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VIA ELECTRONIC MAIL
Financial Stability Board
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Re: Guidance on Central Counterparty Resolution and Resolution Planning

CME Group Inc. ("CME Group") appreciates the opportunity to provide comments on the Financial Stability Board's ("FSB") Guidance on Central Counterparty Resolution and Resolution Planning Consultative Document dated February 1, 2017 ("Guidance").

CME Group wholly owns two central counterparties ("CCPs"). Chicago Mercantile Exchange Inc. ("CME Inc.") is a derivatives clearing organization ("DCO") registered pursuant to the Commodity Exchange Act and regulated by the Commodity Futures Trading Commission ("CFTC") in the United States. CME Inc. is a systemically important derivatives clearing organization ("SIDCO").[1] CME Clearing Europe Limited ("CMECE") is a Recognised Clearing House under the UK Financial Services and Markets Act of 2000 and an authorized CCP under EMIR, and regulated by the Bank of England. In addition CMECE is also registered as a DCO pursuant to the Commodity Exchange Act and regulated by the CFTC in the United States.

The CME Group CCPs offer clearing and settlement for all products traded on the CME Group Exchanges.[2] The CME Group Exchanges provide trading platforms for futures, options on futures, derivatives, and spot contracts and offer a wide range of products, including those based on interest rates, equities, foreign exchange and commodities. The CME Group CCPs also provide clearing for certain OTC derivatives and other services to third parties.

The Guidance is based on a framework that was designed to resolve banks.[3] But CCPs are not banks and are materially different than banks. CCPs and banks have different market structures and

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[1] On July 18, 2012, CME Inc. was designated as a systemically important financial market utility under Title VIII of the Dodd-Frank Act.

[2] The CME Group Exchanges include Chicago Mercantile Exchange Inc., Board of Trade of the City of Chicago, Inc., New York Mercantile Exchange Inc., Commodity Exchange, Inc. and CME Europe Limited.

[3] The Introduction of the Guidance seems to suggest that the Guidance would be read together with guidance issued previously by the FSB regarding the resolution of financial institutions and financial market infrastructures and that portions of such prior guidance may also apply to CCPs even if it is not discussed in the Guidance. This unclear

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perform different market functions. Unlike banks, CCPs have sets of enforceable rules that contractually obligate their customers (clearing members) to engage in default management and recovery efforts if clearing members default. CCP rules generally require each clearing member to post collateral that will be used if it defaults and to make (funded and unfunded) contributions to the CCP's default fund that may be used if fellow clearing members default and the losses resulting from such default exceed the funds of the defaulted clearing member that are available to the CCP, together with the CCP's corporate contribution to the default fund. CCPs are expected to have rules that fully allocate any remaining losses that exceed these resources. Commitments by clearing members to share the losses resulting from clearing member defaults create incentives that encourage clearing members to participate actively in a CCP's default management processes and recovery efforts. It is essential that CCP guidance preserves these incentives—none of which exist in the banking context. In light of these differences, the banking resolution framework is not an appropriate source to use as the basis for CCP guidance. The structure of this guidance should be revisited. Guidance that is drafted specifically for CCPs should surely preserve the incentive structures created by a CCP's rulebook to encourage default management and recovery of a CCP and avoid resolution.

CME Group supports efforts to develop standards to guide the development of principles based resolution strategies and plans for CCPs. The Guidance is, and should be, intended to address what happens in resolution; it should not create the need for resolution by weakening a CCP or its ability to recover.

