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VIA ELECTRONIC SUBMISSION (tfde@oecd.org)

Tax Treaties, Transfer Pricing and Financial Transactions Division

Centre for Tax Policy and Administration

OECD

Re: The OECD Progress Report on Amount A of Pillar One

The Global Association of Central Counterparties ("CCP12") is the international association for CCPs, representing 40 members who operate over 60 central counterparties (CCPs) across the Americas, EMEA, and the Asia-Pacific region.

CCP12 appreciates the opportunity to respond to the OECD Progress Report on Amount A of Pillar One[1] ("the Report"). We already commented on some of the aspects of the proposed solution to the tax challenges of the digitalisation of the economy in the CCP12 responses to the previous OECD consultations: the OECD Consultation Document "Pillar One – Amount A: Regulated Financial Services Exclusion"[2] of May 2022 and the OECD Public Consultation Document "Reports on the Pillar One and Pillar Two Blueprints"[3] of October 2020. With this submission, we would like to yet again comment on the scope of entities which should be exempted from the scope of application of Amount A rules.

As currently proposed, the Model Rules assume the exclusion from the scope of Amount A the revenues and profits from Regulated Financial Institutions ("RFI") which include Depositary Institutions, Mortgage Institutions, Investment Institutions, Insurance Institutions, Asset Managers, Mixed Financial Institutions, and RFI Service Entities. We consider, however, that the Consultation would benefit from an explicit exclusion of Central Counterparties ("CCPs") and the Exchanges they serve. We suggest an exemption for CCPs that are registered, regulated, authorised, or supervised in a jurisdiction or do not need to be registered, regulated, authorised, or supervised by virtue of falling outside the requirement to be so by the competent authorities.

CCPs are risk management entities at the centre of financial markets. They are highly regulated entities, with global standards, local legislation, and regulations which outline their governance, operational requirements, functions, and role in ensuring market transparency and fairness. The use of central clearing services provided by CCPs has been promoted by the International Monetary Fund ("IMF") and

[1] OECD, Progress Report on Amount A of Pillar One (July 2022), available at Link
[2] OECD, Public Consultation Document "Pillar One – Amount A: Regulated Financial Services Exclusion" (May 2022), available at Link; CCP12, Response to OECD Public Consultation Document "Pillar One – Amount A: Regulated Financial Services Exclusion" (December 2020), available at Link
[3] OECD, Public Consultation Document "Reports on the Pillar One and Pillar Two Blueprints" (October 2020), available at Link; CCP12, Response to OECD Public Consultation Document "Reports on the Pillar One and Pillar Two Blueprints" (December 2020), available at Link

the global financial standard-setting bodies ("SSBs"), following the G20 commitments to increase their use in the aftermath of the Great Financial Crisis of 2007-2009[4].

CCPs are risk-managers and "commitment mechanisms" and their "primary function (…) is to assure that clearing members meet their obligations in accordance with the CCP's rules"[5]. They are also commonly considered to be a part of "the "central nervous system" of the financial system. Clearing and settlement systems provide vital linkages among components of the system, enabling them to work together smoothly. As such, clearing and settlement systems are critical for the performance of the economy."[6] Recognising the principles and mechanisms they are based on and the fact that CCPs are essential for financial stability of the markets they operate in, CCPs have been entrusted with a special role of clearing of an extended range of financial instruments through the introduction of the clearing obligation.

It is the clear view of CCP12 and its members that the regulated central clearing space of finance is a sector where the policy challenges of digitalisation do not present themselves and that the OECD work would benefit from an explicit exclusion. Clarity around it would be beneficial not only for CCPs, but also Banking, Insurance, and Asset Management companies that are often the primary participants in the markets for which CCPs provide clearing services.

CCP12 believes that exclusion of CCPs is warranted on the basis of the following key attributes which correspond to the regulatory goals of the proposed taxation rules:

- <u>CCPs are highly regulated entities</u>, subject to <u>local regulatory requirements</u> in their home jurisdictions that are <u>consistent with international standards,</u> such as Principles for Financial Markets Infrastructures[7], that are driven by the G20, SSBs: CPMI, IOSCO and FSB, and other multilateral organisations. These requirements cover, among other things, governance, membership, operations, risk management, and geographical scope. Similarly to banks, a number of CCPs are also formally authorised credit institutions subject to additional prudential requirements.
  <u>CCPs are also very strictly supervised by their national competent authorities (which usually are their respective Ministries of Finance or Treasury, central banks, and financial supervisory commissions) on an ongoing basis</u>. In some instances, <u>the supervisory systems are multi-layer</u> (taking the European Union ("EU") as an example, on top of local supervisors, there are colleges consisting of foreign authorities' representatives and ESMA – the European Securities and Markets Authority, which have strong powers in the licencing and other decision-making processes). As a result of the existing regulatory and supervisory rules, <u>CCPs need a permission/licence for every service they intend to launch or extend and for every major change to their risk models and policies</u>. In cases they provide cross-border services, they are also scrutinised and monitored by the foreign authorities.
- <u>CCPs and their clearing members are also subject to strict global and local capital requirements</u>. The requirements for CCPs are embedded in their respective jurisdictions' laws (such as the European Market Infrastructure Regulation in the EU or the Dodd-Frank Act in the United States).

