LCH.CLEARNET

Financial Stability Board Secretariat
Bank for International Settlements
Centralbahnplatz 2
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Switzerland

Sent by email: fsb@bis.org

15 October 2013

Dear Sirs,

This paper provides the response of the LCH.Clearnet Group ("LCH.Clearnet") to the FSB consultation on the "Application of the Key Attributes of Effective Resolution Regimes to Non-Bank Financial Institutions" of August 2013.

Our response focuses on section I regarding the resolution of financial market infrastructures (FMI) and resolution of systemically important FMI participants and section II on client asset protection in resolution. The answers are specific to CCPs and do not address the other types of FMIs.

LCH.Clearnet is the world's leading clearing house group, serving major international exchanges and platforms, as well as a range of OTC markets. It clears a broad range of asset classes including: cash equities, exchange traded derivatives, commodities, energy, freight, interest rate swaps, credit default swaps, bonds and repos and foreign exchange derivatives.

General comments

LCH.Clearnet appreciates the importance of establishing effective resolution regimes for CCPs as, even if extremely unlikely, it cannot be excluded that a CCP's recovery measures could fail to restore it to viability and ordinary insolvency law would not meet the objective of preserving financial stability.

We would like to stress that resolution regimes for CCPs should be implemented consistently across jurisdictions to avoid competitive arbitrage and would urge the FSB to ensure that such consistency is achieved.

Responses to specific questions in Part I: Resolution of FMI and Systematically Important FMI participants

Q8. Are the conditions for entry into resolution of FMI (paragraph 4.3) suitable for all classes of FMI? What additional conditions (if any) would be relevant for specific classes of FMI?

We believe that primary responsibility for ensuring continuity of clearing services should lie with the CCPs and not the resolution authorities. The conditions for entry into resolution proposed in the report are suitable as they envisage that CCPs implement their recovery measures ahead of resolution while leaving enough flexibility to the authorities to intervene earlier if necessary.

Q16. Are the proposed classes of information that FMIs should be capable of producing (paragraph 12.1) feasible? Are any of the proposed classes of information unnecessary, duplicative or redundant? What additional classes of information (if any) should FMIs be capable of producing for the purposes of planning, preparing for or carrying out resolution?

CCPs should be able to produce the information suggested in the report except with respect to indirect participants. CCPs always hold information on direct participants (i.e. clearing members) but not necessarily on indirect participants (i.e. clients of clearing members). The European Markets Infrastructure Regulation[1] (EMIR) recognises this in article 33, whereby CCPs are required to disclose information on conflicts of interest arrangements to clients only where those are known to the CCP. We recommend that the requirement for CCPs to produce information on indirect participants only applies to the extent that CCPs have such information available.

Q18. Does the draft guidance achieve an appropriate balance between the orderly resolution of FMI participants and the FMI's ability to manage its risks effectively?

We believe that the appropriate balance is achieved. We agree that the CCP's rules should not hamper unnecessarily the orderly resolution of a participant and that a participant should generally be able to continue to participate in the CCP as long as it performs its obligations. However, we would like to highlight that there may be circumstances where local bankruptcy laws consider any delay in exercising the termination of a firm's participation to effectively be a waiver of such rights. In these circumstances the CCP cannot be expected to exclude the automatic termination of participation in its rules. We recommend that the final guidance recognises such cases.

Q20. Are the safeguards set out in the guidance (paragraph 1.3) adequate as regards the conditions and requirements for maintaining access of a firm in resolution or admitting as a new member an entity to which that firm's activities have been transferred? If not, what additional safeguards should be included in the guidance?

We have some comments regarding paragraph 1.3 (ii), which suggests that CCPs' rules 'should facilitate, for example, through a fast track application process, the participation of a third party successor or bridge institution that assumes particular functions or positions of the failing firm, subject to the maintenance of adequate risk control standards'. First, in order for the CCP to support the succession of a new member to the failing firm, we believe that the resolution authority would need to communicate to the CCP its intention to create a bridge institution or transfer some of the failing firm's functions to a third-party successor. Second, the authorities would need, in the period preceding the transfer, to provide the necessary support, including financial support to the failing firm so that margin calls made by the CCP are met. Otherwise, the

[1] Article 16 of EC Regulation 648/2012

CCP should exercise its right to declare the member in default. Expecting a CCP to not put a firm in default where it has breached membership terms creates a significant risk to both the CCP and the other members of the CCP. Third, it is essential that the fast-track application process takes into account the need for the CCP to perform sufficient due diligence so that it is comfortable that the new member meets the necessary requirements to participate in the CCP.