We agree that the objective of CCP resolution should be to protect financial stability and ensure the continuity of critical CCP functions without exposing taxpayers to the risk of losses. An effective CCP resolution should also preserve the hierarchy of claims under the rules of the CCP and under the applicable insolvency regime. Furthermore, we strongly agree that "[e]ffective CCP resolution planning should have regard to maintaining incentives for CCPs, clearing members, and market participants to centrally clear and engage constructively in efforts to achieve a successful default management or recovery and reduce the likelihood of resolution."[4]

CCP clearing services are critical to the CCP's clearing members, the customers of the CCP's clearing members, the smooth functioning of the markets the CCP serves and the maintenance of financial stability. CCPs have a long history and an excellent track record of managing sizable and complex default events in periods of extreme stress and uncertainty. Thus, it is imperative that a CCP is and remains strong and resilient; this is the first priority. Recovery is the second priority. If a CCP operates under the strictures imposed on a systemically important CCP under regulations adopted to implement the Principles for Financial Market Infrastructures ("PFMIs") and has a well-reasoned recovery plan, resolution is a remote contingency. Therefore, it is imperative that resolution strategies should not impair effective and efficient day-to-day operations and should not interfere with the operation of a CCP's recovery plan.

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structure should not be the foundation for the important work of developing effective resolution regimes, which an RA will be tasked with implementing in a stressful and uncertain environment.

[4] FINANCIAL STABILITY BOARD, GUIDANCE ON CENTRAL COUNTERPARTY RESOLUTION AND RESOLUTION PLANNING (Consultative Document) § 1, (Feb. 1, 2017) ("Guidance"), *available at* http://www.fsb.org/wp-content/uploads/Guidance-on-Central-Counterparty-Resolution-and-Resolution-Planning.pdf.

Contrary to our shared objectives, we are concerned that the Guidance —if adopted as proposed— could compromise daily CCP operations and hinder the CCP's ability to default manage and recover from severe stress. Ironically, the Guidance could even create a need for resolution of a CCP that would be unnecessary if the strength and resiliency of a CCP and its recovery plan are not weakened by the Guidance. We do not believe that this is the intent of the FSB. In order for the Guidance to further our shared objectives rather than undermine them, we identify in this letter critical changes that must be made.

A. EXECUTIVE SUMMARY

1. CCPs MUST BE STRONG AND RESILIENT. THIS MUST BE THE FIRST PRIORITY.

We agree with the Guidance that "[e]ffective CCP resolution planning should have regard to maintaining incentives for CCPs, clearing members, and market participants to centrally clear and engage constructively in efforts to achieve a ***successful default management . . . and reduce the likelihood of resolution***."[5]

A strong, resilient CCP is the best defense against failure to the point of resolution. Systemically important CCPs subject to regulations that implement the PFMIs are required to hold resources sufficient to withstand stress in the markets they serve, including stress resulting in two or more clearing member defaults. To address those risks, CCPs maintain pre-funded financial resources—including performance bond, CCP contributions, and clearing member contributions—and default management plans.

CCPs have been in existence for more than 100 years and have a long history and an excellent track record of managing sizable and complex default events in periods of extreme stress and uncertainty. For example, during the financial crisis, defaults in the uncleared markets led to disorder and financial panic, but the cleared markets performed well. CCPs successfully managed all clearing member defaults by hedging, auctioning and liquidating the portfolios of the defaulted clearing members. CCPs satisfied the losses created by the default of any clearing member by utilizing only the defaulter's pre-funded financial resources held by the CCP. The performance of CCPs during the financial crisis can be attributed to good risk management practices, including sound margining, periodic stress testing and sizing of pre-funded resources. However, since the financial crisis, CCPs and regulators have further strengthened CCPs through, for example, requiring many CCPs to maintain financial resources that would cover the losses associated with the default of the two clearing members presenting the greatest exposure to the CCP, providing guidance on CCP margin systems, and requiring CCPs to develop recovery plans.

CCPs and regulators should prioritize maintaining the strength and resilience of CCPs. To that end, the resolution authority ("RA") should not have any powers over a CCP during business as usual in the name of resolution planning. As discussed below, if an RA has, and exercises, powers to reshape a CCP's legal structure, business operations, rules and arrangements (including changes to the CCP's risk and default management practices), and/or governance, such actions will likely

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[5] *Id*.

weaken a CCP in the ordinary course and the abilty of the CCP to recover. There is no evidence, however, that such actions would make resolution less complicated or costly.

2. CCP RECOVERY MUST TAKE PRIORITY OVER RESOLUTION. NEITHER RESOLUTION PLANNING NOR RESOLUTION IMPLEMENTATION SHOULD BE ABLE TO UNDERMINE CCP RECOVERY.