[4] G20 Leaders Statement: The Pittsburgh Summit (Nov. 2011), available at Link
[5] Robert T. Cox and Robert S. Steigerwald, Policy Discussion Paper "A CCP is a CCP is a CCP" (April 2017), available at Link
[6] Michael H. Moskow, "The role of central counterparties" (July 2007), available at Link
[7] CPSS, IOSCO, Principles for financial market infrastructures (April 2012), available at Link

They need to correspond to different types of risks CCPs are exposed to and to cover a part of the default waterfall which is provided by CCPs (so called "Skin-in-the-game"). The other elements of the financial resources pool maintained by CCPs are initial margins and default fund contributions which are assets posted by clearing members in order to guarantee the performance of the obligations resulting from the trades they concluded and to incentivise members to participate in the default management system run by CCPs in case one (or more) of the participants of the system fails to meet their obligations and becomes insolvent.

In terms of the minimum capital requirements for banks – the primary type of CCPs' clearing members – Basel III standards (a set of financial reforms developed by the Basel Committee on Banking Supervision) apply. Basel III was specifically developed to include capital calculations for CCPs, in part to incentivise centrally regulated risk management in opposition to bilateral exposures between banks. The Basel III framework encompasses also uncleared margin rules with the aim to reduce the risk of derivatives exposures.

In addition to it, in order to become a clearing member, a financial institution needs to meet certain minimum capital requirements which are set in the CCPs' rulebooks.

- The markets that CCPs serve include, amongst others:
  1. Government and corporate bond markets (primary, secondary, repo markets, and derivatives), including with Public Treasuries, Debt Management Offices, and Central Banks as members or participants;
  2. Equity markets (primary, secondary, securities financing markets, and derivatives markets); and
  3. Commodities markets (including cash-settled and physically settled and delivered agricultural goods and soft commodities, energy products such as oil and natural gas, and a wide variety of metals).

In addition to these primary considerations, we would note that if CCPs were to be considered in the scope, attention would need to be paid to the specific nature of CCPs' fee policies. CCPs interpose themselves between trades conducted by their members, acting as buyer to every seller and seller to every buyer. CCPs do not have positions of their own, but the entire members' trading volume is processed by the CCP. Thus, substantial technical consideration would be required to determine what the correct metrics, if any, would be for CCPs. This is compounded by the complexity and variety of ultimate clients – ranging from individual farmers to the world's largest insurers, pension funds, and asset managers – that clear business via intermediaries to CCPs.

We are of a strong view that the exclusion should be based on the merit of the policy priorities and the special role CCPs play in the markets. Excluding different types of financial institutions (which are participants of the same system and which enjoy the benefits of central clearing) but not financial market infrastructures such as CCPs, which are some of the most strictly regulated and supervised ones and which facilitate the functioning of the financial markets and make them safer, would create an unlevel playing field and an unjustified and very unwelcome gap in the rules. The lack of inclusion of CCPs (and other FMIs for that matter) in the definition of RFIs (or lack of an equivalent measure which would exclude CCPs from the application of the rules) would negatively affect the manner in which capital markets work, which, as we assume, would be an unintended consequence of overlooking these types of institutions in the proposed taxation rules.

The importance of the issue of an appropriate design of a taxation framework for CCPs has also been emphasised in the IMF paper “Applying the Central Clearing Mandate: Different Options for Different Markets”[8]. As the authors rightfully observe, “[i]t is important to consider these [domestic and international] tax issues when designing the CCP framework in order to ensure that the tax rules do not create market distortions and inefficiencies that could undermine the clearing process itself.” With that in mind, we call for an explicit exclusion of CCPs from the scope of application of Amount A envisaged under the Pillar One rules, as justified above.

[8] International Monetary Fund, “Applying the Central Clearing Mandate: Different Options for Different Markets” by John Kiff, Alessandro Gullo, Cory Hillier, and Panagiotis Papapaschalis, WP/22/14 (January 2022), available at Link

About CCP12

CCP12 is the global association for CCPs, representing 40 members who operate over 60 central counterparties (CCPs) across the Americas, EMEA, and the Asia-Pacific region.

CCP12 promotes effective, practical, and appropriate risk management and operational standards for CCPs to ensure the safety and efficiency of the financial markets it represents. CCP12 leads and assesses global regulatory and industry initiatives that concern CCPs to form consensus views, while also actively engaging with regulatory agencies and industry constituents through consultation responses, forum discussions and position papers.

For more information, please contact the office by e-mail at office@ccp12.org or through our website by visiting www.ccp12.org.

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Japan Securities Clearing Corporation	http://www.jpx.co.jp
JSE Clear Pty (Ltd.)	http://www.jse.co.za
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Korea Exchange	http://www.krx.co.kr
London Stock Exchange	http://www.lseg.com
Multi Commodity Exchange Clearing Corporation Limited	www.mcxccl.com
Minneapolis Grain Exchange, Inc.	http://www.mgex.com
Nasdaq Clearing AB	http://www.nasdaq.com
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New Zealand Clearing and Depository Corporation Limited	https://www.nzx.com/services/nzx-clearing
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