October 07, 2022

VIA ELECTRONIC SUBMISSION (Link)
Commodity Futures Trading Commission
Christopher Kirkpatrick
Secretary of the Commission
Three Lafayette Centre
1155 21st Street NW
Washington, DC 20581
United States of America

Re: CCP12 response to CFTC's Request for Information on Climate-Related Financial Risk

The Global Association of Central Counterparties ("CCP12") appreciates the opportunity to comment on the Commodity Futures Trading Commission's ("CFTC") Request for Information on Climate-Related Financial Risk ("Request for Information" or "RfI").[1]

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

CCP12 recognizes the importance of mitigating the potential risks and impacts of climate change. We therefore appreciate CFTC's initiative on this important topic and our thoughts and comments are presented in the spirit of achieving progress.

Introduction

At the outset, we want to emphasize that any work on climate-related financial risk will likely be more successful to the extent that it clearly recognizes the role of a given entity in the marketplace, as an entity's role impacts the way in which it considers and manages climate-related financial risk. Given that the RfI, for the most part, does not distinguish between entity types in its questions, we believe it is important to emphasize that one of the key roles of CCPs is to manage the risks arising from becoming the buyer to every seller and the seller to every buyer and thereby protecting investors and promoting financial stability in the markets. As you are aware, it is important, first and foremost, that any initiative addressing climate-related financial risk does not distract from or undermine a CCP's ability to carry out its important role in the marketplace and establish its own corresponding risk management practices. That said, we recognise that climate change has the potential to impact all participants involved in the clearing process – not only the buyers and sellers mentioned above, but also the intermediaries, other third parties and the CCPs themselves. Therefore, CCPs must regularly review and update (where necessary) their risk management frameworks that they recognise and adjust to any such impacts.

[1] CFTC, Request for Information, Climate-Related Financial Risk (Jun. 2022), available at Link

Specifically, we would suggest that any climate-related financial risk measures for CCPs should be consistent with the existing risk management principles and frameworks required of CCPs, as opposed to requiring them to implement approaches developed for other very different types of entities (e.g., banks, corporate issuers, and other categories of CFTC registrants). Moreover, requiring CCPs to prioritize the management of climate-related financial risks – which may be outside of the core risks they manage (e.g., market, credit, liquidity, and operational risks) and the typical period of risk for centrally cleared products – could compel CCPs to make trade-offs that may undermine their ability to perform their core risk management role in the marketplace as we describe in more detail below.

Risk Management (Questions 8 to 11)

Another key role of CCPs is to support the overall stability of financial markets. In practice, this means that the risks faced by CCPs must be recognised, foremost, and then mitigated. In order to accomplish this, CCP risk management frameworks must recognise and manage all emerging risks, including those posed by climate change. While many CCPs have made great strides in adapting risk management frameworks to address climate-related financial risk, we recognize that it is important that these frameworks continue to be reviewed in the light of the potential for more extreme weather-related events, such as those we have witnessed in recent years and that have pushed the boundaries of plausibility in "extreme but plausible" scenarios. See examples below of how CCP risk frameworks already mitigate some aspects of climate-related financial risk:

- CCPs' margin and stress testing methodologies are calibrated to ensure that adequate resources are held to cover the default of one or more counterparties during periods of extreme market volatility. To achieve this, CCPs use historical scenarios or simulations that include physical manifestations of weather-related events, in the calibration of these resources.
- CCPs' business continuity frameworks are designed to ensure technological and operational resiliency. With respect to climate-related financial risks, these frameworks already take weather-related events and their related consequences into account, based on historical experience and scenario analysis.
- Some CCPs are also developing their counterparty risk models to take environmental, social, and governance ("ESG") factors into account, thus impacting risk outcomes and participant eligibility.