As discussed below, the proposed Guidance blurs the line between recovery and resolution. If adopted as proposed, the Guidance would undermine the ability of CCPs to recover and would interfere with business structures and operations designed for success in favor of structures designed to mitigate the cost of failure.

Each CCP should maintain a comprehensive, adaptable recovery plan that the CCP would be allowed to exercise and exhaust in the event of stress before the RA steps in. The PFMIs call for each systemically important CCP to prepare and maintain a recovery plan.[6] According to CPMI-IOSCO guidance regarding recovery for financial market infrastructures (including CCPs) ("CPMI-IOSCO Recovery Guidance"), "'[r]ecovery' concerns the ability of an [CCP] to recover from a threat to its viability and financial strength so that it can continue to provide its critical services ***without requiring the use of resolution powers by authorities***."[7] The CPMI-IOSCO Recovery Guidance further defines recovery to mean

> the actions of [a CCP], consistent with its rules, procedures and other ex ante contractual arrangements, to address any uncovered loss, liquidity shortfall or capital inadequacy, whether arising from participant default or other causes (such as business, operational or other structural weaknesses), including actions to replenish any depleted pre-funded financial resources and liquidity arrangements, as necessary to maintain the [CCP's] viability as a going concern and the continued provision of critical services.[8]

Under the CPMI-IOSCO Recovery Guidance, recovery tools in a CCP's recovery plan that impact clearing members and their customers should be transparent to help clearing members and their customers measure, manage and control their potential losses and liquidity shortfalls when electing to clear with the CCP.[9] We agree and believe that a CCP should include each of these recovery tools in its rulebook and in its recovery plan.

We also agree with the CPMI-IOSCO Recovery Guidance that a CCP's recovery tools should create appropriate incentives for participants of the CCP to "(i) control the amount of risk that they bring to

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6 CPMI-IOSCO, TECHNICAL COMMITTEE OF THE INTERNATIONAL ORGANIZATION OF SECURITIES COMMISSIONS, PRINCIPLES FOR FINANCIAL MARKET INFRASTRUCTURES § 3.3.8 (Apr. 2012), *available at* http://www.bis.org/cpmi/publ/d101a.pdf

7 CPMI-IOSCO, BOARD OF THE INTERNATIONAL ORGANIZATION OF SECURITIES COMMISSIONS, RECOVERY OF FINANCIAL MARKET INFRASTRUCTURES § 1.1.1 (Oct. 2014) ("CPMI-IOSCO Recovery Guidance") (emphasis added), *available at* http://www.bis.org/cpmi/publ/d121.pdf.

8 *Id.*

9 *See id*. § 3.3.6.

or incur in the system, (ii) monitor the [CCP's] risk-taking and risk management activities, and (iii) assist in the [CCP's] default management process."[10]

A CCP's recovery tools and recovery plan can only provide transparency and create appropriate incentives if the CCP's recovery plan is not undercut by the Guidance and by the CCP's RA. If a CCP experiences stress events that trigger its recovery plan, a CCP must be permitted to use and exhaust the recovery tools in its recovery plan. Guidance that permits an RA to step in while the CCP still has recovery tools available would undermine a CCP's ability to recover.

3. RESOLUTION IS THE LAST RESORT.

The Guidance is intended to address what happens in resolution; it should not create the need for resolution by weakening a CCP or its ability to recover. Any other outcome would undermine the objectives of the Guidance.

The RA must not interfere with the CCP's recovery plan. Any RA's resolution plan should assume that each of the CCP's tools were unsuccessful or unavailable. The goals of the RA should always be to preserve the continuity of critical CCP functions, financial stability and the hierarchy of claims under the rules of the CCP and under the applicable insolvency regime without exposing taxpayers to the risk of losses.

