

November 20, 2023

VIA ELECTRONIC SUBMISSION (fsb@fsb.org)
Secretariat to the Financial Stability Board
Bank for International Settlements
Centralbahnplatz 2
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Re: FSB Consultation report on Financial Resources and Tools for Central Counterparty Resolution

The Global Association of Central Counterparties (“CCP Global”)¹ is the international association for central counterparties (“CCPs”), representing 42 members who operate over 60 individual CCPs across the Americas, EMEA, and the Asia-Pacific region.

CCP Global appreciates the opportunity to respond to the consultation report on “Financial Resources and Tools for Central Counterparty Resolution”² (“the Report”) issued by the Financial Stability Board (“FSB”). We welcome the FSB’s ongoing efforts to support financial stability and confidence in the financial system, including through supporting the utilization of central clearing.

An enormous amount of work has already been done by the FSB and the other standard-setting bodies on CCPs’ resilience, recovery, and resolution. CCP Global previously provided feedback³ on the FSB’s “Key Attributes of Effective Resolution Regimes for Financial Institutions”⁴ (“FSB Key Attributes”), “Guidance on Central Counterparty Resolution and Resolution Planning”,⁵ “Financial resources to support CCP resolution and the treatment of CCP equity in resolution”⁶ (“2018 Consultation”), “Guidance on financial resources to support CCP resolution and on the treatment of CCP equity in resolution”⁷ (“2020 Guidance”), as well as on the consultative document entitled “Central Counterparty

¹ Previously known as CCP12.

² FSB, Consultation report, Financial Resources and Tools for Central Counterparty Resolution (September 2023), available at [Link](#).

³ CCP Global, Submissions, available at [Link](#).

⁴ FSB, Key Attributes of Effective Resolution Regimes for Financial Institutions (October 2014), available at [Link](#).

⁵ FSB, Guidance on Central Counterparty Resolution and Resolution Planning (July 2017), available at [Link](#).

⁶ FSB, Discussion paper for public consultation, Financial resources to support CCP resolution and the treatment of CCP equity in resolution (November 2018), available at [Link](#).

⁷ FSB, Consultative document, Guidance on financial resources to support CCP resolution and on the treatment of CCP equity in resolution (May 2020), available at [Link](#).

Financial Resources for Recovery and Resolution”⁸ of March 2022 (the “March 2022 Report”). In addition, and of particular note, are CPMI-IOSCO’s *Principles for financial market infrastructures* (“PFMIs”), which include obligations on CCPs to prepare appropriate plans for their recovery or orderly wind-down and, where applicable, provide relevant authorities with the information needed for purposes of resolution planning.⁹

It is vital to recognise what has already been accomplished by standard setters in making CCPs even more robust and to take these accomplishments into account. The work of the FSB should recognize the stability and resilience of CCPs, including in the most volatile periods and unprecedented stress market conditions (such as the COVID-19 pandemic and its associated effects, Russia’s invasion of Ukraine and the resultant geopolitical tensions and energy crisis, and multiple bank failures in 2023, to name just the most recent ones). The solid and robust foundations of existing CCP regulation, which have been agreed internationally and implemented locally, have proven to be effective and resilient.

CCP Global believes it is imperative not to undermine the effectiveness of the existing framework by potentially requiring tools and resources that could lead to disincentivizing the use of central clearing. Any further discussions and/or new or amended standards or guidance must take into consideration CCPs’ historical success and be supported by quantitative data and analysis that would justify a need for additional tools or resources. In our comment letter¹⁰ to the March 2022 Report, we pointed out that the results of even the extreme and implausible scenario analysis covered in the standard-setting bodies’ report affirmed CCPs’ resilience. We observed that overall, CCPs successfully addressed the covered scenarios for both default losses (“DLs”) and non-default losses (“NDLs”). The quantitative analysis conducted at that time by the FSB, along with CPMI-IOSCO, for the purpose of the March 2022 Report, clearly demonstrated that additional resources or tools for resolution were not necessary.

