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**Eurex Clearing
Response
to the**

FSB Consultative Document on

“Guidance on Central Counterparty
Resolution and Resolution Planning”

February 2017

Frankfurt am Main, 13.03.2017

A. Introduction

Eurex Clearing is a globally leading central counterparty clearinghouse (CCP). Eurex Clearing is a subsidiary of Deutsche Börse Group providing central clearing services for cash and derivatives markets both for listed as well as certain over-the-counter (OTC) financial instruments. Eurex Clearing actively contributes to market safety and integrity with state-of-the-art market infrastructure both in trading and clearing services, as well as with industry leading risk management services for the derivatives industry. Customers benefit from a high-quality, cost-efficient and comprehensive trading and clearing value chain.

Eurex Clearing AG is an EMIR authorized CCP incorporated in Germany. Eurex Clearing is also licensed as a credit institution under supervision of the Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin) pursuant to the Banking Act (Gesetz für das Kreditwesen). US Commodity Futures Trading Commission (CFTC) granted Eurex Clearing AG limited Registration as a Derivatives Clearing Organization.

Eurex Clearing highly appreciates the efforts of the FSB to provide establish global standards for resolution through its Key Attributes, and the particular guidance regarding financial market infrastructures (FMIs). Eurex Clearing proactively supports the introduction of resolution plans for CCPs and welcomes the increased level of detail of ongoing FSB and CPMI/IOSCO work, including this consultative document. The establishment of resolution plans is not only essential to account for the extremely unlikely possibility of actual activation of the plans, but also to enforce market discipline and risk management incentives on an ongoing basis.

This response is given in addition to industry responses from CCP associations, which are broadly in line with the Eurex Clearing position. As the consultation has noted that the FSB will consider whether further guidance is required, Eurex Clearing would like to highlight that additional work, not necessarily only in the form of guidance, could be very beneficial both to systemic risk management and financial stability cooperation across the FSB jurisdictions. We would welcome analysis and quantification studies in addition to experience drawn from CMGs and other oversight activities around resolution planning, and would be eager to contribute to such efforts.

B. Questions and Answers

Q1. On Objectives of CCP resolution and resolution planning

Answer:

Eurex Clearing agrees with the objectives laid out in the consultative document. We would however highlight that for 1.1 (ii), certain types of risk or loss distribution should not be mistaken for “contagion”. Indeed, CCPs are essentially built on mutualisation to enhance the stability of the CCP itself and its membership, as well as to create ex ante risk management incentives. Hence, while we agree with the objective of minimizing unnecessary or needlessly concentrated “contagion”, the word should not be deployed in future to undo or weaken mutualisation.

Q2. Resolution authority and resolution powers

Answer:

Eurex Clearing welcomes the guidance laid out in section 2 of the consultative document.

We want to highlight some views on the issues discussed as follows:

2.2: The Resolution Authority should also be permitted to maintain or enhance the risk management incentives of stakeholders by deviating from the presumed path to account for behavior of participants. For instance, unfulfilled default management process obligations, misleading price or market information, or other counterproductive actions from participants should be expected to lead to bearing a greater responsibility for loss coverage.

2.4 - 2.6: As an overarching suggestion to this portion of the guidance, we would stress using partial or full tear-ups as a back-up approach. In cases where participants are unable or unwilling to agree ex ante on loss allocation methods (such as additional cash calls or forms of margin haircutting), partial or full tear-ups should be designed and included in the CCP’s rules in such a manner that they occur at this level of agreed mutualisation. This provides both for clarity in approach, and makes explicit the ability of a market to decide a presumed level of continuity for the full market, and a sense for the degree and manner in which the balanced portion of the CCP, if any, will be continued. In cases where either private or public sector solutions can improve on this situation, they should be enacted in recovery and resolution.

We would also suggest that for 2.5 (ii) and 2.6 (ii), in cases where such tear-up pricing mechanisms failed, CCP rulebooks could benefit from including the last successful settlement price as a fallback. This would have the effect of turning the clock back or keeping stale prices under circumstances so volatile that all other methods have failed to yield a reasonably objective price.

Finally, for 2.6 (i) and (ii), we would stress that the “or” conjunction is essential to cover cases where ceasing to enforce contracts in a particular market segment or asset class in full, at consistent prices across the market at the same time, might indeed improve financial stability overall.

2.9: We would mention that it is conceivable that participants are willing to accept some more limited degree of certainty on the maximum amount, for instance the same degree that they consider their cleared portfolios could gain or lose based on market moves enforced by the CCP’s mechanisms absent any member defaults.

2.11: While we agree that jurisdictions should take due account of the financial stability and incentive to clear effects of initial margin haircutting, we would clarify that this is the case for all the recovery and resolution tools, and not exclusive to initial margin haircutting.