An RA should not have any authority to impose changes on a CCP until a stress event occurs that exhausts a CCP's recovery plan (and any wind-down plan) and the CCP is placed into resolution. If the RA is empowered to require that a CCP change its business model or risk management model to facilitate resolvability in anticipation of a potential stress event, that authority could increase the likelihood that the CCP may experience stress events and undermine the objectives of this Guidance. Furthermore, empowering an RA to have such authority could conflict with the authority of the primary regulator of the CCP, especially in jurisdictions where the primary regulator has exclusive jurisdiction over a CCP's clearing functions.

The powers of an RA should flow out of statutes and regulations adopted by the appropriate legislative and regulatory entities. As discussed below, CCP rulebooks are not an adequate substitution.[11]

As discussed above, we support the objectives of the Guidance. We provide comments below highlighting examples where the Guidance falls short of meeting the objectives. We welcome the opportunity to continue to work with the FSB to further develop guidance that advances our shared resolution objectives of protecting financial stability and ensuring the continuity of critical CCP functions without exposing taxpayers to the risk of losses and our shared resolution planning objectives of maintaining incentives for CCPs, clearing members, and market participants to centrally clear and engage constructively in efforts to achieve a successful default management or recovery and reduce the likelihood of resolution.

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[10] *See id*. § 3.3.7. *See also id.* § 3.3.8 to 3.3.11.

[11] *See infra* Section B.5.

B. OVERVIEW OF COMMENTS.

1. RESOLUTION PLANNING MUST NOT WEAKEN CCPS IN THE NAME OF RESOLVABILITY.

Like much of the Guidance, Section 8 is based upon a framework that was designed to resolve banks. Section 8 of the Guidance focuses on improving the resolvability of CCPs and suggests that the oversight, supervisory or resolution authority of a CCP should have powers to require a CCP to: change its rules and arrangements (including changes to the CCP's risk and default management practices); make operational, structural or legal changes; and/or make changes to the terms or operations of its links with other FMIs. This suggestion ignores the inevitable conflicts between the interests of the supervisory authority in fostering a CCP that operates efficiently in the interests of its direct stakeholders (clearing members, customers and the banking and payment systems) and the interests of an RA concerned about minimizing the costs of failure without regard to ongoing operations. In contrast to banking failures, CCP failures have been extremely rare. Furthermore, taxpayers bailed out banks in the financial crisis as a result of banks being risk takers. By contrast, no CCP needed a taxpayer bail out during the financial crisis as CCPs are in the business of managing—rather than taking—risk. Thus, a framework that was designed to resolve banks is not appropriate to use as the basis for guidance to resolve CCPs.

A proper cost benefit analysis is likely to demonstrate that empowering an RA to reshape a CCP's legal structure, business operations, rules and arrangements (including changes to the CCP's risk and default management practices), and/or governance to facilitate resolvability in anticipation of a failure is unwarranted. There is no evidence that resolution will be more complicated or costly in cases where a CCP is operating solely in accordance with traditional supervisory imperatives. Instead, such authority would jeopardize a CCP's ability to recover. Apart from war or other destruction of the basic infrastructure of the financial system, the most likely cause of a failure of a systemically important CCP is the simultaneous failure of four or more globally systemic important banks that are clearing members of the CCP. To address the risk created if clearing members default, CCPs have sets of enforceable rules that contractually obligate their customers (clearing members) to engage in default management and recovery efforts. Commitments by clearing members to share the losses resulting from clearing member defaults create incentives that encourage clearing members to participate actively in a CCP's default management processes and recovery efforts. It is essential that CCP guidance preserves these incentives—none of which exist in the banking context. An RA thus should not have any authority to impose changes on a CCP until a stress event occurs that exhausts a CCP's recovery plan (and any wind-down plan) and the CCP is placed into resolution.

2. EARLY INTERVENTION BY AN RA WOULD UNDERMINE THE OBJECTIVES OF THE GUIDANCE.

The Guidance contemplates that an RA should be permitted to step in when the CCP still has recovery tools that it could use. *See, e.g.*, Sections 2 and 3. We view an RA stepping in when the CCP has not yet exhausted its available recovery tools as set forth in its recovery plan to be "early intervention" by the RA. Early intervention by the RA would—by definition—preclude the CCP from recovering as set forth in the CCP's recovery plan.

