

May 25, 2021

VIA ELECTRONIC SUBMISSION to [ccp.resolution.consultation@hmtreasury.gov.uk](mailto:ccp.resolution.consultation@hmtreasury.gov.uk)  
HM Treasury – Financial Market Infrastructure  
1 Horse Guards Road  
SW1A 2HQ London  
United Kingdom

**Re: HM Treasury Consultation on Expanded Resolution Regime: Central Counterparties**

**To Whom It May Concern:**

The Global Association of Central Counterparties (“CCP12”) appreciates the opportunity to comment on the HM Treasury’s (“HMT”) consultation entitled *Expanded Resolution Regime: Central Counterparties* (“the Consultation”).<sup>1</sup>

CCP12 is the global association for CCPs, representing 37 members who operate more than 60 individual central counterparties (CCPs) globally across the Americas, EMEA and the Asia-Pacific region. CCP12 has previously contributed input on this topic, for example to Financial Stability Board’s (“FSBs”) consultation on *Guidance on financial resources to support CCP resolution and on the treatment of CCP equity in resolution*<sup>2</sup> in 2019 and 2020<sup>3</sup>.

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<sup>1</sup> HMT, Consultation (Feb 2021), available at [Link](#)

<sup>2</sup> FSB, Consultation (Nov 2018), available at [Link](#) and FSB, Consultation (May 2020), available at [Link](#)

<sup>3</sup> CCP12, Response (Feb 2019) available at [Link](#) and CCP12, Response (Jul 2020) available at [Link](#)

**I. Responses to Specific Questions in the Discussion Paper****Q1. Do you agree with the proposed scope of our NCWO safeguard and counterfactual?**

The NCWO safeguard requires the counterfactual calculation of the result of a CCP's insolvency to be established. Consistent with the FSB's Key Attributes<sup>4</sup>, an appropriate NCWO counterfactual should be: (a) based on what would actually have occurred in a liquidation process if resolution had not commenced and all similarly situated creditors had been treated equally; and (b) a scenario in which hypothetical losses to creditors could be calculated with a high degree of certainty.<sup>5</sup> Therefore, the counterfactual requires an ex-post assessment of the losses that would have occurred under liquidation, assuming at least the full application of the CCP's loss allocation arrangements as defined under its rulebook and recovery plan. Consequently, under the NCWO safeguard, if the resolution authority departs from the CCP's rules and arrangements, participants to whom losses are allocated should be covered by the safeguard where the losses incurred in resolution exceed the losses that would have been incurred in liquidation from the full application of the CCP's loss allocation arrangements consistent with applicable insolvency law.<sup>6</sup>

However, as part of "the assessment of the losses that would have been incurred or the recoveries that would have been made if the CCP had been subject to liquidation", the HMT should clarify that these losses go well beyond those incurred only by the full application of CCP's rules and loss allocation arrangements, but also result from the applicable insolvency law (e.g. closing trades, replacing them, CCP going under the local insolvency procedure). Taking into account those additional financial costs would demonstrate to all relevant stakeholders the value vs. costs of continuity and provide them the necessary transparency in advance. On the contrary, a narrower approach to determining counterfactual, would expose resolution authorities to ex-post financial claims if resolution tools were to be used beyond those contractually agreed between the CCP and clearing members.

**Q2. What factors should be taken into account when calculating the quantum and position in the default waterfall of the second tranche of SITG?**

CCP12 is of the opinion that, a second SITG is not appropriate. We believe that a CCP's SITG is well calibrated to align incentives between the CCP and its members and we don't believe that additional exposure of a CCP's equity in either recovery or resolution phase is justified. CCP12 firmly believe that recovery/resolution already incentivizes CCPs to be fully engaged in doing what is needed to keep operating the business soundly and in the most efficient manner. The cornerstone of these incentives already includes putting CCP financial resources at stake in the form of SITG, or other features appropriate to the particular market and jurisdiction. It is encouraging to see that the HMT acknowledges that the CCP already contributes an appropriate portion of resources. As such we would like to echo the

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<sup>4</sup> FSB, Key Attributes (oct 2015) available at [Link](#)

<sup>5</sup> Key Attributes at 5.2 and PFMI Annex 6.1.

<sup>6</sup> Indeed, in the extreme circumstance where the resolution authority shall exercise its powers, the only possible mechanism that would achieve the desired outcome of protecting the market where the CCP operates and respect the NCWO safeguard is "(iii) transferring critical CCP operations to a bridge entity".

remarks from FSB's discussion paper on *Financial resources to support CCP resolution and the treatment of CCP equity in resolution*<sup>7</sup> that, "SITG is not calibrated with a view to constituting a significant amount of loss absorbing resources. Rather, SITG is calibrated to provide confidence in the risk management incentives of the CCP," which is consistent with CCP12's view that CCPs are inherently incentivized to employ prudent risk management standards, with or without SITG.

