

UNITED STATES OF AMERICA
COMMODITY FUTURES TRADING COMMISSION

MARKET RISK ADVISORY COMMITTEE MEETING

Washington, D.C.
Thursday, November 17, 2016

1 PARTICIPANTS:

2 Commissioners:

3 CHAIRMAN TIMOTHY G. MASSAD

4 COMMISSIONER SHARON Y. BOWEN

5 COMMISSIONER J. CHRISTOPHER GIANCARLO

6 Other Participants:

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Infrastructure, Bank of England

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9 GERALD BEESON
Citadel

10 DAVID BURLAGE
CoBank

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12 THOMAS COYLE
Chicago and Illinois River Marketing, LLC

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15 STEVE GRESKA, Associate Director
Division of Clearing and Risk

16 MICHAEL HENNESSY
Federal Home Loan Banks

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1 P R O C E E D I N G S

2 (10:01 a.m.)

3 MS. WALKER: Good morning. As the MRAC
4 designated federal officer, it is my pleasure to
5 call this meeting to order.

6 Before we begin this morning's panels, I
7 would like to turn to Commissioner Sharon Bowen,
8 the MRAC sponsor for the welcome.

9 Chairman Massad, Commissioner Giancarlo,
10 and Commissioner Bowen will then give their
11 opening remarks.

12 COMMISSIONER BOWEN: Good morning,
13 everyone, on such a gorgeous, beautiful fall day
14 in Washington, D.C. I'll be making my remarks in
15 a few minutes so I just wanted to turn it over
16 first to the chairman.

17 CHAIRMAN MASSAD: Well, thank you,
18 Sharon. First of all, let me thank Commissioner
19 Bowen and

20 her staff, and also the rest of our
21 staff for organizing this meeting. Let me thank
22 the members of the MRAC for all the work that has

1 gone into this and for being here, and your
2 participation. We really appreciate it. And I'm,
3 as always, pleased to be here with Commissioner
4 Giancarlo.

5 You know, I've always underscored the
6 value of these advisory committee meetings as a
7 means for us to have a dialogue with stakeholders
8 and today is, of course, no exception. I'm
9 looking forward to hearing the recommendations of
10 the Subcommittee on Clearinghouse default
11 management. I'm looking forward to hearing David
12 Bailey's presentation. I know he'll be discussing
13 one item in particular, the coordinated default
14 management exercises. We've been pleased to work
15 with the Bank of England on that and on many other
16 aspects of CCP resilience.

17 You know, I've said really since the
18 beginning of my term that CCP resilience was a
19 critical issue for us and we've made it a
20 priority. We've been doing a lot in this area,
21 including strengthening our own oversight, our own
22 risk surveillance activities, working with

1 international regulators, including the Bank of
2 England and others on resilience, recovery,
3 resolution planning, working with our own major
4 clearinghouses to develop recovery plans and
5 rules, and we're hoping to complete that very
6 soon. Working with the FDIC on resolution
7 planning. Working with the Federal Reserve to
8 open accounts for the deposit of clearinghouse
9 cash.

10 And yesterday, we announced some
11 additional important work we have done. We
12 released the results of a series of supervisory
13 stress tests on the largest clearinghouses under
14 our jurisdiction. And I just want to take a note.
15 You probably heard about it but let me just
16 quickly summarize what that report said. We
17 assessed the impact of stressful market scenarios
18 across five clearinghouses, the five major
19 clearinghouses under our jurisdiction, and those
20 are clearinghouses not just in the U.S. but also
21 in the U.K. So this is really the first time I
22 think anyone has looked across borders. I think

1 we're probably the only regulator in a position to
2 do that because we've used actual position and
3 margin data to do this. And our staff constructed
4 a number of scenarios, extreme but plausible
5 scenarios based on historical precedent, and we
6 applied those to the actual positions.

7 And so we could look at both the impact
8 on clearinghouses, as well as the impact on
9 clearing members. And the results showed that the
10 clearinghouses had ample resources to withstand
11 these scenarios. Not only did they meet cover
12 two, but in about two-thirds of the tests they
13 were able to cover all participant shortfalls or
14 losses. And our assumption in this was that no
15 clearing member would make any additional payment,
16 which is obviously a very extreme assumption in
17 this kind of a situation.

18 And I think one of the most interesting
19 things that came out of the test was that risk was
20 diversified across clearing members. If you had a
21 loss at one clearing house, that didn't mean you
22 had losses at all, and I think that's a very

1 helpful finding because obviously there has been
2 some concern about now that we've moved a lot of
3 transactions into central clearing, what happens
4 if there's one default? Wouldn't that trigger a
5 whole series of defaults? We're able to measure
6 what would happen to multiple clearinghouses and
7 to the largest clearing members under these
8 scenarios. There's now extensive margining, daily
9 reporting that gives us detail. And think back
10 where we were eight years ago when with Lehman
11 going under, AIG about to go under, people were
12 scrambling to understand what the exposures of one
13 large institution were to another, what would be
14 the consequences of a default by one. Just think
15 back to that fateful day when the government was
16 trying to decide whether to support AIG and how
17 much it would take, and the number kept going up
18 by the hour. So we've come a long way.

19 The test, and this is the report in case
20 you haven't seen it. It's available on our
21 website. The test is only one step. We need to
22 keep doing this. We need to do a lot more. We

1 talk about various enhancements that we may do.

2 So again, I'm very much looking forward
3 to the meeting. I appreciate Commissioner Bowen
4 for really focusing a lot of the work of the MRAC
5 on the issue of clearinghouse safety. I think
6 that was a very wise decision on her part, and
7 again, thank you all for being here.

8 COMMISSIONER BOWEN: Thank you.

9 COMMISSIONER GIANCARLO: Thank you,
10 Chairman, and thank you, Commissioner Bowen. And
11 Commissioner, thank you for convening today's
12 meeting. I note that this is the sixth meeting of
13 MRAC in a little over two years. That's quite an
14 accomplishment, and I think I, and all of us, have
15 found these meetings to be of tremendous value.
16 The opportunity for committee members to present
17 their views and findings is very helpful in
18 assisting my fellow commissioners and me, as well
19 as the staff and the public, in understanding the
20 competing dynamics and the risk factors in our
21 markets.

22 I believe the success of MRAC brings

1 distinct credit to all of us. We're a better
2 regulatory agency because of the commitment and
3 efforts of the MRAC members, and none of this
4 would be possible without the extraordinary staff
5 work that goes into bringing these agendas and
6 presentations together, and so I do want to
7 commend in particular the facilitator, Petal
8 Walker for all of her efforts in organizing the
9 six meetings we've had. It's been quite an
10 accomplishment.

11 As you all know from the agenda, the
12 first part of today's meeting will address
13 important details in the management of CCP
14 default. It's critically important that clearing
15 and nonclearing members have the ability to
16 communicate and understand their role in a default
17 situation, and we must understand how the
18 mechanics of porting customer portfolios would
19 work in the event of a default and address any
20 obstacles to a smooth transition.

21 The discussion is timely. Yesterday, as
22 Chairman Massad noted, we presented the findings

1 from the Commission's Supervisory Stress Test of
2 Clearinghouses, and this report is really an
3 important accomplishment, and I commend the staff
4 for their work, and I commend the chairman for his
5 leadership in this effort. It really is a
6 watershed moment. The Commission's report
7 concluded that the clearinghouses had the
8 financial resources to withstand a variety of
9 extreme market conditions. Inherent in this
10 conclusion, however, is the expectation that all
11 participants in the CCP ecosystems communicate and
12 understand their obligations in a crisis
13 situation, so I look forward to hearing the
14 Committee's recommendations in this regard.

15 And I also look forward to the second
16 panel today on CCP resilience and hearing
17 presentations from our distinguished guests,
18 Robert Steigerwald, senior policy advisor at the
19 Federal Reserve Bank of Chicago, and David Bailey,
20 Financial Markets Infrastructure at the Bank of
21 England. So welcome gentlemen. Welcome all of
22 you, and thank you for coming today.

1 COMMISSIONER BOWEN: Great. Thank you
2 so much. Welcome to the November 17, 2016 meeting
3 of the

4 Market Risk Advisory Committee. I'm
5 excited to be the sponsor of this important
6 committee. But before we begin our meeting today,
7 I just want to say a few words about the election.

8 I'm sure that much can and will be said
9 about the election's impact on our markets, our
10 investors, consumer protection, and financial
11 regulation. But fundamentally, MRAC's focus on
12 market risk is even more important today. And in
13 that vein, I want to thank Chairman Massad and
14 Commissioner Giancarlo for their support of this
15 committee's hard work. It's been a privilege to
16 work with both of you as fellow commissioners
17 these last two and a half years, and I look
18 forward to working with you both in the future.

19 Turning to today's meeting, I'm greatly
20 looking forward to the Committee's vote on the CCP
21 Risk Management Subcommittee's final
22 recommendations on how central counterparties can

1 further enhance their efforts in preparing for the
2 default of a significant clearing member. And
3 hearing from David Bailey, director of Financial
4 Market Infrastructure at the Bank of England, here
5 to discuss the Bank of England's coordinated CCP
6 default portfolio. I really want to thank you,
7 David, for traveling here from the U.K. to share
8 your insight with us.

9 With this meeting, as Commissioner
10 Giancarlo mentioned, we now have completed the
11 second year of MRAC and our sixth meeting. We
12 started our journey on April 2, 2015. The purpose
13 of MRAC then, as now, was twofold. One, to advise
14 the Commission in its efforts to detect, analyze,
15 and mitigate market risk; and two, to provide
16 information and analysis to the Commission on the
17 evolving market structure.