As discussed above, by setting forth a CCP's recovery tools that could impact clearing members and their customers in the CCP rulebook, a CCP helps its clearing members and their customers measure, manage and control their potential losses and liquidity shortfalls when electing to clear with the CCP.[12] Setting forth such recovery tools in the CCP rulebook also enables the CCP to incentivize clearing members and their customers to participate in default management processes. As provided in the CPMI-IOSCO Recovery Guidance, recovery "tools that incentivise participants to participate in good faith and bid competitively in an auction of a defaulter's portfolio may increase the likelihood of the auction being successful."[13] Such participation is essential to CCP default management processes in the event of a clearing member default.

When a CCP designs its rules to incentivize clearing members and their customers[14] to participate in default management and recovery processes, it is intended that the CCP is the entity that would execute such rules should the need arise. As discussed above, it would be inappropriate for a CCP to anticipate that the RA would step in and use these tools.[15] Furthermore, CCPs have the most relevant expertise, are best suited to execute recovery tools and have a solid track record of managing sizable and complex default events in periods of extreme stress and uncertainty, resulting in excellent outcomes.

Any perception that an RA may intervene before a CCP utilizes and exhausts its default management processes and its available recovery tools creates a disincentive for the CCP's clearing members and customers to participate in the CCP's default management processes and in recovery. The Guidance could thus undermine even the best CCP default management processes and recovery tools and infringe upon the ability of the CCP to recover from a stress event. To meet the objectives of the Guidance, the proposal must be revised to avoid any possibility of the RA even attempting to take any action before the CCP exhausts its available recovery tools.

As proposed, the Guidance contemplates that an RA could step in long before a CCP exhausts its available recovery tools. For example, Section 3.4(iv) contemplates that the RA might step in if clearing member defaults occur and the relevant authorities determine that the CCP's participants no longer have confidence in the CCP's ability to manage risks effectively. An RA could thus step in before a CCP even triggers its recovery plan. The possibility that an RA could step in so soon could

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12 *See* CPMI-IOSCO Recovery Guidance § 3.3.6.

13 *See id.* § 3.3.10.

14 When conducting default management auctions of a defaulter's portfolio, CME Inc. supports including as potential bidders those customers of clearing members that possess the expertise, infrastructure and financial wherewithal to support reasonable bidding on the defaulter's portfolio ("qualified customers"). Inclusion of qualified customers in default management drills and in default management auctions has yielded aggressive and successful bids, hastening a CCP's return to a matched book. Qualified customers may be further incentivized to actively bid in the portfolio of a defaulted clearing member given CME Inc.'s recent adoption of variation margin gains haircutting rules for Base products that would extend to net portfolio gains of customers of clearing members if the relevant pre-funded financial resources and assessment are exhausted and CME Inc.'s book remains unmatched.

15 CPMI-IOSCO Recovery Guidance § 1.1.1.

well undermine the ability of a CCP to default manage and recover and creates tension with the CPMI-IOSCO Recovery Guidance (which expects CCPs to address comprehensively any uncovered credit losses and liquidity shortfalls) and CFTC Regulation 39.35(a) (which requires a SIDCO to "adopt explicit rules and procedures that address ***fully*** any loss arising from any individual or combined default relating to any clearing members' obligations to the [SIDCO]"(emphasis added)).

If the decision whether to step in is left to the subjective discretion of the RA, we believe it could undermine a CCP's carefully-thought out recovery plan. The text in Sections 3.1 and 3.4(iv) of the Guidance may provide such a standard; it should be modified to make sure that the RA will not attempt to act until a CCP's full recovery plan has been exhausted. The sequencing of these steps is crucial to avoiding resolution at all.

Early intervention by the RA itself would contribute to a lack of confidence. The entry by the RA would be viewed as a signal by the clearing members that recovery of the CCP has failed. Such entry by the RA would deter clearing members from participating in any further efforts to restore the CCP to a matched book and/or allocate losses resulting from clearing member defaults as there is no longer any incentive for clearing members and market participants to participate in auctions to restore a matched book after the RA enters. Furthermore, the RA's early entry would create incentives for market participants to stop meeting settlement obligations—resulting in more clearing member defaults and increased losses, further destabilizing the financial markets.

