis. This was accomplished well before the financial crisis brought risky tension into relationships with banks.

In the aftermath of the financial crisis and based on badly experienced difficulties to deposit our cash with a safe and sound counterparty, we started to successfully lobby for admission of insurance companies to the Swiss National Bank's Repo Market. Since 1st July 2010 we are admitted to and are an active member of the Swiss Repo market. This allowed us to considerably reduce the counterparty risk for cash positions.

The requirement to post initial margin, be it on a bilateral basis or via a CCP, triggers a new counterparty risk issue if not mitigated by adequate regulatory or legal measures. Especially for insurance companies with tied assets regulatory limits for counterparty risk apply which make it difficult to concentrate business on a few counterparties only, even more so if the initial margin must be deposited in cash.

We have selected the following questions which impact our business most:

Q22

Are the proposed requirements with respect to the treatment of provided margin appropriate? Is the proposed key principle and proposed requirement adequate to protect and preserve the utility of margin as a loss mitigants in all cases?

In our view the chosen approach to "*encourage* jurisdictions to review the local laws to ensure that collateral can be sufficiently protected in the event of bankruptcy" is much too weak given the fact that the CCP set-up is imposed by governments and regulators worldwide. We expect that an internationally coordinated regulation would set clear standards on a global scale in order to provide for a level playing field across all market participants, when trading OTC or ETD via CCP or on a bilateral basis.

If the higher safety for all market participants shall really be achieved when trading OTC, then also clear and uniform standards must be set for the custody of initial margin.

We clearly favour providing initial margin on a gross basis as otherwise - be it for bilateral trades or via CCP - nothing has been achieved in case of bankruptcy of a counterparty / clearing member. The lessons to be learned out of Lehman and MF Global do not only touch the level of the clearing entity but downstream to each individual customer and counterparty of such defaulting entity because they are the ultimate beneficial owners of the initial margin provided for their transactions.

Although we agree with the proposed requirement (initial margin on gross basis and no re-hypothecation or re-use of cash or non-cash collateral as initial margin) we clearly encourage IOSCO / BIS to make proposals how the minimum level of protection must be designed by local bankruptcy regimes and jurisdictions. The MF Global case has shown that although segregation was confirmed to clients, in fact it was not implemented. Especially in case of cash collateral a real segregation seems difficult unless deposited with a third party.

Q23

Is the requirement that initial margin be exchanged on a gross, rather than net basis, appropriate? Would the requirement result in large amounts of initial margin being held by a potentially small number of custodian banks and thus creating concentration risk?

Only initial margin on a gross basis ensures that in case of bankruptcy the customer providing the initial margin will be paid back in accordance with its rightful claims. Reference is made again to the MF Global case, where the court decided that segregated and non-segregated initial margin be distributed equally to customers. The concentration risk on a small number of custodian banks may be bearable if such banks do not engage

in volatile business (i.e. investment banking etc.) but offer custody services as their main or only business model or are at least legally separated from other business provided by the same banking group. The fact remains though, that big amounts of cash and securities in form of initial margin will be detracted from the markets and impact liquidity.

Q24

Should collateral be allowed to be re-hypothecated or re-used by the collecting party?

No. No automatic re-hypothecation or re-use by the collecting party should be allowed because otherwise the counterparty risk is no longer under the control of the beneficial owner of the initial margin. Initial margin segregated with a custodian bank must remain under the full control of the beneficial owner with regard to re-hypothecation or re-use. A formal agreement between the custodian bank and the depositor of the initial margin with the possibility of setting conditions (i.e. counterparty; rating of counterparty etc.) must be a prerequisite. However, the re-hypothecation or re-use must be an option on behalf of the depositor of the initial margin and by no means mandatory.

Q25

Are the proposed requirements with respect to the treatment of non-centrally-cleared derivatives between affiliated entities appropriate?

Yes, the proposed requirement that full variation margin shall be exchanged between affiliates is in our view appropriate. However, with regard to initial margin an internationally identical level playing field must be achieved. Giving discretion to local supervisors will lead to regulatory arbitrage and an unlevel playing field.

Q26

Should an exchange of variation margin between affiliates within the same national jurisdiction be required?

See answer to Q25.

Q27

<u>Is the proposed approach with respect to the interaction of national regimes in cross-border transactions appropriate?</u>

The proposed requirements illustrated by a variety of circumstances seem logic to us. It is important to firmly regulate this approach.

Yours sincerely
Swiss Life Investment Management Holding Ltd

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