18 To meet these tasks, pursuant to its
19 charter, we assembled a diverse, impressive group
20 of market participants -- end-users,
21 clearinghouses, exchanges, market makers,
22 intermediaries, academics, swap execution

1 facilities, swap data repositories, service
2 providers, public interest groups, and regulators.

3 MRAC's meeting topics in the last two
4 years reflect a commitment to its meetings its
5 goals. To meet its market structure mandate, the
6 MRAC held discussions on the state of the market
7 dealing with a number of issues, including
8 liquidity, the use of SEFs, and portfolio
9 compression. And to meet its market risk mandate,
10 the MRAC discussed many issues, including CCP risk
11 management, cybersecurity, and the implication of
12 resolution above clearing members and CCPs.

13 I look forward to today's discussion and
14 will now turn it over to MRAC's designated federal
15 officer, Petal Walker, who will get us started.

16 MS. WALKER: Thank you for your opening
17 remarks. Before I begin, I would like to
18 acknowledge Steve

19 Greska, who is the associate director in
20 the Division of Clearing and Risk. Over two years
21 ago I had asked Steve about what would be a good
22 topic for our first meeting and he noted that a

1 discussion on enhanced coordination between CCPs
2 in a case of major default would be a very good
3 topic, and because of that, over two years ago we
4 started that discussion and then we had these
5 recommendations, although the staff did not have a
6 hand in the recommendations, the germ of the idea
7 came from Steve Greska. I wanted to acknowledge
8 him. Thank you, Steve.

9 As noted in today's agenda, our first
10 panel will be a discussion of the CCP Risk
11 Management Subcommittee's recommendations for CCP
12 default management.

13 I would now like to call upon Ms. Susan
14 O'Flynn, who led this effort in the CRM
15 Subcommittee, as well as Mr. Gerald Beeson, Mr.
16 Dennis McLaughlin, and Mr. Richard Miller, to
17 present the Subcommittee's final recommendations
18 to the MRAC on how CCPs can further enhance their
19 efforts in preparing for the default of a
20 significant clearing member. As discussed at the
21 April 2, 2015; November 2, 2015; and June 27, 2016
22 MRAC meetings.

1 MS. O'FLYNN: Thank you, Petal. So just
2 to introduce my co-panelists, we have

3 Gerald Beeson from Citadel, COO and CFO;
4 we have Richard Miller from Miller Consulting; and
5 we also have Dennis McLaughlin, Chief Risk Officer
6 from LCH Clearnet.

7 With regard to logistics, please press
8 the button to activate your microphone when you
9 speak, and please press off when you are finished
10 speaking.

11 Before we move into, you know, each
12 panelist is going to address some of the
13 recommendations that are currently in the
14 document, but I'd like to say a few words first.

15 Firstly, I would like to thank
16 Commissioner Bowen for forming this committee two
17 years ago to address this very important topic of
18 CCP default management. It continues to remain a
19 highly relevant and current topic, especially in
20 light of the global regulatory attention and
21 recent papers and guidance issued on resiliency,
22 recovery, and resolution by the CFTC, the FSB, and

1 CPMI-IASCO.

2 The auction and market participant
3 involvement following the default of a significant
4 clearing member is arguably the most important
5 step of the default management process in ensuring
6 CCP resiliency and the timely reestablishment of a
7 matched book. CCPs are becoming the single
8 largest counterparties from many institutions,
9 both sell and buy side, given the clearing mandate
10 and the advent of many other clearing services for
11 products such as securities finance transactions,
12 foreign exchange due to resource implications, be
13 it balance sheet capital or funding. Continued
14 voluntary flow into clearing for nonmandated
15 products can be most reasonably observed since the
16 go live of margin for uncleared derivatives in
17 September.

18 It is critical that the auction process,
19 participant obligations, CCP actions, and client
20 involvement and ex ante transparency of all the
21 aforementioned are addressed now and clarified as
22 we move forward into a trading environment where

1 many existing products will be cleared and a
2 defaulting member will likely be clearing many, if
3 not all of the aforementioned products.

4 Today's recommendations are an
5 amalgamation of two separate sub subcommittees'
6 work over these past two years, as well as
7 previously published recommendations from those
8 subcommittees as mentioned by Petal in 2015 and
9 earlier this year. It must be recognized that
10 this Committee has a very diverse set of
11 representatives and this has, at times, made it
12 challenging to come to recommendations which have
13 reflected all parties' positions. I'm honored to
14 be here today to present today's recommendations.

15 The document also reflects the areas
16 which are either for further discussion or
17 consensus could not be reached in full. I would
18 also like to personally thank BlackRock, most
19 notably Eileen Kiely and Kirsten Walters, who were
20 chief draftswomen for this document. Their help
21 was invaluable.

22 There are six different recommendations

1 which fall into two categories: default
2 management, coordination, harmonization,
3 enhancement, and porting. Within category one,
4 default management, several key recommendations
5 were agreed upon including the following:
6 communication, establishment of a directory of key
7 individuals at clearing member and nonclearing
8 member firms involved in default management will
9 be engaged with clearinghouses and regulators at
10 the time of the default of a clearing member.
11 There were also recommendations around CCPs'
12 engagement of and communication with nonclearing
13 member firms in the event of an FCM default, of
14 the default itself, as well as the porting
15 process.

16 Default management committees.
17 Recommendations of harmonization of certain
18 aspects of the default management process, such as
19 tenure, coordination of rotation of seconded
20 representatives, as well as maintaining a register
21 of seconded representatives to avoid one firm
22 being called multiple times.

1 Involvement of material. Nonclearing
2 member firms should also be considered subject to
3 certain rules and regulations.

4 First, drills. There was wide support
5 that joint to full fire drills and/or three-way
6 fire drills should be considered on an ongoing
7 basis and become a more formalized process.
8 Clients, as well as clearing members should
9 participate, and porting simulation should be
10 included in that fire drill auction process.

11 There were also recommendations around
12 harmonization of auction process and procedure and
13 a call for auction playbooks. So there would be
14 ex ante certainly as to what the rules and
15 responsibilities of clearing member firms and
16 nonclearing member firms would be in advance of
17 the process.

18 There was also a recommendation around
19 customer participation and auctions, and last but
20 not least, porting, a topic much discussed at the
21 previous MRACs and several key issues have been
22 identified, most notably the resource implications

1 for remaining FCMs, as well as the operational
2 intensity of onboarding new clients.

3 With that I'm going to turn to my fellow
4 panelists who each are going to discuss some of
5 these recommendations in more detail. Gerald will
6 be going first with customer participation
7 auctions and portion, followed by Dennis, who will
8 discuss communication and fire drills. Richard
9 Miller will then speak on communication and
10 porting, and I will discuss auction process and
11 default management committees.

12 So I turn to Gerald.

13 MR. BEESON: Thank you, Susan. Good
14 morning. My comments will be on the customer
15 participant

16 and auctions from item 1.E. The success
17 of the auction is perhaps the most critical piece
18 of the CCPs' default management process, and
19 bringing to bear that we have an insured that
20 qualified available and willing sources of private
21 investment capital are brought to bear at an
22 auction increases the likelihood of its success,

1 the fairness, and the efficiency of auction
2 pricing.

3 While direct customer auction
4 participation is contemplated in select instances,
5 it is not universal across the CCPs or even across
6 differing cleared products within the same CCPs --
7 as an example, futures versus swaps. So rather,
8 most of the CCP rulebooks look primarily to the
9 direct clearing members to participate in these
10 auctions. The Subcommittee's recommendations,
11 therefore, encourage CCPs to consider means to
12 allow nonclearing members to participate in the
13 auctions, in the auction process; acknowledge that
14 the correct terms, conditions, and procedures need
15 to be put in place upfront to ensure that there's
16 a governance of the participation of nonclearing
17 member process in the CCP auctions. We believe
18 the customers are an integral process in the
19 central stakeholder group in clear derivative
20 markets, and they certainly have a vested interest
21 in ensuring that these auction processes are
22 successful.

1 Given the correlation of the business
2 models, it is certainly possible that direct
3 clearing members as a whole may not be in the
4 strongest position to bid aggressively at auctions
5 following a clearing member default, which only
6 reinforces the importance of bringing other
7 sources of noncorrelated capital to the table.
8 There certainly may be concerns that exist either
9 with respect to the information with respect to:
10 (a) the defaulted portfolio being leaked to the
11 market; or (b) the nonclearing firms not being
12 appropriately incentivized or qualified to bid
13 responsibly. We believe that those can be easily
14 addressed by setting a priori-qualified and
15 appropriate mechanisms for participation ranging
16 from confidentiality agreements to minimum
17 deposits to be able to participate in the auction
18 itself, having a demonstration of the financial
19 resources required to be able to meet the initial
20 margin deposits should there be a winning bidder,
21 demonstrating the capacity to ultimately be able
22 to clear the portfolio at another clearing member

1 should they actually win the process as well, and
2 then also, potentially having some form of penalty
3 mechanism should their bid fall below a certain
4 threshold. These are as a percentage of the
5 winning bid or below the median of the actual bids
6 that are submitted in the actual auction process
7 itself.