In some jurisdictions, early intervention by an RA before the CCP exhausts its recovery plan (and any wind-down plan) could violate property rights. An RA's powers and the RA's exercise of its powers must be done in a manner consistent with applicable law in order for an RA's actions to be effective and provide certainty.

In many jurisdictions, a CCP's recovery plan is developed ex ante in consultation with the CCP's supervisory authority. We support this process, through which the regulator familiarizes itself with the CCP's plan and provides feedback to the CCP regarding the recovery plan as needed. This is the appropriate time for a regulator to assess the effectiveness of a CCP's recovery tools and recovery plan—not by intervening during the CCP's implementation of the recovery plan.

3. ENTRY BY AN RA SHOULD REQUIRE THE APPROVAL OF A SEPARATE GOVERNMENTAL ENTITY, FOLLOWING DELIBERATION WITH OFFICIALS AT THE HIGHEST LEVEL OF GOVERNMENT.

The Guidance suggests that an RA, in consultation with other relevant authorities, should have the power and practical arrangements to place a CCP into resolution. *See* Section 3. We support the involvement of other relevant authorities in this important decision. Such authorities would provide broader perspectives regarding general economic conditions, financial stability and the CCP's role in the markets that would balance the RA's resolution-centric perspectives and possible proclivity to enter resolution prematurely and preempt a CCP's recovery.

However, separate governmental authorities should have a greater role than merely consulting with the RA in order to ensure that a decision that an RA will enter a CCP is balanced appropriately. The separate governmental entity should be required to approve the authorization for the RA to obtain powers over the CCP. First, the RA should submit to the separate governmental entity a written

request stating the reasons why the RA believes the resolution standard (set forth in the next sentence) has been met. Then, in order for the RA to place a CCP into resolution, the separate governmental entity must find based on clear evidence, which it will evaluate in deliberation with officials at the highest levels of government, that (i) the CCP's insolvency is imminent and no viable alternative exists to prevent such insolvency; (ii) absent resolution by the RA, the CCP would impose material risk to financial stability; and (iii) resolution by the RA would avoid or mitigate this risk.

This process of checks and balances could mitigate inherent conflicts of interest in a jurisdiction where the RA of a CCP is also the RA of banks and the RA is thus focused on maintaining the stability and public confidence in both CCPs and banks. In such jurisdictions, an RA might want to allow a CCP to fail if doing so could save a bank from failing or preserve franchise value of a failing bank. When acting as RA for a clearing member, the RA could work to preserve the franchise value of the bank rather than financial stability.

4. AN ABILITY BY THE RA TO ELECT WHICH CCP CONTRACTUAL OBLIGATIONS TO HONOR WOULD UNDERMINE THE OBJECTIVES OF THE GUIDANCE.

The Guidance suggests that the RA may depart from the general principle of equal treatment of creditors within the same class and order of loss allocation in accordance with the CCP's rules and arrangements (which could include changes to the CCP's risk and default management practices) if necessary to achieve the resolution objectives or maximize value for all creditors.[16] Any ability (or perceived ability) by the RA to elect which contractual obligations to respect and which to ignore when the RA intervenes would inhibit clearing members from measuring, managing and controlling their risks when electing to clear with the CCP. Furthermore, such ability would create perverse incentives—this would not encourage clearing members and their customers to engage in the default management processes of the CCP during business as usual or in recovery. This could be another aspect of the Guidance that inadvertently leads to resolution at the expense of recovery.

Some CCPs may become the subject of a bankruptcy proceeding after being placed into resolution. In order for an RA's actions to be effective and provide certainty, an RA's actions would need to be permitted and/or upheld by the bankruptcy court. However, in at least some jurisdictions, a departure by the RA from the general principle of equal treatment of creditors within the same class may not be permitted and/or upheld by a bankruptcy court. Any actions taken by the RA must be done in a manner consistent with applicable bankruptcy laws and regulations.