We would welcome a clarification on the intention of paragraph 1.3 (iii) that states that CCPs' rules should 'facilitate the transfer of positions of a participant in resolution to other participants of the FMI'. If the intention is to suggest that the CCP would port the positions of the member in default to another member, we would like to stress that this would contradict current legislation both in Europe and in the US. Pursuant to EMIR and Dodd-Frank, in the event of default of a clearing member, its cleared client activity and the related assets may be ported to a back-up clearing member. However, the clearing member's proprietary positions and related collateral must be liquidated in accordance with the requirements set out in those pieces of legislation. It would not be workable for a new legal regime to seek to override the porting outcomes which EMIR and Dodd-Frank provide for.

Responses to specific questions in part III: Client Asset Protection in Resolution

Q37. Is the proposed definition of 'client assets' (paragraph 2.1) sufficiently comprehensive? Are there any other classes of assets (in addition to those specified in paragraph 2.2) that should be excluded from the scope of this guidance?

We seek confirmation that the term client assets covers assets held outside a CCP. It is important in terms of ensuring the operation of CCPs in accordance with clearing regulation for the provisions set out in this paper in respect of client assets to not apply to assets held at a CCP. For example, in the UK "client assets" is usually understood in a UK law context to mean assets subject to the UK's client assets regime (the UK Financial Conduct Authority's CASS) which CCPs are not subject to.

Q39. Is the interaction between transfer powers and contractual porting arrangements or other arrangements under the rules of CCPs, exchanges or trading platforms (paragraph 3.3) sufficiently clear? If not, please explain what aspects might usefully be clarified.

As noted in response to Question 37, we do not believe that assets held at a CCP should be considered to be 'client assets' for the purpose of this consultation. If the drafters of the report, however, intended to cover assets held at a CCP, we would like clarification of the meaning of paragraph 3.3 and how it interacts with paragraph 1.3 of the section of the report on Resolution of systemically important FMI participants.

We believe that the transfer powers of a resolution authority should not interfere with the CCPs' porting arrangements. Under EMIR, the default of a clearing member triggers the right of a client to have its positions ported to an alternative clearing member. Therefore the transfer powers of a resolution authority can only be effective in circumstances where the CCP has not yet declared the default of a clearing member. Please see our answer to question 20 on paragraph 1.3(ii) on how best to prevent a default of a failing firm.

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Market participants, CCPs and regulatory authorities have invested a significant amount of time and effort to establish the porting arrangements necessary to comply with EMIR and Dodd-Frank and market participants would be in a situation of significant legal uncertainty if the transfer powers of a resolution authority could compromise the porting arrangements or the default rules of a CCP. The most effective way of ensuring transfer to a successor firm without interfering with established porting regimes such as EMIR would be to ensure that a firm is not declared in default by the CCP if a transfer is intended by the authorities.

Q48. Are the classes of information that firms should be able to provide promptly in order to facilitate the rapid transfer or return of client assets (paragraph 8.1) feasible? What additional classes of information (if any) should firms be capable of producing for those purposes?

As noted above, CCPs do not hold information on all indirect participants. In addition, CCPs are not able to trace client assets and collateral throughout the holding chain, in particular for indirect holding model. It would therefore be unreasonable to expect CCPs to provide the information listed under point i), ii), iii) and v).

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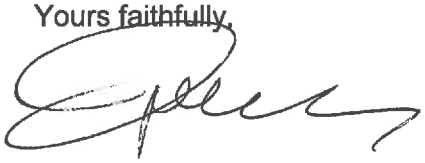
We hope that the FSB finds this contribution useful and we look forward to engaging further as policy options are developed. Please do not hesitate to contact Perrine Herrenschmidt at +44 (0)20 7426 7246 regarding any questions raised by this letter or to discuss these comments in greater detail.

Yours faithfully,



Jacques Aigrain
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