8 Secondly -- and both Rich and I are both
9 commenting on the issue of porting -- we have a
10 few comments. First, in terms of the ability of a
11 solvent customer of a nonclearing member to port
12 their portfolio, and as importantly, the
13 associated collateral associated with that
14 portfolio to a solvent clearing member is one of
15 the key customer protection features of central
16 clearing. Customer porting has certainly worked
17 in a number of situations in past clearing member
18 defaults. We believe that further measures should
19 be undertaken and considered to ensure this is a
20 viable and efficient process going forward.

21 Market participants do believe that
22 certain challenges exist today that may impair the

1 likelihood of a timely and successful porting
2 process, including customer onboarding
3 requirements at the new clearing member if they're
4 not already in place, if they don't have more than
5 one clearing relationship; if there are timing
6 mismatches between the movement of customer
7 positions and customer collateral; the timing of
8 bankruptcy court approvals where applicable; and
9 otherwise industry capacity-wide constraints.

10 In order to improve the porting process,
11 the subcommittees recommended to develop solutions
12 that allow for remaining solvent clearing members
13 to service the portfolios of nondefaulting
14 customers on an interim basis post the clearing
15 member default. And this can serve as a very
16 important bridge while the porting process
17 proceeds. Further, having investment in and
18 development of automated and regular use customer
19 porting capabilities in the nondefault scenario,
20 and at present, porting positions from one
21 clearing member to another clearing member on a
22 regular basis is certainly time-consuming, an

1 overtly manual process that can only be done on an
2 appointment basis. The ability for customers to
3 manage their portfolios across multiple clearing
4 members would be enhanced with more automated, on-
5 demand, and straight-through processing based
6 porting capabilities. And also, the industry
7 investment in such solutions would pay enormous
8 dividends in times of market stress as the tools
9 and capabilities used and developed to efficiently
10 port portfolios in times of nonstress will be
11 battle-tested and able to use in the case of a
12 porting scenario.

13 MS. O'FLYNN: Okay, Dennis?

14 MR. MCLAUGHLIN: Thank you, Susan. I
15 have to talk about communication, which is a
16 vital piece of the whole puzzle, because
17 you have to know who to talk to, how to reach
18 them, at what times at particular times in the
19 process, and that should be as smooth as possible.

20 There are two key recommendations that
21 we have. The first one is to create and maintain
22 a global directory of key individuals -- who do

1 you contact both at clearing member firms and
2 nonclearing member firms. Steps have already been
3 taken to begin this process, so that's a really
4 key part. And now who are you contacting and what
5 do you say to them? Well, obviously, for clients,
6 you can't have a general market communication
7 about an individual client position, but what you
8 can do is provide updates to the market in general
9 about things like when the porting window has
10 opened, when it's closed, when it's completed, is
11 there anybody being -- noncustomer liquidations
12 taking place? But you're not going to talk in the
13 general updates about specific client positions.
14 However, you need to talk to each individual
15 client who is affected about the status of their
16 portfolio. That's key. So, for example,
17 especially if they have positions that are being
18 liquidated as part of the member portfolio, who
19 they are coming to the CCP through.

20 The other part I have to talk about is
21 fire drills, I think. This is a really key and
22 much important thing because we have to test

1 exactly whether we're ready or not to handle a
2 real-life situation. If the CCP can't handle
3 this, it's going to have a profound effect on the
4 global markets, and so we have a couple of
5 recommendations around this.

6 The first one is that the joint fire
7 drills have to be formalized across CCPs,
8 especially where there is significant product
9 overlap with agreement reached as to frequency of
10 drills, the scenarios and the shocks tested in
11 drills, and the required participants. That
12 condition about required participants is key
13 because there are not that many members. There is
14 a shortage or a potential shortage of members to
15 spread around in a default situation from the
16 member perspective. We need to ensure that we
17 have the most efficient use of resources at the
18 time of default so nobody is sort of
19 double-counted in that procedure.

20 The other one is that fire drills should
21 be conducted regularly, and they should include
22 multiple CCPs so we know what's happening because

1 in all likelihood, multiple CCPs will be involved.
2 They should include both clearing members and
3 customers. Traditionally, it's been clearing
4 members, but we need to be also looking at the
5 impact on customers during the fire drill. So the
6 drills should periodically include simulations of
7 the porting and inability to port the nondefaulted
8 customers' portfolio, and include representative
9 material customers in this aspect of the fire
10 drills. So we need to incorporate the customer
11 view into the fire drill for the default
12 management process.

13 That's all.

14 MS. O'FLYNN: Richard?

15 MR. MILLER: Thank you, Susan. If I'm
16 clearing my throat, it's not a virus; it's
17 allergies. I'm dealing with it. Excuse
18 me. I think this is the first opportunity I've
19 had at

20 the MRAC to give some extended remarks,
21 so I'd like to begin by thanking Chairman Massad
22 and Commissioners Bowen and Giancarlo for creating

1 this opportunity in this forum. I think it has
2 been a valuable means of exchanging views.

3 I'm here representing the American
4 Council of Life Insurers and the life insurance
5 industry, and I would like to underscore this
6 somewhat unique role that I think life insurers
7 have in the processes that we're dealing with here
8 today because life insurers are hedgers. They're
9 prohibited by law to speculate in these markets,
10 so they use these markets, derivative markets, to
11 hedge their portfolios and the risks that arise
12 from the products they sell. And it's almost a
13 correlated situation where they could not sell the
14 products that they presently sell to the public
15 without having the opportunity to hedge as they do
16 in these markets. And the hedging has been going
17 on since the emergence of annuity products and
18 other products that require the hedging, the
19 proper hedging and risk management by the
20 insurance companies. And we went through the
21 crisis. Chairman Massad refers us back to eight
22 years ago, and I remember it well. And we went

1 through the crisis and there were some lessons
2 learned obviously in the crisis that I'll get to
3 in a moment, that are relevant to these
4 conversations here today. And at the time we went
5 through the crisis, of course, life insurers were
6 dealing on a bilateral basis. But because life
7 insurers are financial end-users under Dodd-Frank,
8 they're compelled now to use the clearing
9 mechanism of the CCPs when they're using interest
10 rates and equity products to hedge their risks.

11 So in that respect, life insurers, like
12 other financial end-users, like some hedge funds
13 and pension plans, are captives of the system. We
14 have no option, but we must use the CCPs to clear
15 these products. And captive of the system, we
16 don't have any direct voice in the management or
17 the governance or the oversight of the systems
18 that we are at risk to. So it's very important,
19 and it's useful in our view to have the means in
20 this MRAC conversation to interface with
21 regulators because we rely on the regulatory
22 scheme and the good faith of the CCPs to manage

1 these risks that we're subject to, like captives
2 in a moving vehicle.

3 So with that said, I'll turn to a couple
4 of the recommendations that I've been asked to
5 speak about. And I don't want to go over the same
6 territory that makes this redundant, but a couple
7 of points probably could be underscored.

8 I referred back to the crisis.
9 Obviously, one of the worst things that you
10 experience in a crisis situation is uncertainty,
11 not knowing what is going to happen next or when
12 it's going to happen, so the availability that
13 we're talking about here of having playbooks with
14 distinct timelines and means of communication that
15 provide the market with transparency. So we know,
16 for example, in the auction process where we are
17 at what stage, when we can expect the result, and
18 having a plan beforehand so that there is that
19 kind of playbook that we can look at would remove
20 to some degree -- there's always going to be
21 uncertainty, but at least you'll have something to
22 rely upon in the crisis situation.

1 Similarly with porting. To have a
2 distinct timeline, to have a playbook, to know
3 where you stand in the porting process. That's
4 why the recommendations of the Subcommittee with
5 respect to transparency in both respects I think
6 are very well thought of.

7 Two other points. One is referred to
8 earlier by my colleagues on the Committee having
9 to do with the availability of FCMs. Large
10 insurers, like my former employer Prudential and
11 others that are in the ACLI group, have multiple
12 clearing relationships, but yet in the life
13 insurance industry there are smaller life insurers
14 who are compelled to use central clearing who
15 don't have the same bulk of transactions so that
16 they are limited to practically one FCM. They
17 really can't have multiple relationships. They
18 don't have the bandwidth to do it. So if that FCM
19 should be in a crisis situation, they will not
20 have another one in their portfolio to easily port
21 their positions to.

22 So one of the recommendations of the

1 Subcommittee is to think about creating "break the
2 glass" solutions for FCMs that could be, you know,
3 emerge in a crisis to provide a safety net for
4 those customers who don't have preexisting
5 relationships with multiple FCMs. That would give
6 more confidence to the market and again create the
7 kind of certainty in a crisis that would eliminate
8 the uncertainty of where am I going to put my
9 positions if my FCM is going down and I don't have
10 a preexisting relationship?

11 On that point, one of the issues that we
12 discussed in the Subcommittee as to which we did
13 not have a complete resolution of consensus was
14 whether there should be capital relief, at least
15 on a temporary basis for FCMs in a crisis so that,
16 you know, when you increase the customer book of
17 an FCM, they need a consequently higher amount of
18 capital. If you could get some relief from that
19 requirement at least temporarily, an FCM could
20 take on more customer positions without having to
21 immediately increase its capital.

22 Lastly, being a lawyer I can't avoid the

1 bugaboos of some of the legal principles involved
2 here, particularly the bankruptcy issues that
3 Gerald referred to. There's a disconnect
4 potentially in the timing of the transfer in
5 porting of customer positions and the underlying
6 collateral and margin that creates uncertainty and
7 disconnection in the marketplace, and it's, I
8 think, important and the Committee has recommended
9 that regulators and legislators address that issue
10 so that we have the bankruptcy fix that's probably
11 necessary.