More broadly, the Guidance should clarify how actions of an RA would interact with applicable bankruptcy regimes and what protections clearing members and their customers would have against the risk that an RA's actions will be reversed in bankruptcy. CCPs and their owners cannot be held liable for the actions of an RA that a bankruptcy court wants to reverse.

5. THE RA SHOULD OBTAIN ITS POWERS THROUGH STATUTES AND REGULATIONS, NOT CCP RULEBOOKS.

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16 *See* Guidance § 5.3. *See also id*. § 2.2.

The Guidance appears to contemplate that at least some of an RA's powers would originate in the CCP's rulebook. *See, e.g.,* Section 2.10. The powers of an RA should flow out of statutes and regulations adopted by the appropriate legislative and regulatory entities. A CCP rulebook—which is a contract between the CCP and its clearing member—is not an adequate substitution as a source of powers.

Furthermore, an RA's powers and any exercise of such powers need to be consistent with applicable law. Otherwise, the actions taken by the RA may not be upheld. A CCP cannot empower an RA to have or exercise a power that would violate applicable law by including such power in the CCP rulebook.

6. ANY COMPENSATION MUST SUPPORT THE PROPER INCENTIVES.

The Guidance discusses the writing down of a CCP's equity. *See, e.g.*, Sections 2 and 4. In the United States, the concept of writing down equity appears in both accounting and legal constructs and means different things. The Guidance needs to be revised to clarify what the FSB intends to accomplish by writing down equity and how the FSB envisions equity being written down. We look forward to commenting on portions of the Guidance that relate to equity once a clarification is made as to what is intended by writing down of equity.

Section 4.1 of the Guidance contemplates that a CCP's shareholders should fully absorb loss resulting from the default of a clearing member in resolution and provides that it should be clear and transparent at what point in resolution any remaining equity would be written down. Clearing member defaults should not lead to a resolution of a CCP unless clearing members fail to participate in default management and in recovery. Rewarding such behavior by allocating remaining losses away from clearing members and instead forcing those losses somehow on the CCP's shareholders would weaken a CCP's ability to default manage and to recover and thus create a threat to financial stability and the continuity of critical CCP functions. The Guidance should be revised to make certain that it could not be read to reward such behavior and instead would preserve fully the incentives created by the CCP's default management processes and recovery plan. To that end, it is critical that no equity write downs be permitted until a CCP exhausts all available recovery tools and clearing members meet all their obligations.

This is especially important if the RA is permitted to place a CCP into resolution as a result of clearing members losing confidence in the CCP. *See, e.g.*, Section 3.4(iv). Rather than being incentivized to satisfy their obligations to contribute to CCP default management and recovery efforts, clearing members would be incentivized to lose confidence in the CCP, encourage the RA to place the CCP into resolution and avoid satisfying such obligations through the RA's writing down of the CCP's equity.

7. IN JURISDICTIONS WHERE CCPS ARE REQUIRED TO MAINTAIN WIND-DOWN PLANS, CCP WIND-DOWN PLANS SHOULD BE RESPECTED BY THE GUIDANCE.

To the extent a jurisdiction requires a CCP to maintain a wind-down plan, the CCP's wind-down plan should be take priority over and not be superseded by the Guidance. In the United States, each SIDCO is required to maintain a wind-down plan to effect the permanent cessation or sale or transfer

of one or more services necessitated by (i) uncovered credit losses or liquidity shortfalls; or (ii) general business risk, operational risk, or any other risk that threatens the SIDCO's viability as a going concern.[17] A wind-down plan is a SIDCO's back-up plan to its recovery plan. A SIDCO develops its wind-down plan ex ante in consultation with the CFTC. We support this process, through which a regulator familiarizes itself with the CCP's plan and provides feedback to the CCP regarding the wind-down plan as needed. This is the appropriate time for the regulator to assess the effectiveness of a CCP's wind-down plan—not by intervening during the CCP's implementation of the wind-down plan.

