

November 20, 2023

VIA ELECTRONIC SUBMISSION

Secretariat to the Financial Stability Board
Bank for International Settlements
Centralbahnplatz 2
CH-4002 Basel
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Re: Consultative report on Financial Resources and Tools for Central Counterparty Resolution

To Whom It May Concern:

CME Group Inc. (“CME Group”)¹ appreciates the opportunity to comment on the Financial Stability Board’s (“FSB”) Consultation report on *Financial Resources and Tools for Central Counterparty Resolution* (the “Consultation”).²

Chicago Mercantile Exchange Inc. (“CME”) is a wholly-owned subsidiary of CME Group. CME is registered with the Commodity Futures Trading Commission (“CFTC”) as a derivatives clearing organization (“DCO”) (“CME Clearing” or the “Clearing House”). CME Clearing offers clearing and settlement services for listed futures and options on futures contracts, including those listed on CME Group’s CFTC-registered designated contract markets (“DCMs”), and cleared swaps derivatives transactions, including interest rate swaps (“IRS”) products. These DCMs are CME, Board of Trade of the City of Chicago, Inc. (“CBOT”), New York Mercantile Exchange, Inc. (“NYMEX”), and the Commodity Exchange, Inc. (“COMEX”) (collectively, the “CME Group Exchanges”). On July 18, 2012, the Financial Stability Oversight Council designated CME as a systemically important financial market utility (“SIFMU”) under Title VIII of the Dodd-Frank Wall Street Reform and Consumer Protection Act. As a SIFMU, CME is also a systemically important DCO (“SIDCO”).

I. INTRODUCTION

CME Group appreciates the ongoing focus of the FSB—along with the Committee on Payments and Market Infrastructures (“CPMI”) and International Organization of Securities Commissions (“IOSCO”) (together, with the FSB, the “standard setting bodies” or “SSBs”)—on the stability of the broader financial system. The SSBs have provided a strong framework to support stability by, in part, promoting central counterparties’ (“CCPs”) resilience, which makes the possibility of a recovery or resolution event

¹ As a leading and diverse derivatives marketplace, CME Group enables clients to trade in futures, cash and over-the-counter markets, optimize portfolios, and analyze data – empowering market participants worldwide to efficiently manage risk and capture opportunities. CME Group’s exchanges offer the widest range of global benchmark products across all major asset classes based on interest rates, equity indexes, foreign exchange, energy, agricultural products, and metals. CME Group offers futures trading through the CME Globex platform, fixed income trading via BrokerTec, and foreign exchange trading on the EBS platform.

² Financial Stability Board, Consultative report, *Financial Resources and Tools for Central Counterparty Resolution* [hereafter, “Consultation”] (Sept. 2023).

remote. This framework includes the *Principles for financial market infrastructures* (“PFMIs”)³ adopted by CPMI-IOSCO and implemented by local-policymakers. Notably, since the implementation of the PFMIs, no CCP has failed and even before the PFMIs were implemented CCP failures were extreme outlier events.⁴ The inherent resilience of the CCP model calls into question the approach outlined in the Consultation of designing a bank-like resolution framework for CCPs, particularly where that framework, as proposed, negatively impacts the risk management incentives that are the building blocks of the central clearing model.

CME Group recognizes that CCPs must plan for remote events, as demonstrated by the comprehensiveness of their recovery planning, which was affirmed in the SSB’s report on *Central Counterparty Financial Resources for Recovery and Resolution* (“March 2022 Report”).⁵ However, planning for remote events, like a CCP’s resolution, should not undermine a CCP’s resilience, particularly market participants’ incentives to effectively manage their risks. As the FSB aptly stated in the Consultation, “[r]esolution planning should maintain incentives for CCPs, clearing members and market participants to centrally clear and to engage constructively in efforts to achieve a successful default management or recovery and to reduce the likelihood of resolution.”⁶ Promoting incentives for central clearing is also consistent with the G-20’s commitment to central clearing following the financial crisis.⁷

Notwithstanding the FSB’s objective, the Consultation’s proposals, if adopted, would undermine the risk management incentive-based success of the central clearing model. The quantitative analysis performed to date, including by the FSB, clearly demonstrates that the post-crisis reforms implemented to date are sufficient and additional resolution resources and tools are not necessary. The FSB ignores the results of this analysis that was undertaken using extreme and implausible scenarios and fails to provide any data or quantitative analysis supporting its proposals. Consequently, CME Group recommends that the FSB not adopt the proposals in this Consultation.

II. GENERAL COMMENTS

A. Policymaking should be based on data and quantitative analysis. A data-based approach demonstrates that resolution-specific resources and tools are not necessary.