12 So with that I'll conclude. Thank you.

13 MS. O'FLYNN: Okay. So that leads me to
14 the two topics which I'll just make some comments
15 on.

16 So first, let's look at default
17 management committees. How can they be enhanced,
18 harmonized, or further coordinated?

19 Currently, they include seconded
20 clearing members who bring the requisite skill and
21 expertise necessary to hedge the defaulted
22 clearing member's portfolio, as well as structure

1 and liquidate the portfolio via the auction. What
2 recommendations can be made to enhance the
3 process?

4 First, a harmonization of certain
5 elements of the process, such as tenure, timing
6 and frequency of rotation of seconded
7 representatives, as well as appropriate sizing of
8 default management committees, taking into
9 consideration the complexity and/or the liquidity
10 of the products. We see varying sizes as to the
11 default management committees. We just think this
12 would be an important thing to look at.

13 Secondly, CCPs should maintain a default
14 management committee register of seconded
15 representatives and this should be shared between
16 clearinghouses to ensure on clearing member firm
17 is called upon more than once for a particular
18 product. This is to ensure that those clearing
19 members have sufficient trading expertise to be
20 able to bid well in auctions.

21 Thirdly, consideration should be given
22 to expand the existing pool of representatives who

1 sit on the default management committee to include
2 nonclearing member firms, those firms are active
3 in the products liquidated can bring relevant
4 market expertise into the process. Such
5 participation should be subject to the same rules
6 and obligations, such as confidentiality, that
7 existing clearing members are subject to.

8 Auction process. It's been touched on
9 by a number of my peers here but, you know, I
10 think we just need to reaffirm, and given the
11 breadth of products now being cleared, consistency
12 and ex ante transparency into each CCP's auction
13 process and procedures are critical to ensure an
14 auction's success. CCPs should harmonize their
15 auctions where feasible. Where a single "one size
16 fits all" may not be appropriate given the breadth
17 of products, a general alignment of procedures and
18 timelines is needed, especially where a large
19 clearing member has defaulted at more than one
20 CCP.

21 CCPs should develop auction playbooks
22 for participants to give ex ante transparency

1 which include the following: methods of disposal
2 available for CCPs including auctions; auction
3 participation rules, be it mandatory or voluntary
4 and potential liability; the sequence of events
5 and timing of the different events in the process;
6 bid submission auction results; and information
7 should be delivered and to be received. For
8 example, the file format. We have to consider
9 that, you know, and with obviously these drills
10 which are being run, you know, now joint and
11 sometimes three-way, that you're going to be
12 bidding in probably two to three auctions at once
13 if a large clearing member has defaulted in IRS,
14 for example. So the standardization of auction
15 files and formats means from a best execution
16 perspective and also from kind of an operational
17 efficiency perspective that is something that
18 needs to be looked at.

19 Today's panel on the joint drill could
20 not be more timely, and I look forward to hearing
21 David's comments on these aspects of the auction.

22 MS. WALKER: Thank you all for that

1 presentation on the CRM Subcommittee's
2 recommendations.

3 I would like to open the floor to the
4 MRAC to discuss any further comment on the
5 Subcommittee's recommendations.

6 Kim?

7 MS. TAYLOR: Thank you. Thank you to
8 the MRAC Committee for hosting this important
9 discussion.

10 CME was a participant on the default
11 management working group, and we appreciate the
12 efforts of the Subcommittee to come up with
13 recommendations that reflect kind of a
14 broad-basset set of views; however, kind of by
15 definition, when you have a paper drafted by a
16 committee, it's not going to necessarily represent
17 the kind of full diversity of use, so I wanted to
18 just make a comment on a couple of items.

19 First of all, communication, we believe,
20 is critical, and actually, CCPs have a strong
21 history of having good communication during a
22 crisis, and so these principles endorse and

1 encourage that and we support that.

2 When it comes to coordination, we also
3 support conceptually the idea that standardization
4 of the input and output formats for sure,
5 standardization of kind of terms and terminology
6 and types of auctions so that when somebody says
7 Dutch auction it kind of means the same thing no
8 matter which CCP is using the term. We fully
9 support that. And we fully support the idea that
10 there needs to be some transparency to the
11 marketplace so that they know what to expect. We
12 would encourage the industry to stop short of
13 requiring CCPs to make an ex ante commitment to
14 follow a defined exact process though because that
15 might not be the process that given the
16 circumstances that we're facing at the time is the
17 best -- going to provide the best outcome for the
18 marketplace. So I think we're very supportive of
19 this coordination process as long as there's an
20 understanding that these are guidelines rather
21 than an ex ante commitment that the auction is
22 going to be at two o'clock on the third day. So

1 we believe in sensible crisis management
2 coordination.

3 The principles advocate sensitivity to
4 the impact on the clearing members of potentially
5 being called for multiple default management
6 committees. We are very supportive of the need to
7 sensibly manage the impact of that with cross CCP
8 coordination of who is called to be on default
9 committees. The principles also advocate
10 strengthening the default management auction
11 process not only by standardizing the input and
12 output formats and definitions but also by
13 broadening out the participants. I'm very
14 supportive of the comments that Gerald made on
15 behalf of bringing in other nonclearing member
16 participants into the default management process
17 or the auction process and actually, our
18 experience has shown in futures, which is somewhat
19 different, more liquid, more visibly liquid than
20 swaps, but our experience has shown that we very
21 effectively were able to use nonclearing member
22 bidders in the default management process, for

1 example, with Lehman. So we are very supportive
2 of that.

3 And we support the idea of joint fire
4 drills. I think it's very important for
5 clearinghouses to work together in practice the
6 way we would need to work together in reality if
7 there is a crisis, and we very much support the
8 industry recommendations regarding the porting.
9 The protection of the innocent customers in a
10 customer default is one of the key things that
11 underpins the safety and security of the market as
12 a whole because protecting the innocent customers
13 and not liquidating more positions than are
14 absolutely necessary is an important way of
15 containing the market impact. So we're very
16 supportive of the suggestions that there be some
17 sort of safe harbor on the "know your customer"
18 and the money laundering aspects, the paperwork
19 aspects of transferring customers from one
20 clearing member to another, and we would also be
21 supportive of reasonable and temporary capital
22 relief that would allow clearing members not to

1 have to dramatically increase capital while they
2 absorbed the new set of customers. But I'm
3 sensitive to the fact that clearing members need
4 to be well capitalized, and so we would be
5 supportive of that relief being relatively
6 temporary to allow for time to absorb and
7 capitalize appropriately.

8 Thank you.

9 MS. O'FLYNN: Kevin?

10 MR. MCCLEAR: Good morning. Thank you
11 for including ICE in this process. We found it to
12 be very productive. In fact, many of the
13 recommendations that we're discussing today have
14 already become practices.

15 And I want to follow up on what Kim said
16 in many instances and give a real life example.
17 The CME and ICE recently conducted a joint fire
18 drill. We included ICE Clear Credit, ICE Clear
19 Europe and the CME with respect to credit default
20 swaps. And this provided a perfect opportunity
21 for us to put into place these recommendations
22 we've been discussing. The first one was the

1 coordination of the seconded traders. And to
2 Kim's point, we shared in advance our respect of
3 seconded trader lists, so we were in a position to
4 manage seconded traders across three
5 clearinghouses, and we didn't have any problem
6 because of that. We were also able to coordinate
7 having clearing participants bid simultaneously in
8 three default auctions and that went smoothly.

9 The other thing we were able to do was
10 test ICE's newly developed automated default
11 management system. We had the benefit of
12 developing our default management system in recent
13 months, so we were able to incorporate the
14 standard default terms that Kim referenced so that
15 the participants were working from, call it the
16 common play book, and we found that to be very
17 productive. We had over 200 people set up to
18 participate in the default auction and entered
19 bids into the automated default system. They
20 could cancel bids, resubmit bids, and importantly,
21 because it's electronic, they could take the
22 auction portfolios and break them down into the

1 risk management systems to price their bids.

2 We also practiced porting. We
3 successfully ported customer positions both out of
4 ICE Clear Credit and ICE Clear Europe. So I've
5 said before at this forum that practice is so
6 important, and here's a real life example of us
7 practicing the very recommendations that come out
8 of this Committee. So thank you.

9 MS. O'FLYNN: Jerry?

10 MR. JESKE: Hi, I'm Jerry Jeske from
11 Commodities Market Council.

12 So to Kim's point about the paperwork, I
13 think that the Commission should introduce a
14 regulatory framework when it comes to porting, and
15 some of the things Kevin mentioned are really
16 important from a timing perspective. Having lived
17 the process with Lehman at a large British bank
18 which will go unnamed, that received a lot of
19 these positions, timing is critical. There's not
20 much of it typically.

21 So one of the paperwork items that I
22 think Kim just mentioned in terms of anti-money

1 laundering and KYC should absolutely be relaxed
2 because by definition you have an implied
3 understanding that the KYC and AML has already
4 taken place for those innocent customers as you
5 put it, Kim. And that, I think, should not be a
6 standard or a hurdle for any porting process
7 because it's already been done. Likewise from a
8 capital perspective, I think leniency should be
9 considered. Obviously, you know, not everyone is
10 made the same and you want to have a robust,
11 competitive bidding process as Kevin was just
12 explaining, but not everyone is going to have the
13 same capital available to them. So again, you
14 know, some leniency in regards to how that's done
15 particularly from a timing perspective and more
16 participants I think would be the best.