8. COMMUNICATIONS BETWEEN RELEVANT AUTHORITIES MUST RECEIVE PROPER CONFIDENTIALITY PROTECTIONS.

We support cooperation between a CCP and the relevant regulators. *See* Sections 3.6-3.8 of the Guidance. The Guidance should clarify, however, that all sharing of information should be done in a manner consistent with the applicable laws and regulations that preserve confidentiality and anonymity. To that end, a CCP must be permitted to send directly to its regulator any information that may be shared with other regulators. If the CCP's RA or regulators in other jurisdictions need data from the CCP, the data should be sent by the CCP's regulator to the RA or such regulators, provided that Memoranda of Understanding are in place to preserve the confidentiality of the information being shared and to protect the anonymity of clearing members and their customers. These Memoranda of Understanding should respect the role of the CCP's regulator or RA and should not enable other regulators to undermine the CCP's regulator or RA.

Similarly, open communication between the RA of a clearing member and the clearing member's CCP is imperative. CCP resolution will be significantly impacted by the bank resolution framework. Apart from war or other destruction of the basic infrastructure of the financial system, the most likely cause of a failure of a systemically important CCP is the simultaneous failure of four or more globally systemic important banks that are clearing members of the CCP. Bank regulators and resolution authorities will likely have advanced knowledge of distress at a major bank and an understanding of how that distress will impact CCPs, non-defaulting clearing members, market participants and the broader financial markets. What regulators do with that knowledge will be critical in determining the outcome of the stress, but it is unclear to the market how they will approach this situation.

An understanding by the CCP of the RA's anticipated actions will enable the CCP to better use its default management and risk management practices. Bank resolution authorities should share relevant information with CCPs in conjunction with their regulatory authorities for better coordination and management of the stress event. It is essential that the resolution authorities for any failing banks prioritize the well-being of markets and financial stability, to prevent contagion of the bank stress to CCPs, non-defaulting clearing members, market participants and the broader market and public interests that derivatives markets serve.

By way of example, the United States has a coordination process that brings together market regulators and CCPs when a broker dealer or futures commission merchant encounters financial

[17] *See* CFTC Regulation 39.39.

stress or is non-compliant with certain regulatory requirements. This coordination process has proven very useful and enabled market regulators and CCPs to work together to resolve a number of failures without impacting the markets. We encourage bank resolution authorities to join this coordination process and share information with both market regulators and CCPs to enable market regulators and CCPs to minimize the impact of a default of a bank on the markets.

C. CONCLUSION.

CME Group supports efforts to develop standards to guide the development of principles based resolution strategies and plans for CCPs. CCPs are not banks and are very different from banks. The guidance for CCP resolution should not be based upon guidance developed for bank resolution.

We agree that the objective of CCP resolution should be to protect financial stability and ensure the continuity of critical CCP functions without exposing taxpayers to the risk of losses. An effective CCP resolution should also preserve the hierarchy of claims under the rules of the CCP and under the applicable insolvency regime. We further agree that "[e]ffective CCP resolution planning should have regard to maintaining incentives for CCPs, clearing members, and market participants to centrally clear and engage constructively in efforts to achieve a successful default management or recovery and reduce the likelihood of resolution."[18]

We welcome the opportunity to work together with the FSB to craft guidance that furthers—and does not undermine—our shared objectives. To that end, the Guidance should prioritize maintaining the strength and resilience of CCPs and provide that an RA should not have any powers over a CCP during business as usual in the name of resolution planning. The Guidance should recognize that a successful CCP recovery negates the need for resolution of the CCP. Neither resolution planning nor resolution implementation should be able to undermine CCP recovery. A CCP's rulebook is structured to incentivize clearing members and market participants to participate in auctions and restore a matched book. A CCP must be permitted to exhaust its recovery tools before an RA intervenes. If the Guidance contemplates any possibility of the RA even attempting to take any action before the CCP exhausts its recovery tools, the Guidance would infringe upon a CCP's ability to recover and undermine the objectives of the Guidance.

Sincerely,

Sunil Cutinho
President, CME Clearing

[18] Guidance § 1.