JPMorgan Chase & Co.

Adam M. Gilbert
Managing Director

September 20, 2013

Via Electronic Submission to: baselcommittee@bis.org
Secretariat of the Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002 Basel, Switzerland

Re: Consultative Document: Revised Basel III leverage ratio framework and disclosure requirements

Ladies and Gentlemen:

JPMorgan Chase & Co ("JPMC") is pleased to provide comments on the Consultative Document regarding revisions to the leverage ratio framework (the "Proposal"). We believe that a properly calibrated, globally consistent leverage ratio is a prudent regulatory capital management tool and agree with the Basel Committee on Banking Supervision's (the "Committee") stated objective to reinforce the risk-based requirements with a simple, non risk-based "backstop" measure.

We support the views expressed in the comment letters being submitted jointly by the Global Financial Markets Association ("GFMA"), American Bankers Association ("ABA"), the Financial Services Roundtable ("FSR"), the International Institute of Finance ("IIF"), the International Swaps and Derivatives Association ("ISDA") and the International Institute of Banks ("IIB"), the "Joint Trade Group Letter" and by The Clearing House ("TCH"). Our comments and those in the industry letters are meant to help ensure that the leverage ratio remains a simple backstop that measures exposures in a reasonable fashion.

Specifically, our key concerns and recommendations are as follows:

- **Reserves held at Central Banks**
  - Inclusion of deposits with Central Banks in the denominator of the leverage ratio will have two undesirable effects from a policy perspective.
    - First, it will discourage banks from holding a high quality liquid asset thereby working at cross purposes with the Committee's Liquidity Coverage Ratio, another important prudential policy.

        - Second, it will encourage banks to turn away deposits especially during periods of market uncertainly when banks often experience an influx, as evidenced during the recent financial crisis.
    - JPMC therefore supports the view expressed in the Joint Trade Group letter and TCH letter that reserves held at Central Banks should be excluded from the denominator of the leverage ratio.

- **Derivatives**
    - The Proposed calculation for derivatives exposures is flawed in two fundamental respects:
        - First, the Proposal requires the use of the Current Exposure Method ("CEM") for the calculation of derivative exposures. CEM represents an inaccurate measurement tool for counterparty exposures, as has been well documented by the Committee. A more accurate measurement is achievable with an appropriately calibrated, revised Non-Internal Model Method ("NIMM").
        - Second, the Proposal does not currently recognize the use of legally enforceable cash collateral as an exposure mitigant. JPMC agrees with the Joint Trade Group and TCH letters' recommendations that recognition of full cash collateral netting is necessary to achieve a more accurate measurement of these exposures.
    - The Proposal will cause impediments to the Committee and Financial Stability Board's stated objectives of promoting more central clearing for derivatives because banks that are acting as clearing members will be required to calculate exposures and hold capital against both the client facing and central counterparty facing legs of centrally cleared trades.
    - At a minimum, JPMC believes that the leverage ratio should calculate exposure only on the client facing leg of centrally cleared derivatives, as is required under risk-based capital rules, provided that the bank does not guarantee the performance of the central clearing counterparty to their client.
    - The exposure measurement for centrally cleared derivatives should also utilize the NIMM methodology with full collateral netting. In addition, we believe that the inclusion of a shorter margin period of risk due to the expedited close-out process for these trades is appropriate. Client money rules and required segregation of funds further support two necessary adjustments to the exposure as the clearing member is unable to re-use this collateral to create additional leverage.
        - First, initial and variation margin received should offset the derivative exposure.
        - Second, any excess cash margin received by the clearing member from the client and held in a third party bank account on the client's behalf should be excluded from the exposure measure.

- The Committee has expressed concerns about banks' re-use of collateral received in bi-lateral derivative transactions to create additional leverage. JPMC supports the Joint Trade Group and TCH letters' observations regarding existing regulations limiting re-hypothecation. In addition, should the Committee continue to have concerns about this activity, we believe that these concerns would be better handled through direct regulation as opposed to the blunt gross up of the leverage ratio.

- **Written Credit Derivatives**
  - The Proposal's parameters for hedging (same name, same seniority and greater than or equal tenor) are too narrowly defined.
  - JPMC supports a broader recognition of hedging with regard to tenor, seniority and decomposition of indices as outlined in both the Joint Trade Group and TCH comment letters and believes that the positions taken in both comment letters more accurately reflect a bank's true exposure of written CDS under legally enforceable netting agreements.
  - As the Proposal attempts to equate written credit derivative exposures with cash loans and bonds, JPMC agrees with the Joint Trade Group and TCH comment letters that written credit derivatives exposures should be capped at the maximum possible loss to the bank, measured as the market value of the underlying reference obligation in order that written credit derivatives not be disadvantaged relative to their cash counterparts.
  - In addition, JPMC believes that purchased credit protection should be permitted to offset notional credit exposure on the same reference entity. Such an approach would recognize the contractual protection provided. This approach is consistent with the Committee's view that written credit protection represents exposure to the credit risk of the underlying entity. JPMC believes that it would be appropriate for the Committee to also recognize that purchased credit protection mitigates the credit risk of the underlying entity.

- **Securities Financing Transactions ("SFTs")**
  - The Proposal does not recognize the historically reliable contractual netting of payables and receivables in SFTs.
  - As a result, banks will be compelled to reduce activity or substantially increase pricing in this market.
  - Accordingly, the Proposal will have an adverse effect on liquidity in the financing markets for government debt and by extension the pricing thereof. This problem is especially acute if the leverage ratio is a binding constraint.
  - If banks reduce their activities in the SFT markets as a result of this Proposal, the implications for monetary policy initiatives would need to be considered and addressed.

- **Credit Conversion Factors ("CCF") for Off-Balance Sheet Commitments**
  - The Proposal uses inconsistent exposure measurement for unfunded commitments when compared to other recent regulatory rules[1] that have acknowledged 100% CCF measurement is significantly overstated.
  - JPMC therefore supports the view expressed in the Joint Trade Group and TCH letters that the CCFs recently enacted in connection with the Standardized Risk Based Capital Rules would provide for a simplified, more accurate measurement of these exposures.

JPMC appreciates the opportunity to comment on this Proposal and wishes to thank the Committee for its consideration of the views expressed in this letter. If you would like to discuss the contents of this letter or need additional information, please feel free to contact me at your convenience at 212-270-8928.

Respectfully yours,

Adam M. Gilbert
Managing Director
Head of Regulatory Policy
JPMorgan Chase & Co.

---

[1] BCBS Basel II Standardized Approach and BCBS: The Liquidity Coverage Ratio and liquidity risk monitoring tools (January 2013)