CCP's SITG size currently balances the goal of aligning CCP and clearing member interests and also ensuring proper incentives for clearing members to manage the risks they bring to the CCP, as well as participate in the default management process. As such, the amount of funding required from members is based on the risk they bring to the CCP. Likewise, the amount of funding from CCPs considers their market risk neutral position, meaning their contributions serve a different purpose than the contributions of clearing members. CCP SITG is determined by the CCP, considering the characteristics of the products it clears and the market participants it serves, as well the regulatory framework under which it operates. There is no "one-size-fits-all" approach to CCP SITG and it needs to be determined based on the totality of circumstances for that particular CCP. CCP SITG must be fit for purpose and neither CCPs nor international standards contemplate it being a significant loss absorbing resource. Therefore, the size of CCP SITG should not undermine the incentives for market participants to manage the risk they bring to the CCP. If CCP SITG is overly large, it will subsidize the risk taking of market participants, creating moral hazard concerns and distorting the fundamental CCP clearing model. This will weaken market participants' incentives to participate in the default management process, as they will consider CCP SITG and the potential for their own mutualization when constructing bids in a default management auction.

Notwithstanding the above, while CCP12 believes current CCP resources are appropriate, to the extent any additional resources are required, they should be covered through existing regulatory capital and should not be prefunded.

**Q3. Do you agree with the proposal to limit the statutory VMGH power to default loss scenarios, and instead have a larger cap on the cash call for non-default-loss scenarios?**

CCP12 would agree with limiting the statutory VMGH power to default loss scenarios which would mean that the resolution authority could use VMGH subject to the NCWO counterfactual.

CCP12 also agrees with having instead a higher cap on the cash calls for non-default losses in resolution. However, the higher cap on resolution cash calls should not be used to limit a CCP's recovery cash calls or prevent a CCP from implementing recovery cash calls.

**Q4. Do you agree with the proposed power to delay the use of resolution tools for up to 18 months and its current scope?**

CCP12 believes having the power to delay the use of resolution tools for up to 18 months could benefit the objectives of resolution and avoid adverse effects on financial stability.

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<sup>7</sup> FSB, Discussion paper (Nov 2018), available at [Link](#)

**Q5. Do you agree with the modalities of the proposed compensation process?**

CCP12 appreciates that the HMT recognizes the importance of considering the NCWO safeguard relative to the use of CCP equity given the dependence on applicable insolvency laws and individual CCP creditor circumstances and since any adjustment of CCP equity beyond what is stipulated in CCP rulebooks may give rise to legal claims. While CCP12 believes that the treatment of CCP equity under a CCP's rulebook should be respected, where the treatment of equity is adjusted in resolution in deviation of the rulebook, the impact to the NCWO safeguard must be considered in a manner that respects the insolvency claims hierarchy. Appropriately defining the NCWO safeguard helps all participants understand the economic value of continuity of clearing, compared to the cost of closing down the CCP. This comparison also helps to counteract the argument that participants would need to be compensated in a situation, where in fact they would be economically better off.

Against this background, CCP12 disagrees with the principle of compensating clearing members for tools utilized as a part of CCP recovery and resolution, particularly with equity in the CCP, beyond what is provided under the NCWO safeguard. The introduction of compensation beyond the NCWO safeguard has the potential to undermine the effectiveness of a CCP's recovery process, by, in part, creating an incentive on members to reduce the resources available in the CCP's waterfall and recovery process and hence precipitate the CCP into resolution. Such actions may skew the incentives of the participants to support the recovery in a way which limits the effectiveness of the recovery process. Similarly, it may adversely affect the efficacy of the resolution plan, where participants are not incentivized to act with a focus on financial stability. We also note that the FSB guidance states, "[c]reditors should have a right to compensation where they do not receive at a minimum what they would have received in a liquidation of the firm under the applicable insolvency regime."<sup>8</sup>

**Q6. What lead in time would be appropriate for industry to prepare for the new regime? Are there any elements of the new regime that would not require a lead in time?**

CCP12 believes the new regime should have at least 18 months for implementation; with special transition periods for specific provisions where appropriate, as this would allow CCPs, clearing members and clients sufficient time to prepare for the new regime.

**Q7. Do you have any other thoughts on the proposals that you would like to bring to our attention?**

CCP12 does not have comments on the proposals.

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<sup>8</sup> Key Attributes at 5.2.

## II. About CCP12

CCP12 is the global association for CCPs, representing 37 members who operate more than 60 individual central counterparties (CCPs) globally 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@ccp12global.com](mailto:office@ccp12global.com) or through our website by visiting [ccp12.org](http://ccp12.org).

## III. CCP12 Members