Unfortunately, the Report does not appear to take those results into account and fails to provide any additional empirical evidence or quantitative analysis that would merit changes to the existing framework for CCP resolution. We believe that any approach to policy-making that is not grounded in publicly available data and analyses is concerning and could result in unintended consequences. Indeed, many jurisdictions require publicly available data and analyses be provided to support proposed rulemakings. The Report clearly recognizes the importance of quantitative analysis, since it references several times the need for jurisdictions to calibrate the size of specific resources and tools, but it does not point out how the evidence and data gathering from the March 2022 Report was used to inform FSB’s proposed approach in this Report. As discussed above, we believe the quantitative analysis from the March 2022 Report makes clear that further resources or tools for CCP resolution are not necessary, and the Report states, “[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”.¹¹ This statement recognizes the

⁸ FSB, CPMI, IOSCO, Consultative document, Central Counterparty Financial Resources for Recovery and Resolution (March 2022), available at [Link](#).

⁹ CPMI, IOSCO, Principles for financial market infrastructures (April 2012); see Principle 3, Key Consideration 4 available at [Link](#).

¹⁰ CCP Global, response to the FSB, CPMI, IOSCO Report “Central Counterparty Financial Resources for Recovery and Resolution” (April 2022), [Link](#).

¹¹ FSB, Consultation report, *op.cit.*, point 4.23 at p. 25.

need for proper quantification, but does not demonstrate how data and analysis justify the need for such resources and tools. In light of the above, we would strongly urge the FSB to embrace a data-driven approach to policy-making in this area and include consideration of the results of their prior work on this subject (i.e., the March 2022 Report), and the robust framework for CCPs that is already in place (including their existing resources and tools), before making any additional recommendations.

Given the potential systemic implications of CCP resolution which FSB has acknowledged, policy-makers should focus on continuing to support CCPs' resilience and, ultimately, embracing practices that promote recovery over resolution. CCPs' risk management practices and robust recovery planning greatly mitigate the likelihood of an event leading to a resolution. Recovery, orderly wind-down, and resolution should be viewed holistically to avoid requiring CCPs to maintain resolution-specific resources and tools that could upset the careful balance of incentives that exists in central clearing today. The incentive structure of central clearing must be preserved for CCPs to be able to perform their core function of effectively managing risk. Therefore, the potential benefits of resolution-specific tools and resources that would be utilized only in a remote tail event¹² must be weighed against the potential for those tools and resources to undermine the business-as-usual ("BAU") central clearing model, particularly the incentives for effective risk management. Similarly, we are of the view that CCP recovery should be allowed to fully play out and warn against the potentially negative impacts of early intervention by the resolution authority, as this can undermine the incentives for market participants to actively engage in default management and recovery and create uncertainty as to how the CCP's rulebook will operate.

The impact of the tools/resources on clearing participants' incentives

We agree with the Report's statement that "[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."¹³ While we believe that maintaining incentives should be at the forefront of any FSB work, we are concerned that that is not the case based on the proposal for resolution-specific tools and resources in the Report. To the extent jurisdictions consider the adoption of resolution-specific tools and resources, they should carefully consider the impacts of those resources and tools on market participants' incentives to manage risk prior to, during, and after any recovery efforts. Consistent incentives are a prerequisite to successful CCP default management and recovery. As noted in our response to the March 2022 Report, CCPs' purpose is to manage the risk brought into the system by its participants, not to underwrite it. Resolution-specific resources and tools for DLs, particularly where they are funded by those that are not engaging in risk taking (as would be the case with bail-in bonds and CCP equity write-down, as discussed further below), could weaken or remove the incentive for participants to effectively support default management and recovery. This would put some of the core principles of central clearing, such as appropriate mutualisation and proper incentive structure, in

¹² The low probability of a CCP failure, the strength of the CCP waterfall, and the CCP resilience to NDIs have been also ascertained in the CentER Discussion Paper Nr. 2021-002, "Why Is a CCP Failure Very Unlikely?" by Dennis McLaughlin and Ron Berndsen (December 2021), available at [Link](#).