Policymaking should be based on publicly available data and quantitative analysis. This is critical to ensure policymakers and the broader industry fully understand the costs and benefits of policy proposals

³ Committee on Payment and Settlement Systems (later renamed Committee on Payments and Market Infrastructures) and Board of the International Organization of Securities Commission, *Principles for financial market infrastructures* (Apr. 2012).

⁴ Cf. Federal Deposit Insurance, Failed Bank List (November 13, 2023) (noting that the rarity of a CCP failure contrasts with the more frequent occurrence of bank failures, where, according to the FDIC, 568 banks failed in the United States alone since October 1, 2000), available at <https://www.fdic.gov/resources/resolutions/bank-failures/failed-bank-list/>.

⁵ Financial Stability Board, Committee on Payments and Market Infrastructures, and Board of the International Organization of Securities Commissions, *Central Counterparty Financial Resources for Recovery and Resolution* [hereafter, “*March 2022 Report*”] (Mar. 2022).

⁶ *Consultation* at pg. 5.

⁷ Group of 20, Leaders’ Statement, Pittsburg Summit (Sept. 24-25, 2009), pg. 9, available at https://www.fsb.org/wp-content/uploads/g20_leaders_declaration_pittsburgh_2009.pdf.

and to identify areas for improvement. A data-driven approach to policymaking has long been a cornerstone of the SSBs' work⁸ and local policymakers' legal and regulatory frameworks. Unfortunately, the FSB did not embrace data-driven policymaking here, issuing a consultation that disregards the outcomes of the March 2022 Report, which made clear that CCPs were sufficiently resourced.

In particular, the data and quantitative analysis included in the March 2022 Report demonstrated the ability of CCPs to successfully manage extreme and implausible default loss and non-default loss ("NDLs") scenarios.⁹ The SSBs also explicitly recognized this lack of plausibility for default losses, stating that the "scenarios were intended to be significantly more severe than the 'extreme but plausible' standard set out in the" PFMI.¹⁰ In summary, the results from March 2022 Report were as follows:

- **Default Loss Scenario:**

In the case of default losses, no participating CCP entered resolution under the scenario evaluated where a 1.4x multiplier was applied to the CCPs' historical stress scenarios and four of the largest clearing members at each of the participating CCPs were assumed to have defaulted. Seven out of the 15 service lines for participating CCPs fully addressed the potential default losses via pre-funded financial resources, and of the eight CCP service lines that used recovery tools beyond the mutualized default fund, six were able to address the losses using their rules-based recovery cash calls. It was further noted in the March 2022 Report that where cash calls and variation margin gains haircutting ("VMGH") were employed, the analysis of the impacts on bank clearing members "identified only limited impacts on their liquidity and solvency from the use"¹¹ of such tools.

- **NDL Scenarios:**

In the case of NDLs, some of the participating CCPs entered resolution under one of two base scenarios: i) a CCP lost access to accounts at an institution (other than a central bank) holding assets on its behalf that would have caused the largest liquidity risk to the CCP and that institution's affiliated clearing members, if any, defaulted; or ii) a quantum of cash equal to the highest daily value of the sum of all cash transferred to any single institution on a single day was subject to cyber theft.

For the first NDL scenario, all CCPs were able to address the liquidity needs and did not enter resolution. The first NDL scenario was also evaluated considering the application of two additional complicating assumptions where the two clearing members generating the largest

⁸ See, e.g., *March 2022 Report* at pg. 25 (the FSB clearly recognizes the importance of quantitative analysis since the report states that "[j]urisdictions should determine and make transparent their approach to calibrating one or more resolution-specific resources and tools in the resolution toolbox, for both default losses and non-default losses, which will serve as an expected amount of resolution-specific resources and tools that can be relied upon for resolution"); Financial Stability Board, *2022 Resolution Report* (Dec. 2022), pg. 5 (the FSB states that the Resolution Steering Group "is analysing the need for, and **costs and benefits** of, potential alternative financial resources and tools for CCP resolution, alongside a comparison to existing resources and tools" (emphasis **added**)), available at <https://www.fsb.org/wp-content/uploads/P081222.pdf>.

⁹ See CME Group, Letter to the FSB-CPMI-IOSCO on the report on Central Counterparty Financial Resources for Recovery and Resolution (Apr. 2022), available at <https://www.fsb.org/wp-content/uploads/CMEGroup.pdf>.

¹⁰ *March 2022 Report* at pg. 1.