2.15: We strongly disagree with the need for “awards” or “compensation” to market participants who have contributed to the continuity of a service. The possible negative consequences of even an orderly wind-down on the (wider) business of the participants is the rationale for stressing the need to continuity. We fail to see why an award is warranted in such cases, especially in light of the fundamental role participants play in the ex ante structuring or risk management and supporting a CCP’s default management process. Such awards or compensation at the end of the waterfall can only harm incentives for prudent risk management.

Q3. Entry into resolution

Answer:

3.3: Eurex Clearing considers that public communication of resolution authority indicators can have a positive impact on the CCP eco-system. However, we would caution that in by definition unforeseen crisis required for such actions, the indicators published in the past may be out-of-date and care should be taken in the manner and definitiveness with which they are communicated.

3.4 (iv): Participant perception of a CCP’s operating ability is a key consideration, however we question whether authorities – who will be very closely engaged in monitoring a CCP – would not have an even better ability to judge and even create conditions for confidence.

3.6: We would suggest that authorities consider establishing, where they have not already done so, agreed formats of key information considered essential to such communications, to prevent increased complexity in a time of stress. This could also consist of explaining the format and information extracted by the CCP itself for default management processes or similar risk management, so as to prepare for rapid understanding of disseminated material.

Q4. Allocating losses to equity holders in resolution

Answer:

No Comment

Q5. No creditor worse off safeguard

Answer:

5.2, 5.5 (ii), 5.5 (iv): Eurex Clearing would like to stress that the key consideration for participants of the CCP is likely to be the consequences of a service closure, given the impact this has on their wider business. As such, we consider that the reference to “financial stability” in previous sections of this consultation includes the overall impact that a CCP closure can create if CCP trades are part of holistic trades, offset other exposures for the participant, or the effect that the lack of a central clearing mechanism has on future business and risk management. Thus, we consider that a purely CCP-payment related NCWO default loss counterfactual will dramatically undervalue continuity, as it ignores the real cost occurring to participants. Therefore, the NCWO threshold for CCPs, in particular 5.5 (iv), should be understood to incorporate much of the negative impact a wind-down would have for the participants.

We would stress that if participants have sought and benefitted from continuity as arranged by the CCP or a resolution authority, and they have elected to remaining a member of the CCP, then they have forfeited the right to any additional “compensation” under the NCWO safeguard.

We refer to our submission to the December 2016 FSB CCP discussion note as well as the EACH response to this guidance consultation.

Q6. Financial resources

Answer:

Eurex Clearing appreciates argumentation outlined in section 6. We would like to add some considerations in the context of temporary public funding.

The primary purpose of recovery and resolution planning, in general, as well as the move of OTC markets to central clearing, is to create conditions in which financial market participant failures do not require the use of public money. We therefore do not favour the idea to include the use of public money in recovery and resolution as outlined in paragraphs 6.5 to 6.9.

A rightly balanced incentive structure is the indispensable foundation of crisis proof functioning markets. The possibility of public money breaks centrally cleared market incentive structures. If participants can obtain public money for the continuity of “critical services” above and beyond what they themselves have contributed for risk mutualisation, then there will be a drive to weaken the commitments given to the CCP’s waterfall and rulebook.

In cases where public money is framed in resolution planning, we agree with the guidance that great care must be taken around the controls for its use, the consideration of its effect on incentives, and recovery methods. To this end, we would note that 6.6 at present appears to miss this primary concern: in determining the amounts to be recovered, the authorities should consider not only what participants would otherwise have been required to contribute, but also what the benefit of public funds was.

Additionally, we note that setting up a new CCP with market participant support is relatively easy, and thus authorities might find it difficult to enforce ex ante collection mechanisms unless these come with safeguards beyond the simple continuity of the CCP in question.

Q7. Resolution Planning

Answer:

7.5: Eurex Clearing would suggest that authorities also consider:

- both the types of information and the channels of transmission they may seek to use to communicate general information to the CCP’s participants and the public.
- how to obtain, interpret and use the information provided by the CCP (for instance, familiarity with the CCP’s default management factsheets, liquidity reports, etc.).
- how to compare, corroborate or evidence market conditions or views provided by participants on the situation and in particular how to draw these together to ascertain possible financial stability concerns or lack thereof.

Q8. Resolvability assessments and addressing impediments to resolvability

Answer:

8.2: Eurex Clearing would propose that authorities conduct such exercises based on scenarios they devise, to challenge and validate the risk management and recovery and resolution tool adequacy.

Q9. Crisis Management Groups

Answer:

9.6: Eurex Clearing would suggest including feedback and testing of such communications in the aforementioned crisis management exercises.

Q10. Cross-border effectiveness and enforcement of resolution actions

Answer:

Eurex Clearing believes in general terms that in order to treat all Clearing Members independent of their home jurisdiction equitably it is necessary to ensure that the CCPs rulebook and also resolution proceedings can be applied to all Clearing Members.

In this context, we believe the consultative document addresses the main points to be taken into account.

C. Closing

We hope that you have found these comments useful and remain at your disposal for further discussion. If you have any questions, please do not hesitate to contact:

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