17 MS. WALKER: At this time, in keeping
18 with the meeting agenda, the MRAC will take a
19 break. We will return at 11:05 for the vote.

20 (Recess)

21 MS. WALKER: We will now resume. I move
22 that the MRAC adopt the CRM Subcommittee's

1 recommendations as recommendations of
2 the MRAC and that the MRAC recommend to the
3 Commission that it consider the CRM Subcommittee's
4 recommendations.

5 Is there a second?

6 MS. O'FLYNN: I second.

7 MS. WALKER: Are there any questions or
8 comments? We do have two MRAC members on the
9 phone for the

10 vote, John Nixon and Kirsten Walters.

11 Are there any other MRAC members on the phone?

12 I now call for the vote on the CRM
13 Subcommittee's recommendations. Pursuant to the
14 MRAC charter, our two regulatory members are
15 nonvoting members and thus will not vote.

16 All those in favor of adopting the
17 Subcommittee's recommendations as recommendations
18 of the MRAC and recommending that the Commission
19 consider the recommendations, please say aye and
20 raise your hand.

21 Thank you. Do we have any ayes on the
22 phone?

1 MR. NIXON: Aye.

2 MS. WALTERS: Aye.

3 MS. WALKER: All those opposed please
4 say nay and raise your hand.

5 Any abstentions? For the record, the
6 number of ayes is 19; the

7 number of nays is zero; and there is one
8 abstention. The ayes have it; the motion carries.

9 So with that, we'll take a five-minute break and
10 prepare for --

11 CHAIRMAN MASSAD: I would just would
12 like to underscore again how valuable this is and
13 what a great job Commissioner Bowen and Petal and
14 the rest of her staff and all of you have done.
15 You know, to have an advisory committee produce
16 something like this, which is just very, very
17 useful. There was clearly a need for it. You
18 brought together all the interests and worked
19 through the issues. And I recognize as I think
20 Kim wisely pointed out, a committee product, you
21 know, maybe it's not exactly what everybody wants
22 and all that, but you know, it really reflected

1 all of these views and you reached a consensus on
2 these things, and it's terrific work. So thank
3 you to Commissioner Bowen, Petal, the rest of her
4 staff, and thank you to all of you.

5 MS. WALKER: So we'll have a five-minute
6 break and start at 11:20. Give a chance for the
7 next panel to come up.

8 (Recess)

9 MS. WALKER: It is my pleasure to call
10 this meeting back to order.

11 As noted in today's agenda, our second
12 panel discussion will cover a regulatory
13 perspective on CCP resilience.

14 I would like to introduce Robert
15 Steigerwald, senior policy advisor of Financial
16 Markets at the Federal Reserve Bank of Chicago,
17 who will facilitate this discussion.

18 MR. STEIGERWALD: Thank you, Petal, and
19 thank you, Commissioner Bowen, for scheduling this
20 meeting and for placing on the agenda a very
21 important topic. I think it's quite fortuitous
22 that we have the opportunity to discuss in greater

1 detail some of the lessons to be learned from fire
2 drills of CCP resiliency following on the vote by
3 the CRM today.

4 I'm about to introduce our speaker, our
5 honored guest from the Bank of England. Let me
6 just make a personal observation that for the best
7 of reasons, the international policy community has
8 been very focused recently on issues of recovery
9 and resolution for financial market
10 infrastructures. Those are very thorny problems
11 not yet fully worked out, but the attention that
12 those issues get should not distract us from the
13 business of thinking about day-to-day CCP
14 resiliency and the important exceptional, yet
15 occasional need to deal with clearing member
16 default and default management processes.

17 I think that the discussion today of
18 fire drills and related policy concerns will help
19 us focus again on a more ordinary aspect of CCP
20 risk management.

21 Our guest is David Bailey. He is
22 director of the Financial Market Infrastructure

1 Directorate at the Bank of England, and he will be
2 making a presentation and taking questions from us
3 and interacting with us after his presentation.

4 David?

5 MR. BAILEY: Thank you. Thank you,
6 Robert, and good morning, everyone. I'd
7 particularly like to thank Committee Chair Bowen
8 for inviting me to speak to the Committee today on
9 this important topic of CCP resilience.

10 As supervisors of some of the biggest
11 and the most systemically important CCPs that
12 serve global markets, the Bank of England and the
13 CFTC have a very strong history of collaboration
14 on market infrastructure and clearing issues and
15 on which the discussion can build.

16 So I listened with great interest to the
17 previous panel discussion and on recommendations
18 regarding CCP default management, and I would like
19 to congratulate the Committee on agreeing on such
20 a thorough and pragmatic set of recommendations
21 which are very important. What I'd like to do
22 today is follow on from that discussion by

1 focusing on one important element of CCP
2 resilience, the way in which CCPs test default
3 management preparations and procedures via default
4 management fire drills.

5 So as has already been said, I think
6 Susan referenced this, we know from past
7 experience that default of a material clearing
8 member is likely to be a stressful event for a
9 CCP. Realistic fire drills therefore help
10 maintain CCP and clearing member preparedness, and
11 they test the robustness of default management
12 arrangements. Fire drills are examples of the
13 importance of proper preparation in ensuring
14 readiness from likely and potentially challenging
15 events. Given that the default of a material
16 clearing member is likely to be accompanied by a
17 period of market stress, there is absolutely no
18 scope for poor performance by CCPs in managing a
19 default.

20 This is clearly recognized in regulatory
21 standards and regulations. For example, the
22 CPMI-IOSCO Principles of Financial Market

1 Infrastructure state that an FMI should involve
2 its participants and other stakeholders in a
3 testing and review of the FMI's default procedures
4 at least annually; know the preparedness extends
5 beyond just the FMI but also applies to its
6 participants and stakeholders as well. I think
7 that's really important. This is also mirrored in
8 European regulation, which requires CCPs to
9 regularly test and review their default procedures
10 to ensure they're both practical and effective,
11 and I understand that similar requirements also
12 exist in the Code of Federal Regulations as well.

13 Furthermore, and this has also been
14 referenced earlier this morning, it's very clear
15 that as a result of regulatory initiative, such as
16 mandatory clearing obligations, clearinghouses are
17 becoming increasingly important to global
18 financial markets and they are increasingly
19 interconnected with many key market participants.
20 It is therefore more likely than not that a
21 material clearing member default will impact
22 multiple CCPs at the same time.

1 So given this at the Bank of England, we
2 asked ourselves, to what extent does an
3 idiosyncratic or a single CCP fire drill scenario
4 on its own still constitute the scale of proper
5 preparation that we would expect to see? The
6 answer we came to, and it builds on some of the
7 recommendations of this Committee, is that
8 regulators and CCPs must devolve some fire drills
9 towards multiple CCP scenarios in order to provide
10 a realistic and proper simulation of a material
11 clearing member default. The consequences of such
12 a default would be visited upon a number of CCPs
13 simultaneously, so it makes sense to test the
14 response of multiple CCPs at the same time. This
15 is especially the case, since CCPs rely on their
16 members to provide bids in personnel and default
17 managements as the Committee has already talked
18 about this morning, and thus, there's a clear risk
19 that the demands of multiple CCPs could overwhelm
20 available capacity of clearing members. So it's
21 really important that we test these in a multiple
22 CCP format.

1 We took a first step in this direction
2 with a conclusion earlier this year of a fire
3 drill exercise involving RCH Limited, which we
4 supervise at the Bank of England, and Eurex
5 Clearing, which is supervised by our colleagues at
6 Bafin and Bundesbank. The scenario involved the
7 default of a common, hypothetical clearing member
8 clearing interest rate swaps and futures and was
9 integrated into the two CCPs annual fire drills
10 which were held in parallel. And along with our
11 colleagues from the Bafin and Bundesbank, we
12 observed the fire drills. We carried out
13 post-drill bilateral meetings with both of the
14 CCPs involved and seven of their largest clearing
15 members participating in the drill. And we also
16 reviewed all of their procedural documentations
17 associated with the drill.

18 The exercise yielded some valuable
19 findings which I'm going to move on to outline.
20 Our overall objective was to identify, assess, and
21 ultimately address weaknesses in default
22 management arrangements, which may not be apparent

1 when we tested them in a single CCP default
2 scenario. In particular, one area of focus which
3 this Committee is also focused on was the extent
4 to which clearing members' internal procedures
5 support their ability to seconded traders to
6 multiple CCPs in parallel in order to participate
7 in default management groups. This matters
8 because seconded traders bring valuable up-to-date
9 market and trading experience to CCP default
10 management groups, helping CCPs to return to the
11 matchbook as effectively as possible.

12 Our findings on this point were broadly
13 positive and I think reflect some of the comments
14 that we heard around the Committee earlier today.
15 Our view of a range of CCP members' procedural
16 documentation and how they behaved in the fire
17 drill found generally sound arrangements in place
18 when considering their commitments across the two
19 CCPs in question.

20 There are a small number of notable
21 exceptions which we're following up to help ensure
22 that best practices are broadly adopted.

1 We recognize that there are other
2 factors potentially affecting seconded trader
3 availability, and our findings are by no means the
4 last word in this area. Demand for trading
5 resources are likely to increase as more CCPs
6 complete and clear similar products, and this,
7 therefore, remains an area that we'll need to keep
8 under active review.