We believe it is of the utmost importance that any work with respect to climate-related financial risks recognizes and builds upon the various practices that CCPs already employ to effectively mitigate and manage climate-related financial risk. In many instances, we believe the focus should be less on the origin and specifics of weather- or climate-related events and more on whether CCPs have put in place effective risk management practices to manage such events. Broadly, we believe that CCPs are best suited to appropriately design their risk management practices in a manner that captures the unique risks inherent in their role in the marketplace, including climate-related financial risks. This is in line with Principle 3 of the *Principles for Financial Market Infrastructures* (April 2012) ("PFMIs")[2], which states that "[a]n FMI should have a sound risk-management framework for comprehensively managing legal, credit,

[2] CPSS – IOSCO, Principles, Principles for financial market infrastructures (Apr. 2012), available at Link

liquidity, operational, **and other risks**" (emphasis **added**)[3] – note, the CFTC has also appropriately reflected this in its regulatory framework (e.g., CFTC Regulation 39.13(b)).

To illustrate this point, we note that CCP risk management frameworks already take into account both categories of climate-related financial risks – physical and transition risks – presented in the RfI:

> *Physical Risk:*
> The physical risks presented by climate change as identified in the RfI, such as weather events and the related consequences (and other operational risks), are already assessed and addressed by CCPs in their business continuity, disaster recovery, and operational risk management frameworks. The secondary effects stemming from these events, such as increased volatility, are also already recognized in many CCPs' financial risk management practices (e.g., margining and stress testing frameworks), where relevant to the products that they clear.
>
> *Transition Risk:*
> Similarly, the transition risks presented by climate change as identified in the RfI are already commonly recognized in CCPs' general business risk management frameworks to the extent that they would be impactful. It is important to emphasize that such transition risks would most likely occur over a longer period of time than the relevant period of risk for CCP's risk management (typically 1-5 days) as elaborated in the FSOC report[4]. Furthermore, while transition risks may also be relevant to specific products cleared, we believe that these risks are or will be priced into the market as they arise. More specifically, we believe it is important for the CFTC to recognize the short-term risk horizon of products cleared by most CCPs. Given this short-term risk horizon, it is highly unlikely that transitional climate-related financial risks would impact a CCP's financial risk management practices. Today, CCPs' margining and stress tests appropriately focus on the period of time that is commensurate with the margin and stress period of risk applied by CCPs, which typically varies from 1-5 days.

For the reasons stated above, CCP12 continues to support a principles-based regulatory framework for CCPs, such as the PFMIs and the DCO Core Principles (and their implementing regulations). The CFTC has a long history of embracing such a principles-based framework, which allow CCPs to effectively account for the unique risks related to the products which they clear, including climate-related financial risks. As referenced above, CCPs already employ a number of practices under these established principles-based approaches that account for climate-related financial risks. Consequently, defining granular requirements that are specific to climate-related financial risk may be duplicative and ignore the ways that CCPs have, and continue to, effectively address the risks for which they are exposed. We have noted several examples:

- *Collateral Treatment*: Requiring a CCP to provide preferential treatment to asset types that are considered "green", including through collateral haircuts or preferencing certain types of assets/issuers over others, would not be appropriate. While it may be appropriate for central banks to pursue this approach (subject to having a clear legal mandate to do so), CCPs should

[3] CPSS – IOSCO, Principles, Principles for financial market infrastructures (Apr. 2012), available at Link
[4] FSOC, Report, FSOC Report on Climate-Related Financial Risk (Nov. 2021), available at Link, figure 5.2, page 94

not be required, either directly or indirectly, to trade-off appropriately addressing market and liquidity risks, to address climate-related financial risks.

- *Period of Risk*: Requiring a CCP to change or modify existing risk horizons (e.g., margin period of risk or liquidation period) for the products cleared and the existing market structure the CCP serves, would also not be appropriate.
- *Add-on Charges/Credits*: With respect to the RfI's question whether CCPs' risk management frameworks should directly incorporate climate-related risk specific to clearing member firms or their clients, we believe that absent some clearly established interrelationship between a financial risk concern and a climate concern, this would be challenging from an equal access/treatment perspective for both cleared products and members.