¹³ FSB, Consultation report, *op.cit.*, at p. 5.

question and thereby negatively impact financial stability.

For these reasons, we believe the FSB's proposed Parameters C and D relating to financial stability and preserving incentives for clearing are collectively the most important factors to consider when evaluating resolution-specific resources and tools. As such, we disagree with the Report's determination that "none of the parameters and their underlying analytical dimensions could be prioritised over others and instead all are essential in establishing an effective set of resolution resources and tools capable of addressing the various scenarios that could lead to resolution."¹⁴ As a simple illustration of our concern, resources could provide loss absorption (i.e., Parameter A) and be reliable (i.e., Parameter B), but undermine incentives for clearing (i.e., Parameter D) and, ultimately, financial stability (i.e., Parameter C). Thus, we believe the Parameters C and D and how they interact with each other should be weighted more heavily.

In addition to undermining incentives to participate in default management and recovery, the introduction of resolution-specific tools and resources may also raise the cost of clearing for clearing members and end-users, potentially reducing participation in cleared markets and eliminating hedging or moving it into opaque, uncleared markets. This is for example the case with user- or exchange-owned CCPs where the participants themselves would bear those additional costs. Raising the costs of clearing could also ultimately lead to decrease in the number of clearing members, leading to increased concentration in an already concentrated sector. We therefore urge the FSB to consider with caution the potential costs to cleared-market participants, over and above what is already accounted for under existing frameworks, that could result from the proposed resolution-specific tools and resources. The consideration of the full costs of the resolution-specific resources and tools is critical to avoid negatively impacting a CCP's resilience during BAU and therefore undermining financial stability.

DLs vs. NDLs

We note that DLs and NDLs are considered together throughout the Report, without appropriately differentiating between these two types of losses. The Report therefore apparently fails to reflect the results of the March 2022 Report that *did* distinguish the data gathered with regard to DLs versus NDLs, and the resources available to address these markedly different scenarios. In a DL scenario, CCPs' existing default waterfalls are designed to avoid resolution by fully allocating any resulting losses, primarily to market participants, creating incentives for them to actively participate in default management and recovery. Generally speaking, NDLs would not have a significant impact on a CCP's capital given the risk mitigating practices CCPs have in place based on their existing obligations under the PFMI (e.g., Principle 15, General Business Risk).¹⁵ In an NDL scenario, CCPs distinguish between the different sources of risk, including different sources of operational problems that may occur, and

¹⁴ *Ibid.*, at page 17.

¹⁵ CPMI and IOSCO note in their discussion paper on central counterparty practices to address non-default losses of August 2022 (available at [Link](#)) that "[t]he risk of a specific type of NDL materialising might be low due to the CCP's internal controls and other risk mitigants." at p. 7. Please see also "Why Is a CCP Failure Very Unlikely?", *op. cit.*, in particular: "In other words, an NDL loss event which exhausts both the Regulatory Capital held by the CCP and the annual profits held by the CCP has a very rare chance of occurring of about 1.5bps." at p. 16.

specify different resources and tools to address the facts and circumstances of the NDL scenario. These tools and resources are designed to respond to the probability and scale of risks in line with local regulations and authorities. At the same time, non-default types of risks are heterogeneous and do not necessarily result in financial losses (e.g., in some cases of operational or cyber risk scenarios). For such circumstances, no amount or source of additional financial resources would be helpful to address the non-default situation, nor would any of the proposed resolution-specific tools and resources help mitigate the risk.