9 A second area we assessed was the
10 operational capacity of clearing members to
11 process auction files from two CCPs at the same
12 time. This matters because auctions are an
13 essential part of the default management process
14 and a successful auction with effective member
15 participation helps return the CCP to a matchbook
16 as soon as possible. It requires members to price
17 and assess the risk in the CCP's data file which
18 can be thought of as akin to an auction catalogue,
19 enough that contains tens of thousands, if not
20 hundreds of thousands of records describing the
21 contract specifications for each clear trade. And
22 we found considerable variation in clearing

1 members' ability to process these files in a
2 timely manner.

3 In a multiple CCP scenario, this could
4 throw into question some clearing members'
5 capability to consistently submit competitive and
6 timely auction bids to participate effectively in
7 a CCP's auction, and therefore, default management
8 process.

9 Our analysis attributed this variation
10 amongst clearing members to a combination of
11 insufficiently frequent testing of the process by
12 some clearing members, underdeveloped operational
13 systems, and the multiple auction file formats
14 used by the CCPs.

15 As a first step in dealing with this,
16 and again, this builds on some of this Committee's
17 recommendations that you've just agreed, I'm
18 pleased to say that the two CCPs in question, LCH
19 and Eurex, have agreed to work together to explore
20 opportunities to more closely align their auction
21 file format and contents and we're expecting them
22 to report back to us in due course on this issue.

1 The outcome we're seeking to achieve
2 here is to find a simple way of lifting some of
3 the operational burden from clearing members of
4 processing files in different formats and
5 therefore, increase the likelihood of effective
6 auction participation by members.

7 And there's a third area of
8 investigation. We identified a number of
9 prerequisites for running more effective fire
10 drills across multiple CCPs, and these include
11 more tightly defining the timing of the CCPs'
12 hedging activity in auctions to ensure that the
13 exercise robustly tests clearing members' capacity
14 to participate. It includes ensuring defaulted
15 portfolios material in size with correlated risks
16 above clearing members' business as usual risk
17 model assumptions. This helps ensure that the
18 exercise identifies and really tests clearing
19 members' risk management capacity. And also, it
20 includes enabling regulators to complete ex-post
21 reviews of clearing member auction bids,
22 particularly to assess the impact of capital or

1 liquidity costs on the bids that have been put
2 into the auction.

3 So jointly, the Bank of England, with
4 the Bafin and the Bundesbank, we've communicated
5 with the participating CCPs and clearing members
6 outlining our observations, and we'll be following
7 up as necessary over the coming period.

8 Looking ahead, we're building on this
9 exercise which took place in February in 2016,
10 aiming for the next multiple CCP fire drill with
11 regulatory involvement to take place in 2017. And
12 I'm very pleased to announced to the Committee
13 that building on our close collaboration with the
14 German authorities and with the CFTC, we've agreed
15 to extend the 2017 exercise further to run across
16 three CCPs, and CME, Inc., has agreed to join LCH
17 Limited and Eurex Clearing in a coordinated fire
18 drill in the first half of next year.

19 We're very much looking forward to
20 working with these three CCPs, as well as our
21 German and U.S. regulatory counterparts in
22 continuing to build and involve our approach.

1 We're in the process of defining the scenario and
2 objectives of that drill. It will certainly
3 include testing, hedging, and auctioning
4 procedures at CCPs and at members in stress market
5 conditions.

6 Building on some of the comments the
7 Committee made earlier today, we're also
8 considering testing the capacity of client porting
9 arrangements which we recognize is a key area of
10 focus on both sides of the Atlantic. And I'll be
11 happy to discuss the outcomes of next year's test
12 with the Committee at an appropriate juncture.

13 So just to conclude before I open up for
14 some questions. Fire drills, both idiosyncratic
15 and across multiple CCPs are part of the vital
16 work that CCPs, clearing members, and regulators
17 should take forward collaboratively in order to
18 promote safety, soundness and financial stability.
19 Building on this Committee's recommendations,
20 we'll continue to refine and adapt the way in
21 which they're run to ensure that they recognize
22 the increasingly complex interconnections within

1 global markets and the systemic importance of the
2 CCPs that serve them.

3 So I'm going to pause now and I thank
4 you for your attention. I'm very happy to take
5 questions, and I'll pass the floor back to Robert
6 for questions and discussion.

7 MR. STEIGERWALD: Thank you very much,
8 David. For the members of MRAC, in accordance
9 with the

10 usual custom, if you will use your name
11 tent to indicate your interest in asking a
12 question, this is now the time to share your
13 thoughts and inquire further about the comments
14 David has just made.

15 David, let me kick things off while
16 Richard is thinking of his question. There's
17 quite a lot of testing going on in this space.
18 There's back testing of models. There's stress
19 testing of the adequacy of CCP financial resources
20 and fire drills as well, all of this directed to
21 very important policy objectives, of course, but
22 it takes some time. It costs some resources. How

1 do you assess the overall benefits of these
2 related testing protocols in relation to the costs
3 associated with them?

4 MR. BAILEY: Thanks, Robert. It's a
5 very good question, and I think I'll tell you two
6 points in response.

7 The first thing is it's really important
8 that we actively test CCPs and clearing members'
9 resilience and their preparedness for default
10 management situations. In the discussions of the
11 Committee and my comments earlier today, I've
12 highlighted just how important that is.

13 The second point I'll make is we
14 recognize though that testing comes with overhead.
15 It comes with cost to both clearinghouses and to
16 their members and to the regulators as well.
17 These exercises, the more complex they get, the
18 more complex they are to organize, the more
19 involvement they need, and as regulators, we can
20 help with that, especially where we can help to
21 resolve some of the barriers of doing this on a
22 cross-border basis. Hence, some of the

1 discussions we've been having with CFTC and our
2 regulatory colleagues in Germany.

3 I think where possible, we will always
4 try and build and leverage on existing practices
5 that are taking place within industry. As I said
6 earlier, CCPs already have requirements in
7 regulatory expectations in multiple jurisdictions
8 that they will run, for example, default fire
9 drills on a periodic say annual basis. And so in
10 the case of the multiple CCP drills that I've
11 discussed, the one that took place in February
12 this year and the one we're going to do next year,
13 we'll seek to build on the existing tests that
14 already happened rather than require something
15 additional. So what we're seeking is
16 coordination, i.e., to run the fire drills
17 simultaneously and in parallel, rather than
18 request additional tests to be run.

19 There are, however, in other areas, new
20 tests that we will want to run, standardized
21 stress testing being a good example. Those are
22 new tests that can be built on existing stress

1 tests, and for those of you who haven't had a
2 chance to look at it yet, I would commend and
3 recommend you to read the excellent report that
4 the CFTC published yesterday. We had good liaison
5 with the CFTC staff as they developed the
6 exercise, and I think it's got a number of
7 thought-provoking conclusions and findings that we
8 can build on as regulators.

9 So I think in summary, Robert, what I'll
10 say is the kind of testing that you mentioned in
11 your question is really important. We need to
12 take it forward, and we need to think about how it
13 needs to evolve in light of increasing importance
14 of CCPs and increased interconnections in global
15 markets. But we will seek to do so in a
16 proportionate way building on existing exercises
17 where possible, mindful of the overheads and
18 commitments it brings to all involved, both in
19 terms of market participants and regulators.

20 MR. STEIGERWALD: Thank you, David.
21 Richard?

22 MR. MILLER: Thank you. This is an

1 interesting subject matter.

2 You know, from the perspective of
3 end-users who aren't intimate to the way these
4 fire drills work, I would be interested in hearing
5 a little bit more color on how you actually go
6 about doing this, what form it takes, and you
7 know, how you arrange the program. And second
8 question, if you get into the issue of porting in
9 future fire drills, would you envision including
10 end-users in the process so that they participate
11 in the fire drill as well?

12 MR. BAILEY: Thank you. So we're going
13 to take that question in two parts. The first
14 part is how we go about coordinating them and the
15 second point is your question around porting and
16 involvement of end-users.

17 So on the first point, in terms of how
18 the individual CCPs organize their fire drills,
19 then you've got a number of the experts sitting
20 already on the Committee who I'm sure will want to
21 comment on that. I think the additional value
22 that's added by the multiple CCP fire drill is

1 coordinating the timing, making sure that they're
2 run in parallel and that they're truly, actively
3 testing arrangements. So they need to be
4 stressful scenarios that really robustly test both
5 the CCP's and the clearing member's capacity to
6 support the exercises. So what we can bring is
7 running the exercises in parallel so that in the
8 case of the CCP of the fire drill I referenced,
9 that both CCPs were running out to their members
10 and asking for traders to be seconded at the same
11 time, that they were running their auctions at the
12 same time so clearing members were having to deal
13 with multiple requests. They were having to
14 price, size, and assess the risk associated with
15 multiple portfolios at the same time and respond
16 accordingly and work out could they bid as
17 aggressively in two auctions at the same time as
18 they might have done if they were only faced with
19 one portfolio at the time.

20 So what we bring is the additional
21 challenges of coordinating at the same time. And
22 I think next year when we run this across CCPs,

1 we'll see that the complexity will go up by an
2 order of magnitude again. The more and more we
3 can test that, I think the more lessons that we
4 will learn. And as I said, there were already
5 some very interesting findings. There were
6 already some points that we are taking and some
7 actions that we put on both CCPs and the clearing
8 members involved to ensure that the preparations
9 can be even better next time. So that's a
10 response to your first question.