¹¹ *March 2022 Report* at pg. 3.

payment obligation also defaulted and the funds deposited to a settlement bank also became inaccessible mid-settlement cycle. For the first complicating assumption, all CCPs continued to be able to address the liquidity needs and did not enter resolution, and the same was true when applying the second complicating assumption for all but one CCP.

For the second NDL scenario, two CCPs' prefunded and recovery resources were sufficient to cover the theft of cash and resolution was triggered for the other CCPs.

The scenario analysis outlined in the March 2022 Report demonstrates that even in implausible scenarios, CCPs' financial resources and tools are sufficient to address the related potential losses. CME Group acknowledges that the NDL scenarios included in the March 2022 report resulted in resolution for certain participating CCPs, but implausible scenarios should not be the basis for requiring resolution-specific resources and tools for CCPs. These scenarios also did not account for the participating CCPs' operational arrangements and cyber security measures, which would further reduce the likelihood of the already-implausible scenarios occurring. CPMI-IOSCO's recent publication, *A discussion paper on central counterparty practices to address non-default losses*, also found that "[g]enerally, CCPs consider a range of NDL scenarios that may arise from risks relevant to their business activities, including general business risk, operational risk, investment risk, custody risk and legal risk."¹² The same publication also recognized that the historical data for severe NDL events is limited.¹³ This lack of historical data is a good demonstration of the effectiveness of CCPs' practices in addressing NDLs.

While covering a narrower subset of CCPs, the CFTC's supervisory stress tests have similarly demonstrated the sufficiency of CCPs' tools and resources to address extreme stress scenarios for default losses. For example, the CFTC's 2019 supervisory stress test report summarized the results of a reverse stress test of two CCPs, including CME Clearing, that showed that the CCPs had sufficient pre-funded resources to cover all clearing members with losses under the selected 1x historical stress scenarios.¹⁴ The same was true for all but one of the 2x historical stress scenarios.¹⁵ Notably, this supervisory stress test did not take into account the CCPs' ability to assess non-defaulting clearing members for additional resources, a material part of a CCP's recovery tools. The CFTC's 2016 and 2017 supervisory stress test reports reached similar conclusions with a broader set of CCPs participating.¹⁶

Because the Consultation lacks supporting data and quantitative analysis, while ignoring contradictory data in the public sphere, it may not provide relevant regulatory authorities in local jurisdictions sufficient basis to implement any of the proposals in the Consultation. For example, in the United States, the CFTC

¹² Committee on Payments and Market Infrastructures and Board of the International Organization of Securities Commissions, *A discussion paper on central counterparty practices to address non-default losses* (Aug. 2022), pg. 7, available at <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD709.pdf>.

¹³ *Id.* at pg. 8.

¹⁴ Commodity Futures Trading Commission, *CCP Supervisory Stress Tests: Reverse Stress Test and Liquidation Stress Test* (Apr. 2019), pg. 4, available at <https://www.cftc.gov/system/files?file=2019/05/02/cftcstresstest042019.pdf>.

¹⁵ *Id.*

¹⁶ Commodity Futures Trading Commission, *Supervisory Stress Test of Clearinghouses* (Nov. 2016), available at <https://www.cftc.gov/sites/default/files/idc/groups/public/@newsroom/documents/file/cftcstresstest111516.pdf>; Commodity Futures Trading Commission, *Evaluation of Clearinghouse Liquidity* (Oct. 2017), available at https://www.cftc.gov/sites/default/files/idc/groups/public/@newsroom/documents/file/dcr_ecl1017.pdf.

is required to consider the costs and benefits of any binding regulation before it is issued.¹⁷ The CFTC uses reasoned data and economic analysis to demonstrate that the benefits of any pending proposal exceed the costs. If the CFTC were to undertake a proposed rulemaking to adopt the Consultation’s proposals without adequate data-based analysis regarding relevant cost and benefits involved, its rulemaking could face a challenge under the federal Administrative Procedure Act.

B. Requiring resolution-specific resources and tools is inappropriate given the criticality of preserving the risk management incentives of the central clearing model and supporting financial stability.

The Consultation acknowledges the importance of mitigating adverse effects on financial stability and preserving incentives for market participants to participate in central clearing and recovery. However, it does not adequately recognize that establishing distinct resources and tools for resolution, regardless of type, risks promoting resolution over recovery and therefore, undermining financial stability. The Consultation also acknowledges “[a]s the cost magnitude of a resource increases, it could increase the cost of central clearing.”¹⁸ Indeed, these costs could also disincentivize central clearing and, in turn, undermine financial stability. This risk is unacceptable, particularly without any supporting data and/or analysis.