Flexibility

Bearing in mind the above, we think that the FSB should predominantly focus on monitoring different jurisdictions' implementation of CCP recovery and resolution frameworks through the Crisis Management Groups of systemically important CCPs, as this would allow the FSB and local jurisdictions to continue to recognize the unique characteristics of individual CCPs and the legal and regulatory frameworks under which they operate. This would also serve as a way to gather additional empirical data, which we believe is necessary as described above. If, notwithstanding the foregoing, the FSB decides to move forward with a standard relating to resolution-specific tools and resources, it should ensure that any new toolbox remains flexible and appropriately designed for systemically important CCPs, allowing jurisdictions to continue to employ practices appropriate for the markets they oversee. This includes consideration of a variety of factors, such as their market structure, the relevant legal framework, and the business size and ownership structure of CCPs. This would in turn permit local authorities to take into consideration whether the existing wind-down frameworks of CCPs required in some key jurisdictions may achieve similar outcomes as the FSB's framework for resolution (i.e., to effect the permanent cessation, sale, or transfer of critical services). CCPs in these jurisdiction are also commonly required to have sufficient capitalization to wind down their businesses, which should be recognized.

It is also critical that any potential proposals aimed at modifying the resolution framework for CCPs be conducted in alignment and coordination with CPMI-IOSCO, where a number of supervisory authorities across jurisdictions participate, since the proposals being contemplated by the FSB impact the areas where CPMI-IOSCO has standard-setting authority, such as on incentives for market participants to participate in recovery. Cooperation among standard-setting bodies provides for holistic policy-making that achieves their shared mandate of supporting financial stability. Cooperation is paramount in all local jurisdictions' legal and regulatory frameworks. In some jurisdictions, the resolution authority is also the supervisory authority of the CCP (including, among others, Germany, Japan, Spain, and the United Kingdom) whereas in other jurisdictions the supervisory and resolution authorities are different entities (e.g., the U.S.). In jurisdictions where the supervisory and resolution authorities are not the same, coordination and communication between such authorities is particularly vital to understanding the relationship between resiliency, recovery, and resolution. For example, it may be the case that the supervisory authority would need to agree to adopt rules or approve CCP rulemakings in order to implement tools and resources to be included in a CCP's resolution toolbox. As the day-to-day supervisor of the CCP, the supervisory authority has a deep understanding of the CCP's risk management practices and recovery and wind-down plans, which they would have reviewed and this should be taken into consideration.

CCP Global comments to individual tools/resources

(i) Bail-in bonds

CCP Global would like to emphasize that CCPs are very different than banks. Among the fundamental differences between CCPs and banks are their roles, risk profiles, business objectives, credit and market risk coverage, risk management and lines of defence, collateral, transparency, and balance sheet structures.¹⁶ It is therefore critical not to view “CCPs through the lens of bank regulation”¹⁷ and not to apply to CCPs the same or similar practices stemming from the resolution framework applicable to banks. The bail-in bonds proposed in the CCP resolution toolbox resembles the total loss-absorbing capacity tool in the bank resolution framework. Because of the fundamental differences in structure and function of banks and CCPs, bail-in bonds would be inappropriate given that they potentially undermine CCPs’ organizational and incentive structure for central clearing, which has historically proven to be robust and reliable. Bail-in bonds would also turn CCPs into leveraged institutions akin to banks and alter their risk profiles. Additionally, this tool may be unavailable or impractical for certain CCPs based on their ownership structure, particularly for user- or exchange-owned CCPs.

If bail-in bonds were held by parties other than clearing members, this would significantly impact the incentive structure for central clearing. The success of the phases prior to resolution (i.e., BAU risk management, default management, and recovery) rely heavily on the current central clearing incentive structure, which includes appropriate risk mutualisation among clearing members as an incentive to participate. These incentives should not be disturbed or weakened by resolution-specific measures. Bail-in bonds may introduce resources from entities other than a CCP’s market participants to cover DLs, which creates moral hazard at the end of the waterfall by decoupling loss mutualisation from continuity of access. Moreover, transmitting losses to participants outside the CCP and its clearing members could increase contagion risk while at the same time not supporting effective CCP risk management, default management, or recovery. If, on the other hand, the buyers of bail-in bonds were clearing members of the CCP, then this could also create a disincentive for them to participate in default management or recovery, since the conversion of the bail-in bonds to equity would provide the holders with an ownership stake following resolution, which would become a part of these members’ cost-benefit analysis in a DL scenario. With bail-in bonds, the CCP would also bear the ongoing costs of the debt issuance for an extremely remote tail event. Ultimately, this would increase the cost of central clearing and discourage the movement towards cleared markets, which is supported by policy-makers globally.