11 Secondly, in terms of porting, what we
12 really -- well, we're still defining the scope and
13 the scale of the exercise for next year. Were we
14 to look at porting as part of that, there are a
15 number of aspects we could look at and we need to
16 define what's appropriate, what's proportionate,
17 but we certainly want to make sure that the CCPs
18 and the clearing members involved actively have
19 the procedures and purchases in place to
20 facilitate porting. It sounds, well, in practice
21 it sounds a relatively straightforward process,
22 but making sure that the CCPs can facilitate the

1 transfer of client positions from one clearing
2 member to the other, making sure that the
3 defaulting clearing member has in place the
4 capacity to provide the necessary information to
5 the CCP and to the receiving clearing member, of
6 making sure that the receiving clearing member has
7 the capacity to assess price and size of the risk
8 they're taking on and then operationally process
9 that could all be areas that we seek to look at.

10 You specifically asked whether it would
11 include clients in that. I can't say at this
12 point, but we'll certainly think about what the
13 challenge is for clients as well as clearing
14 members and CCPs are when we're developing the
15 test.

16 MR. STEIGERWALD: Dr. Lo?

17 MR. LO: So I want to thank you, Mr.
18 Bailey, for coming and describing your experiences
19 at the Bank of England. For whatever reason, the
20 Bank of England seems to be a real leader in
21 thinking about these issues, so it's very useful
22 to get your thoughts on it. I have two questions

1 about the fire drill that you conducted, and they
2 have to do with data and analytics.

3 So obviously, fire drills are very
4 expensive to run and there's no substitute for
5 them because they deal with a lot of the
6 operational aspects that you really can't tell
7 unless you go through the exercise. But I wonder
8 whether there are ways of running ongoing fire
9 drills virtually by collecting data for the entire
10 CCP network, mapping that network, and being able
11 to do simulated shocks over the course of even,
12 you know, days or weeks and in a way that is a lot
13 less intrusive. It may not give you the same
14 information, but it can provide you with some
15 useful ideas for where the pressure points are and
16 then you can focus on those during the fire
17 drills. So that's one question. Is that
18 something that's feasible or worthwhile to explore
19 and has the Bank of England looked into that?

20 And the second issue is that after every
21 fire drill there's an enormously valuable set of
22 data that you collect from the results. Is it

1 possible to make that data available in some
2 anonymized form to academics to study to get a
3 sense of how these markets work under distressed
4 scenarios? Even if they're simulated, they could
5 be actually very valuable for quantifying some of
6 the things that we can only guess at with existing
7 market data.

8 MR. BAILEY: Thank you. Thank you for
9 the question. So I'll take that again in two
10 parts.

11 The first question was around the
12 potential to run ongoing, as you described them,
13 virtual fire drills or tests, and I think taking a
14 step back, what are the real values of running
15 fire drills. And I'll split that into two points.

16 The first thing is assessing the
17 financial resilience of the CCP and the clearing
18 members' capacity to absorb or participate in
19 auctions and the financial impacts. The second
20 point, and equally as important, is the
21 operational capacity of CCPs and clearing members
22 to run the default management process. And I

1 think that second point you can only really test
2 via the fire drills.

3 In terms of assessing the financial
4 impacts of default, you're quite right that there
5 are exercises that can be run on an ongoing basis.
6 I think, again, just referring back, and I'm going
7 to start charging the CFTC for every time I plug
8 this report of theirs yesterday, so I'll submit a
9 bill to Chairman Massad later on, but the report
10 published yesterday was a really good example of
11 how regulators can do that kind of testing
12 virtually using the data that's reported to us.
13 From a Bank of England perspective, that is
14 something that we are thinking of doing. In fact,
15 CPMI-IOSCO, learning the lessons and looking to
16 the lessons learned from authorities that have
17 done this, such as the CFTC, such as in Europe,
18 ESMA, are looking to define standards around
19 standardized stress testing. From the Bank of
20 England's perspective, we will look to those when
21 they are defined next year and look to develop
22 stress tests that would allow us to assess what

1 the financial impacts are and the financial
2 resilience of CCPs and the potential cause they
3 could make of their clearing members. So I think
4 we can do that. But on its own, just virtually
5 testing the financial resilience of the system
6 doesn't pick up the important operational aspects
7 that the fire drills actually test. So that's the
8 first point.

9 The second point was around data, and
10 you're not the first academic to come asking for
11 data. I think what we're taking away to think
12 about, we need to be very careful that the data
13 used here is, first of all, importantly market
14 sensitive. It is of clearing members' actual
15 positions at the time that we run the exercises.
16 And secondly, in many cases, it is constrained and
17 proprietary in nature, and therefore, there will
18 be some quite formidable legal aspects that we
19 would need to think to. But the point is taken
20 that should there be any data that we can
21 released, then it could be used for valuable
22 academic purposes. So I know that point.

1 MR. STEIGERWALD: Dennis?

2 MR. MCLAUGHLIN: Thanks. Very
3 interesting. Did you give any thought, or have
4 you given any

5 thought to how one would test nondefault
6 losses in a fire drill?

7 MR. BAILEY: So, Dennis, I should have
8 asked you that question. In fact, I might do
9 afterwards, and in fact, I might submit a
10 regulatory action for LCH to come back to me with
11 a plan of how to do that.

12 I think you raise a very important
13 point. When it comes to a number of aspects of
14 CCP resilience and recovery, we think about -- we
15 focus on -- understandably, we focus on the
16 default of a substantial clearing member. That's
17 a key risk that CCPs have developed and through
18 regulatory means we have forced more trades into
19 clearing. Precisely so, we can remove some of the
20 bilateral risks that existed in the system
21 previously, and we can ensure that those risks are
22 essentially and to very high and transparent

1 standards and it can be seen to do so. That very
2 much promotes financial stability and it promotes
3 confidence in the system.

4 But CCPS are also exposed to other forms
5 of losses that may not arise purely through the
6 default of a clearing member, and we need to think
7 quite carefully about how we assess CCPs and their
8 members' abilities to deal with that. So as far
9 as I'm aware, we haven't seen a fire drill run
10 that takes into consideration nondefault losses
11 but it's only something that we should think
12 about. And it's also an important consideration
13 of the recovery arrangements that have been
14 developed under CPMI-IOSCO and which CPMI-IOSCO
15 are currently reviewing is thinking about what
16 recovery arrangements and what resources are in
17 place to allocate losses and deal with nondefault
18 losses where they exceed a CCP's capital. So I
19 think it's something that we need to think about.
20 Any input that members of the Committee would like
21 to give to us as we think about that I think would
22 be very valuable.

1 MR. STEIGERWALD: Susan?

2 MS. O'FLYNN: Well, firstly, you know, I
3 think from a clearing member perspective, we
4 welcome joint rules like the ones that were run in
5 February, and obviously, as an observer and both a
6 participant, it was a very useful process to be
7 able to test our capability to both bid and
8 operationally intakes files north of 12,000 swaps
9 I think was one of them. And it's very
10 encouraging to hear that there's going to be a
11 three-way process with CME next year because that
12 effectively reflects the entire IRS market, so we
13 think that will be really a good, dry run of
14 potentially what could happen. If there is a
15 significant clearing member default, we expect
16 there to be split risk so, you know, you need to
17 have the whole universe of players involved.

18 It's also very -- I wouldn't say
19 comforting but it's good to hear that the auction
20 file format finding is something that is already
21 kind of in process to create something that's more
22 consumable from a clearing member perspective to

1 be able to bid well and efficiently within the
2 timeframe. That's obviously one of the
3 recommendations here today.

4 You know, back to I think my initial
5 introduction, I think it's very important to think
6 about multiproduct drills. We're talking about
7 swaps specifically and ETD, but as more products
8 become clearable, it is likely that a significant
9 clearing member default will default in repo
10 exchange trader derivatives and, you know, other
11 forms of OTC derivatives. How do we think about
12 drills looking at the cross products and
13 coordination and capacity? And thirdly, to
14 Dennis's point around non-default losses, it's
15 been a topic of great debate in the recovery and
16 resolution forums. I think we would very much
17 welcome a drill, looking at that as an
18 alternative, and also the involvement of clients
19 just to then, I suppose, for want of a better road
20 test, the communication policy that Dennis
21 outlined earlier.

22 MR. BAILEY: If I could just respond to

1 a couple of those points. That's very helpful,
2 Susan. Thank you for the comments.

3 I think in terms of the three points
4 that you made, firstly, in terms of the file
5 formats and very much building on recommendations
6 that this Committee has just approved, we do see
7 that to be scoped to make enhancements in terms of
8 consistency. I wouldn't have or want to lay all
9 of the work at the CCP's feet. I think there is
10 important work for clearing members to do in
11 ensuring that they have the systems and the
12 capacity to absorb those files as they're
13 developed. We'll seek to make it as easy as
14 possible, but some of the findings of our test
15 back in February was clearing members weren't
16 fully prepared from an operational capacity to
17 absorb more than one file at a time and run the
18 price and run the risk on a number of portfolios
19 at the same time. So there's work to be done both
20 at the CCPs and at the clearing members.

21 And then my second point is you talked
22 about multiple products and I fully agree. I

1 think that is a further revolution that we can go
2 through. We also need to be cognizant as we go to
3 multiple CCP, multiple product testing, the
4 complexity of the exercise gets more and more each
5 additional step that we add and I'm not sure that
6 complexity increases on a linear basis. I think
7 it's increasingly more complex the more facets you
8 add to the test. So I think we will go down that
9 route in due course. We'll probably go one step
10 at a time to make sure that we can learn the
11 lessons suitably at each stage.