Moreover, as has been recognized by the Commission, it is impossible for the CFTC or any policymaker to enumerate every risk type to which a CCP may be exposed. This is yet another reason that a principles-based regulatory framework is appropriate for management of risks, including climate-related financial risks.[5] In addition, it should be recognized that the varied and unique markets that CCPs' serve present unique climate-related financial risks, which cannot be effectively managed in homogeneously across all CCPs. CCPs require the flexibility that the CFTC's current regulatory framework affords to tailor their risk management practices to the unique risks inherent in their markets and the products they clear. Because of this and the fact that CCPs already employ risk management practices to address relevant climate-related financial risks, CCP12 does not believe that the CFTC should adopt additional regulatory requirements for CCPs that are specific to climate-related financial risks.

<u>Scenario Analysis and Stress Testing (Questions 4 to 7)</u>

In the context of CFTC regulations, CCP stress testing is used to size a CCP's financial resources to meet its financial obligations to its clearing members notwithstanding the default of the largest clearing member (commonly two largest clearing members) in extreme but plausible market conditions. As noted above, CCPs already have existing scenarios within their stress testing frameworks to address physical risks related to weather events and to appropriately respond to rising market volatility, including volatility resulting from these events. With respect to transition risks, it is highly unlikely there are short-term climate-related transition risks that are relevant to, or would likely be sufficiently significant for, stress testing. By definition, the transition risks described in the RfI – shifts in policy, regulations, customer and business preferences, technology, credit or insurance availability, or other market or social forces that can affect business operations – are unlikely to result in stresses that would reach the magnitude of "extreme but plausible" within a period of risk of 1 to 5 days. Any assumptions that such transition risks could arise during a 1-to-5-day period would likely be implausible, and therefore not suitable for or consistent with the objective of CCP stress testing. Practically speaking, even if a CCP *were* to include transition risk-related events in stress scenarios, the financial losses associated with those "plausible"

[5] *See* CFTC, Final Rule, Derivatives Clearing Organization General Provisions and Core Principles (Jan 2021), at pg. 4810 (noting, the CFTC specifically enacted changes to remove references to specific types of risks that a CCP must consider in margining, in an effort to emphasize that the risks noted are not exhaustive or meant to enumerate endless types of risk, but rather, that CCPs should be accounting for all relevant risks and have discretion with respect to how they identify, label, and address such risks), available [Link].

scenarios would likely be insignificant when compared to the other scenarios currently incorporated into a CCP's stress tests.

In sum, we believe that CCPs are best suited to appropriately design their stress testing frameworks and size their financial resources to capture the unique risks inherent in the products they clear, as is evidenced by their successful navigation of various stress events, both recent and historical ones.

Disclosure (Questions 13 to 17)

CCP12's members are aware of and have been evaluating the various climate-related and ESG disclosure frameworks and standards currently under development. There are various standards that CCP12's members may consider in their ESG frameworks, including: World Economic Forum's Measuring Stakeholder Capitalism[6]; ISO 50001:2018[7]; ISO 14001[8]; and the United Nations Global Compact[9], among others. As the work on climate-related disclosures is ongoing, there will likely continue to be differences in approaches to and standards for disclosure frameworks across global financial markets. This, in part, will be driven by the fact that certain disclosures will be relevant and meaningful for some types of businesses, customers or market participants, but not others. As such, CCP12 continues to emphasize that any approach taken by the CFTC related to climate-related financial risk-disclosures should be flexible (i.e., outcomes-based) to permit each CFTC-regulated entity, including CCPs, to use such data points and other information in the manner most appropriate to their roles in the marketplace.

Conclusion

CCP12 appreciates CFTC's engagement in this important topic and the opportunity to comment on this Request for Information. We look forward to continuing to work with the CFTC and other regulatory bodies towards our shared goal of secure and efficient markets and are available to further discuss our position as outlined above.

[6] World Economic Forum, Measuring Stakeholder Capitalism, available at Link
[7] ISO, Standard, Energy management systems – requirements with guidance for use (Aug. 2018), available at Link
[8] ISO, Standard, Environmental management, available at Link
[9] United Nations Global Compact, available at Link

About CCP12

The Global Association of Central Counterparties ("CCP12") is the international association for central counterparties ("CCPs"), representing 40 members who operate over 60 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.

CCP12 Members