Another potential negative impact of creating a tool such as bail-in bonds, which would only be used when a determination is made that resolution is necessary, is that it creates a new friction for making that determination. The already difficult – and time-sensitive – process of determining when recovery has failed and resolution is required may be further complicated and delayed by the bail-in bond holders’ push back, potentially giving rise to “no creditor worse off” claims.

¹⁶ Please refer to two publications: (1) Reserve Bank of Australia, “CCPs and Banks: Different Risks, Different Regulations” by David Hughes and Mark Manning (December 2015), available at [Link](#); (2) Federal Reserve Bank of Chicago, “A CCP is a CCP is a CCP”, by Robert T. Cox and Robert S. Steigerwald (April 2017), available at [Link](#).

¹⁷ “A CCP is a CCP is a CCP”, *ibid.*, at p. 1.

(ii) Resolution fund

While certain jurisdictions utilize resolution funds for the banking sector, this approach is inappropriate for CCPs. As recent events have demonstrated, bank failures are a more common occurrence as compared to CCP failures, which are rare (i.e., only a limited number of CCPs have failed and the most recent was almost 40 years ago). Considering the negative effects of resolution funds on incentives and their significant associated costs, we caution against creating a resource for CCP resolutions that is not fit for purpose.

We believe the coordination issues involved in establishing a resolution fund – particularly but not exclusively a supranational fund – are likely insuperable. Among the questions that would need to be resolved would be how to size the fund, who would pay for it, what the size of required contributions would be relative to each CCP covered (taking into account different levels of risk for different markets and asset classes), whether there would be membership standards for such a fund, and how authorities would coordinate the administration of the fund. These elements would make the implementation of a resolution fund very challenging. Also, DL and NDL scenarios would likely have to be considered separately in the resolution fund context, which would add another layer of complexity and challenge to the process of designing and implementing such a fund.

Beyond the broad incentive impacts resolution-specific resources and tools would have as described above, it is difficult to determine the specific impact of the resolution fund on the incentive structure given the wide range of possibilities for how such a fund could work in practice. Generally, if the fund was to be financed by CCPs' contributions, it would undermine the incentive structure for central clearing by disincentivizing market participants from actively participating in default management and recovery, as described above. Regardless of how the fund would be structured, it would increase the cost of clearing as either market participants would pay for it directly or CCPs would likely need to increase clearing fees to finance it. For user- or exchange-owned CCPs, the costs of the resolution fund would ultimately be borne by the members.

The above further indicates that there would be a tension between some of the parameters and analytical dimensions, such as between Parameter A, Dimension 1 (sufficient loss absorption, purpose and usability), Parameter B, Dimension 3 (reliability and availability, legal and operational considerations), and Parameter C, Dimensions 5 and 6 (alignment of incentives and achieving outcomes consistent with FSB Key Attributes, magnitude and allocation and impact on business models and incentives).

(iii) Resolution-specific insurance

Insurance coverage as a resource in resolution, like other resources that separate the relationship between risk-taking and cost-bearing, could have negative impacts on risk management incentives, as described above. Insuring against DLs would be fundamentally incompatible with the incentive structure for central clearing, which focuses on loss mutualisation. Such a practice would change a CCPs' role from neutral risk managers to market participants' risk underwriters which, in turn, would negatively impact the participants' incentive to manage risks and participate in default management

or recovery, and thereby undermine financial stability.

While insurance is commonly used by CCPs today to address certain types of NDLs, depending on the underlying cause of the loss, it may not always be effective protection given that it could take time to receive the proceeds. Hence, we do not believe such insurance would be “reliable and readily available in resolution” (i.e., meet Parameter B).

- (iv) Resolution-specific third-party contractual support (e.g., letters of credit/performance bonds/advance payment guarantees)

In the case of a DL scenario, third-party contractual support would compromise incentives for market participants to actively participate in default management and recovery. Where the third-party contractual support is coming from a CCP’s parent, the CCP group would effectively become a risk underwriter, which would significantly change the role of a CCP, as described above. Where third-party contractual support is provided by a CCP’s parent, the different types of ownership structures and how this loss allocation tool could impact the entire group should be considered.

