The Great Taking:
When the Derivatives Bubble Bursts, A “Protected Class” of Secured Creditors Will Take All Collateral

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The public is exposed to a monolithic vulnerability concentrated in the derivatives complex. This is an urgent matter. Triggers which could collapse this include large-scale insolvencies due to the sharp escalation of interest rates, or an event as sudden as the closing of the Strait of Hormuz.

Essentially all securities “owned” by the public in custodial accounts, pension plans and investment funds are now encumbered as collateral underpinning the derivatives complex, which is so large— an order of magnitude greater than the entire global economy—that there is not enough of anything in the world to back it. The illusion of collateral backing is facilitated by a daisy chain of hypothecation and re-hypothecation in which the same underlying client collateral is re-used many times over by a series of secured creditors.

It is now assured that in the implosion of the derivatives complex, collateral will be swept up on a vast scale. The plumbing to do this is in place. Legal certainty has been established that the collateral can be taken immediately and without judicial review, by entities described in court documents as “the protected class.” Even sophisticated professional investors, who were assured that their securities are “segregated,” will not be protected.

An enormous amount of sophisticated planning and implementation was sustained over decades with the purpose of subverting property rights in just this way. It began in the United States by amending the Uniform Commercial Code (UCC) in all 50 states. While this required many years of effort, it could be done quietly, without an act of Congress.

These are the key facts:

- Ownership of securities as property has been replaced with a new legal concept of a “security entitlement,” which is a contractual claim assuring a very weak position if the account provider becomes insolvent.
- *All* securities are held in un-segregated pooled form. Securities used as collateral, and those restricted from such use, are held in the same pool.
- *All* account holders, including those who have prohibited use of their securities as collateral, must, by law, receive only a pro-rata share of residual assets.
- “Re-vindication,” i.e., the taking back of one’s own securities in the event of insolvency, is absolutely prohibited.
- Account providers may legally borrow pooled securities without restriction to collateralize proprietary trading and financing.
- “Safe Harbor” assures secured creditors priority claim to pooled securities ahead of account holders.
- The absolute priority claim of secured creditors to pooled client securities has been upheld by the courts.

In 2005, less than two years before onset of the Global Financial Crisis, "safe harbor" provisions in the U.S. Bankruptcy code were significantly changed. "Safe harbor" sounds like a good thing, but the change was about making it certain that secured creditors can take client assets, and that this could not be challenged subsequently. This was about "safe harbor" for secured creditors against claims of customers to their own assets.

With these changes to "safe harbor" provisions, the transfer of customer assets to creditors previously considered to be fraudulent can no longer be challenged.

Further, it is now "legal" for the transfer of the public's assets to be made free-of-payment (FoP), as there is no requirement to show that reasonably equivalent value was received.

Comprehensive "collateral management" systems have been implemented, which assure automated transport of legal control of collateral to the Central Clearing Counterparties (CCPs) particularly in a time of "systemic stress." Certain secured creditors then take the collateral when the CCPs fail, having assured for themselves that their taking of assets cannot be "legally" challenged.

Is there a risk that CCPs might fail? CCPs assume counterparty risk between parties to derivative contracts. If a participant fails, the CCP assumes the obligations of the failed clearing participant. The CCP combines the exposures to all clearing members on its balance sheet.

The Depository Trust & Clearing Corporation (DTCC) operates two CCPs, both of which have been designated in the U.S. as Systemically Important Financial Market Utilities (SIFMUs). As of March 31, 2023, the consolidated Total Shareholder's Equity of DTCC was $3.5 billion. This is the entire capitalization underpinning the Central Security Depository and CCPs for the U.S. securities market and derivatives complex.

DTCC is clearly under-capitalized. However, the start-up of a new CCP is planned and pre-funded. This construct assures that certain secured creditors will take all collateral upon which they will have perfected legal control.

The objective is to utilize all securities as collateral and hence to have the practical means to take all securities as collateral. Collateral transformation is the encumbrance of all types of client securities under swap contracts, which also end up in the derivatives complex. This is done without the knowledge of the clients, who were led to believe that they safely owned these securities, and it serves no beneficial purpose whatsoever for the clients.

Urgent Congressional Action Required

That these legal constructs are in place now is irrefutable. Full explanation and documentation are provided in a PDF available for download at thegreattaking.com

Congressional investigation into, and remedies for these legal constructs is urgently needed!

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