From:	Mathias Weber
To:	Financial Stability Board (FSB), Service
Subject:	Re: Guidance on Central Counterparty Resolution and Resolution Planning
Date:	10 March 2017 17:11:18

Dear Madam or Sir,

Thank you very much for providing the public with the possibility to comment on the standard setting process of guidance on CCP resolution.

As a general principle, recovery and resolution can be avoided if the pre-funded resources available at a CCP are increased or in other words: higher initial margin, higher skin-in-the-game and higher default fund contributions would lower the probability for the need to activate recovery or resolution plans. There is a strong similarity to the capital charges for banks that were increased significantly in the aftermath of the global financial crisis.

Here are my detailed comments on the sections of the Consultative Document:

Overall objectives of CCP resolution:
It might be questionable that resolution can aim at various equally weighted objectives at the same time because the issue of conflict of goals might arise. It would be preferable to clearly spell out that the primary objective of resolution is the pursuit of financial stability. This aim includes (but is not restricted to) the continuity of systemically critical CCP functions (but not all services of a CCP) and the avoidance of knock-on effects from resolution measures. Finally, taxpayers money shall not be used, however, public funding is not forbidden to stabilise a CCP if otherwise financial stability cannot be maintained. A systemic financial crisis will lead to a downturn in the real economy and therefore indirectly lead to a loss in taxpayers money. Therefore, the "no taxpayers money" aim should be subordinate to the financial stability aim.

Resolution powers
It is not clear if the requirements "avoid significant adverse effects on the financial system", "consider the systemic impact of tear up actions", "have systemic consequences for the market or participants", "no other option would result in a better outcome for financial stability" and "take into due account the impact on financial stability" are meaning the same tasks or require different assessments by the resolution authority. Maybe it is just a language issue but if they mean the same thing the same wording should be used. Furthermore, it is unclear why such requirements with regard to financial stability and systemic risk are listed only at some tools. It is for example not an explicit requirement for cash calls or VMGH, however these tools too could have a significant impact on the stability of clearing members and therefore on the financial stability. For a clearer guidance it might be better to require an assessment of the systemic impacts/financial stability consequences at each tool separately, including tools for non-default losses.

Full tear-up and forced allocation are both called "last resort tools". However, it might not be practicable to stipulate a particular order of use of tools in advance because only one of them can be used finally and it is not clear how a resolution authority should decide if both tools would achieve the objective to stabilise a failing CCP. My proposal: The tool that better protects financial stability (the primary objective of resolution actions). The full tear-up of a non-systemically critical CCP service should be possible very early in a resolution phase and not only as a last resort tool.

It is unclear why only for the tool write down of initial margin "jurisdictions should take into due account the impact ... on incentives to centrally clear". This might be because this tool is very controversial. However, as Darrell Duffie states (see http://www.darrellduffie.com/uploads/pubs/DuffieCCP-ResolutionJan2015.pdf), from „a risk-corrected basis, … loss sharing that is proportional to total paid-in initial margin“ would be preferable to VMGH and tear-ups and it „is not clear why many CCPs and clearing members prefer to use VMGH or tear-ups rather than to adjust their clearing agreements so as to allow legal end-of-waterfall access to initial margin funds.“ Therefore, this should not be allowed to be „a last resort tool" only.
Coming back to the question of incentives, first, for many OTC derivatives it is or will become mandatory to centrally clear, so there is no possibility that incentives will be changed by this tool. Second, all other tools like forces allocation, cash calls or VMGH will also have an impact on the incentives to use this particular CCP. Third, the FSB Discussion Note of August 2016 had a broader look on incentives and it remains unclear why incentives are now only mentioned here. Therefore, it might be better to require from the resolution authority to assess the impact on the incentives from all proposed tools beforehand.

Finally, it is unclear why the guidance for most of the tools now only refers to clearing members and therefore deviates from the Key Attributes on FMI resolution from 2014. For example, non-defaulting clearing members can be required to make cash calls; however, CCP participants could be hurt by VMGH. As a general principle, all the stakeholders of a CCP should be involved in a resolution because all have benefited from the central clearing prior to the resolution. The Key Attributes therefore rightly refer to the whole group as direct and indirect FMI participants, including the direct clearing members, the indirect clearing members and their clients. This should be done in the guidance, too.

Entry into resolution

As CCP failures are only imaginable in a severe crisis, the macro-prudential authority for oversight of financial stability should also be informed on an entry of a CCP into resolution.

Resolution planning

The resolution authority should also be required to describe in the resolution plan how it will consider the systemic impact of tools to return a CCP to a matched book and how it does account the impact of allocation financial losses on financial stability. These are very complex questions and issues to solve, so some guidance on a possible way for a quantitative assessment would be helpful. As these assessments need to take into account the loss absorbing capacity of stakeholders from various financial sectors (banks, funds, insurers) the macro-prudential authority for oversight of financial stability should also be involved in the planning phase as it should have the best overview of the state of the whole financial system. This would also avoid the duplication of work as resolution authorities would not be required to build up expertise of their own for such financial stability assessments.

Crisis management groups

It remains a bit unclear how the process of establishing CMGs will be started and work. How does the home authority know which host authorities it shall approach? How does the host authority obtain the necessary data to make an assessment which foreign CCPs are systemically relevant for its own jurisdiction? By the way, the FSB seems to be best equipped to set up a list of global systemically important CCPs as it has done with global systemically important banks. At some of the aspects for establishing CMGs (but not at all of them) there is a reference to "off-shore CCPs“, a term that is not used in the Key Attributes on FMI resolution of 2014 or the Discussion Note of 2016. So, is this only a requirement for host authorities as off-shore would mean that it is the view from the outside? But links for example should be a requirement for both, home and host authority.

Finally, as the central clearing landscape evolves over time, it might be necessary to monitor the developments and accordingly adapt the CMGs.

I would be happy if my remarks help to further improve the quality and clarity of the guidance on CCP resolution.

Yours sincerely,
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