- (v) Cash calls reserved for resolution

Although the use of resolution cash calls (in addition to a CCP’s cash calls) is already provided for in some jurisdictions, this tool may also have negative impacts if used by a resolution authority in resolution. For example, additional cash calls in resolution could result in some clearing members’ withdrawing from the CCP, leading to heightened concentration risk and potentially undermining recovery tools. This tool also has the potential to exacerbate stress and increase contagion risk in already stressed markets. A further consideration is the need to ensure that, like cash calls in recovery, the size of any resolution-specific cash call be set in proportion to members’ contributions to the default fund, in order to avoid unanticipated liquidity strains and create appropriate incentives during the recovery phase.

- (vi) Statutory or contractual VMGH for resolution

Broadly, although some jurisdictions provide for the availability of VMGH in resolution, in addition to recovery, this tool has limited applicability and could potentially have negative impacts. VMGH is only appropriate for some OTC and listed derivatives¹⁸ markets and is not suitable for instruments such as repos and cash securities clearing. In discussing VMGH, the Report notes that “VMGH allocates costs to clearing participants that experience mark-to-market gains on their positions, which avoids allocating costs to clearing participants with mark-to-market losses (...).”¹⁹ This means that it allocates losses to just those participants who happen to be on one side of a particular market movement at a given CCP (i.e., participants may have exposures hedged outside of the given CCP), rather than more broadly across the entire diversified spectrum of participants (as would a cash call). For that reason, the amount of variation margin that can be haircut should be capped by using either financial or temporal limits.

¹⁸ Please note that it is essentially impossible to use VMGH for premium style options and these are often traded and cleared alongside as a portfolio with the ETD futures wherein the tool can work.

¹⁹ FSB, Consultation report, *op.cit.*, at p. 16.

(vii) Equity (to the extent not having absorbed losses prior to entry into resolution)

In terms of DLs, requiring that more capital be provided by a CCP already at risk of failure can limit potential risk management options and impede the CCP's ability to react to unprecedented market conditions. Further, any use of equity as part of the first set of tools during resolution could disincentivise market participants from actively participating in default management and recovery, particularly if other resolution-specific tools result in the receipt of equity by those market participants. Therefore, exposing more CCP equity in resolution would negatively impact the incentive structure put in place at CCPs, as described above, and create a threshold beyond which resolution could be preferable to market participants. It would also put more pressure on a CCP that is already distressed and, ultimately, have detrimental effects on financial stability. In addition, we note that in the case of CCPs that are user- or exchange-owned and operate as market utilities, this will raise clearing costs for members (ultimately passed to end-users).

Potential Additional Tool: Partial Tear-ups

In terms of the tools included in the Report, we note that at least one tool was omitted. Partial tear-ups were included in the FSB Key Attributes, 2018 Consultation, as well as 2020 Guidance, and we believe, to the extent the FSB moves forward with resolution-specific resources and tools, they should be considered and included in the resolution toolbox. The possibility that partial tear-ups may be used acts as an incentive for clearing members to participate in default management and recovery before any tear-ups are effected. Partial tear-ups also provide for the ability for the CCP to return to a matched book. Many CCPs' rulebooks already include the ability to perform partial tear-ups as part of the default management and recovery, but we also note that this tool is applicable to derivatives clearing and not cash clearing. We therefore believe the Report would be incomplete if it fails to include partial tear-ups in its assessment of resolution-specific resources and tools. .

About CCP Global

CCP Global is the international association for CCPs, representing 42 members who operate over 60 individual central counterparties (CCPs) across the Americas, EMEA, and the Asia-Pacific region.

CCP Global promotes effective, practical, and appropriate risk management and operational standards for CCPs to ensure the safety and efficiency of the financial markets it represents. CCP Global 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.

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CCP Global MEMBERS