CCPs’ clearing services must be, and are, supported by comprehensive resources and tools to provide for their continuity. CCPs have carefully designed their risk management practices, including their resources and tools, to support incentives for market participants to effectively manage their risks.¹⁹ Preserving these incentives is critical to the continued success and resiliency of the central clearing model. In the case of default losses, maintaining dedicated resources and tools for resolution may undermine market participants’ incentives to actively participate in the default management and recovery processes. As part of their own cost-benefit analysis, market participants would likely consider the availability of these resolution-specific resources and tools, knowing that they could benefit from this additional layer of protection should the CCP enter resolution. The proposals outlined in the Consultation could make resolution more attractive, when, in practice, it should be the least attractive outcome to encourage successful recovery and the continuity of clearing services.

For default losses, these negative impacts on incentives are exacerbated in situations where resolution-specific tools and resources weaken the principle that those who take the risk, pay for the risk. This is particularly true in the case of the write-down of a CCP’s equity, since the CCP—a market risk neutral counterparty—would be fully bearing the costs.²⁰ Additionally, in situations where market participants bear the costs of resolution-specific tools and resources for default losses, such as additional cash calls in resolution, these increased costs risk incentivizing them to cease central clearing and either leave their exposures unhedged or, where possible, go to the bilateral markets. Similarly for NDLs, increasing the

¹⁷ 7 U.S.C. § 19(a) (Considerations of Costs and Benefits).

¹⁸ *Consultation* at pg. 11.

¹⁹ See CME Group, Letter to the FSB on the consultative document on Guidance on financial resources to support CCP resolution and on the treatment of CCP equity in resolution (July 2020), available at <https://www.fsb.org/wp-content/uploads/CME-Group-3.pdf>.

²⁰ Bail-in bonds, resolution funds, resolution-specific insurance, and resolution-specific third-party contractual support may present similar risks.

costs of central clearing by adding resolution-specific resources and tools to address events that are unlikely to lead to a CCP's resolution could disincentivize activity in cleared markets.

CME Group has similar concerns with the Consultation's support for early intervention by resolution authorities where recovery resources and tools are still available. Resolution should only occur where a CCP is, or is likely to be, no longer viable or able to meet applicable legal or regulatory requirements on a continuing basis or stability of the broader financial system is likely to be compromised. Early intervention by the resolution authority could create a crisis of confidence in the CCP and unnecessarily increase the risk of failure, which is the precise outcome that CCPs and policymakers have devoted tremendous efforts and resources to avoid. In this regard, the potential for a resolution authority to intervene early would diminish incentives for market participants to actively participate in the default management and recovery processes as explained above.

C. The flexibility of local policymakers to adopt regulatory frameworks tailored to their jurisdictions must be preserved.

While the data and analysis conducted by the FSB makes clear that mandated resolution-specific resources and tools are neither necessary nor appropriate, in the event the proposals from the Consultation are nonetheless adopted by the FSB, local jurisdictions must be able to tailor them to their legal and regulatory frameworks and the unique characteristics of the CCPs they supervise.²¹ This flexibility is particularly important for resolution planning given that legal and regulatory frameworks vary significantly across jurisdictions. For example, the CFTC uniquely requires SIDCOs to plan for not only their recovery, but the orderly wind-down of their clearing services, which is designed to effect the permanent cessation, sale or transfer of critical services.²²

III. Conclusion

CME Group appreciates the opportunity to comment on this Consultation. As set out above, we recommend against adopting the proposals contained therein. The lack of data and quantitative analysis supporting these proposals for resolution-specific resources and tools, coupled with the unacceptable risks to central clearing and financial stability, demonstrate that no additional policymaking is necessary or appropriate at this time.

²¹ See CME Group, Letter to the FSB on the consultative document on Guidance on financial resources to support CCP resolution and on the treatment of CCP equity in resolution (July 2020) (Noting that local authorities are most familiar with the unique characteristics of their CCPs and the legal and regulatory framework under which they operate. These unique CCP characteristics, such as products cleared, market participants served, customer protection regime, and ownership structure, among others, cannot be adequately taken into account by the SSBs.), available at <https://www.fsb.org/wp-content/uploads/CME-Group-3.pdf>.

²² 17 CFR § 39.39(a)-(b).

We would be happy to further discuss our comments with the FSB. If any comments or questions regarding this submission arise, please feel free to contact me at suzanne.sprague@cmegroup.com or Sean Downey, Managing Director, Chief Compliance Officer, Enterprise Risk Officer and Head of Policy at sean.downey@cmegroup.com.

Very truly yours,



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