12 And I think the same comment applies to
13 looking at tests to involve clients (inaudible)
14 yes, the places we'd like to go. We just need to
15 make sure that we take sensible and proportionate
16 steps to get there rather than rushing to make the
17 test as complex as possible because I think there
18 are enough benefits and enough lessons we can
19 learn from each incremental stage that we will
20 make the process more robust, more resilient at
21 each stage as we increase in complexity step by
22 step.

1 MR. STEIGERWALD: Kim?

2 MS. TAYLOR: I understand that the
3 purposes of the joint drills and the simultaneous
4 auctions probably maximize certain types of
5 stressors for the clearing members to absorb, but
6 I'm wondering whether the movement to assume that
7 the auctions should be held simultaneously would
8 actually turn out to be the market stability
9 maximizing outcome. Because I think that it could
10 be that holding auctions sequentially would
11 actually allow people to bid on the second and
12 third pieces or the second and umpteenth pieces of
13 the portfolio exposure with knowledge of what
14 they've already won or lost and it might actually
15 benefit in terms of the bids that we would get for
16 the different pieces of the exposure. So I'm
17 interested in thoughts on including that type of
18 sequential auction rather than just simultaneous
19 auction in the process.

20 MR. BAILEY: That's a really good point,
21 Kim. Thanks for raising it. I should just be
22 clear. My earlier remarks, I wasn't implying that

1 the auction should be run at exactly the same time
2 simultaneously, but we do need to think about the
3 challenges involved in the timing of having a
4 number of auction processes going on at roughly
5 the same time.

6 Certainly, in the default fire drills,
7 one aspect we can test is running them at the same
8 time. That provides challenges of its own from an
9 operational perspective. But we do need to think
10 about in a real-life default scenario, what's the
11 best outcome for the market as a whole for
12 efficiency and for stability in terms of timing of
13 those auctions. And there are a number of aspects
14 at play. So, for example, I can imagine if you've
15 got a number of CCPs, there might be a rush to be
16 the first one to run your auction because you can
17 give away your positions when members have got the
18 maximum capacity to absorb those positions. That
19 might be one outcome.

20 A second point we need to think about is
21 what's realistic in terms of coordination between
22 CCPs at the time that you're merging a stressful

1 material member default.

2 And thirdly, how much collaboration can
3 we expect, or how much interaction can we expect
4 given the legal constraints that you're under and
5 your own fiduciary duties to your shareholders.

6 So there's a number of factors at play,
7 and I think that's where close collaboration
8 between the regulators, as well as the CCPs can
9 come into play because in a default management
10 scenario across multiple CCPs, we would absolutely
11 be talking to our colleagues at the CFTC, at other
12 regulators both on this side of the Atlantic and
13 in Europe. That doesn't mean to say we would
14 force a certain ordering, but we just need to
15 think about some of the challenges and how we
16 might manage the best outcome for the stability of
17 the system as a whole. So I think you've raised
18 some really good points that maybe we can test as
19 we move into future default fire drills and we
20 evolve sort of the best practice that comes out of
21 them.

22 MS. TAYLOR: And I think some of the

1 comments that you're making also kind of reinforce
2 some of the comments that we made earlier about
3 our concerns about kind of an ex ante agreement
4 that the lockstep process is going to be like this
5 when we don't, any of us know the exact
6 circumstances that the CCPs or the market as a
7 whole will be facing at the time of the crisis.
8 So I think we encourage the process to allow for
9 transparency in general about the process without
10 kind of tying the industry's hands to a specific
11 process that might not actually be the best one at
12 the time.

13 MR. STEIGERWALD: David, recent events,
14 in particular the immediate aftermath of the
15 U.K.'s Brexit vote reminded us of the critical
16 importance of intraday liquidity, in particular
17 really time-critical liquidity associated with
18 variation settlements at CCPs. Now, you've
19 cautioned us against rushing to include too much
20 complexity in these fire drills for good reason.
21 I wonder, can you comment at all on the extent to
22 which liquidity issues are already incorporated in

1 the fire drills and the plan going forward to
2 incorporate realistic simulations of actual
3 liquidity constraints in future fire drills?

4 MR. BAILEY: Thank you, Robert. So
5 there are a couple of aspects there, and I'm
6 going to take them separately. The
7 first thing is to talk about liquidity management
8 and its inclusion in the various tests that we
9 run. And the second point, I'll come back to the
10 first comment you made around some of the margin
11 calls we saw back in June.

12 So the first one, in terms of liquidity
13 aspects and some of the tests that we run. So
14 that was not liquidity aspects. Well, I should
15 take a step back. First of all, liquidity and
16 liquidity management is just important as a number
17 of the other risks that CCPs and their members are
18 managing. Whether that's credit risk or whether
19 it's operational risk, it's equally as important,
20 and it's equally a focus of regulators. It wasn't
21 specifically a test of the default fire drill
22 exercise that we ran back in February, and again,

1 I think it is something that we can usefully pick
2 up in, for example, some of the stress tests that
3 we expect CCPs to run on their own, but also some
4 of the standardized stress testing that I referred
5 to earlier. And I recognize again it wasn't the
6 focus -- it's my understanding it wasn't a
7 specific focus of the CFTC's exercise, but I think
8 it can be of future standardized stress testing.
9 And it's really important that we do that because
10 the calls that CCPs make for the default waterfall
11 and some of the processes through the auctions can
12 place or have the potential to place significant
13 liquidity calls, liquidity needs, liquidity
14 burdens onto clearing members and we need to
15 understand the interconnections that we have there
16 and some of the risks that arise as a result.

17 So I think it will be a focus going
18 forward. Liquidity risk management is already a
19 focus, but in terms of the default fire drill
20 exercises, and specifically, some of the stress
21 testing exercises that we run going forward, I
22 think liquidity will be an absolutely important

1 aspect of that. So that's the first point.

2 The second point was you noted some of
3 the calls from back in June, and specifically, as
4 you said, referring to intraday variation margin
5 payments. I think I'll just say two things. The
6 first one is that variation margin is an important
7 aspect of the CCP risk management process. It
8 should be no surprise to anyone that CCPs call
9 variation margin on at least a daily basis. That
10 is enshrined within the regulatory expectations
11 that we have. What I think we can look at, and we
12 should look at, is some of the processes through
13 which variation margin is called on an intraday
14 basis because that can pose some challenges. And
15 it does vary from CCP to CCP, so that is something
16 we're thinking about. But the concept of calling
17 variation margin, whether a large market move or
18 to cover market moves is an inherent part of the
19 CCP process. It should not be a surprise; it
20 should be something that CCPs are expecting to do.
21 In fact, they're required to do. It should be
22 something that clearing members and clients are

1 expecting. What we need to look at and what we
2 should think about is the process through which
3 intraday variation margin is called.

4 MR. STEIGERWALD: Kim?

5 MS. TAYLOR: If I could just add not
6 really a question but more of a comment to that.
7 I definitely agree that variation margin is a very
8 important risk management tool and that the market
9 should be expecting that the CCPs would use it as
10 part of their risk management. The other side of
11 that though, I think the market could fairly have
12 the expectation that the CCP would not just
13 collect losses but would also pay out profits,
14 especially when there are situations as we've seen
15 recently where there have been big swings in one
16 direction and then swings back. So that is a way
17 to help CCPs manage their risk while also not kind
18 of exacerbating the risk of other elements in the
19 chain of the market.

20 MR. STEIGERWALD: Dennis?

21 MR. MCLAUGHLIN: Yeah, just a slightly
22 different question.

1 So you've been looking at more of the
2 operational reasons that the fire drill could
3 fail. Have you seen, or can you share with us any
4 reasons why you might think there's a structural
5 reason why a fire drill might fail? Not an
6 individual little operational deficiency
7 somewhere, but are there structural reasons why
8 something might fail?

9 MR. BAILEY: So it's a good question,
10 Dennis. I'm pausing because I'm thinking hard.
11 You can probably hear the clock turning. It's
12 late in U.K. time so I need a little bit of time
13 to think about that.

14 It's something we should think about,
15 and we need to be cognizant that the default
16 management process, where the failure of large
17 clearing members are involved, is likely to take
18 place in very stressed market conditions, and we
19 need to think about -- one of the things we can
20 think about as we increasingly run more complex
21 fire drills involving more CCPs, more members, and
22 more products as we talked about, whether there

1 are constraints placed on that process by the
2 level of volatility in markets or simply the
3 number of participants that are involved. So your
4 question is a good one and one I would certainly
5 need to take away and think about, and I think we
6 need to flush out as we run more and more complex
7 fire drills. But obviously, if CCPs or their
8 members already can see some structural
9 constraints to fire drills being successful, then
10 that is something we would want to consider now,
11 as early as possible, so we can aim to remove
12 those structural constraints where possible and
13 think about whether we need to evolve the default
14 management processes accordingly.

15 MR. STEIGERWALD: Thank you, David. I
16 can say personally I've learned quite a lot about
17 what has been going on with respect to fire drills
18 and the expectations for such exercises going
19 forward. Thank you for your time and sharing your
20 thoughts with us. On behalf of the Committee,
21 we're grateful for your time.

22 MS. WALKER: At this time, and keeping

1 with meeting agenda, I would like to thank Robert
2 Steigerwald for facilitating the discussion, and
3 Mr. David Bailey for his insights during our
4 second panel.

5 I will now turn to Commissioner Bowen
6 and the other commissioners and the chairman for
7 any closing remarks.

8 COMMISSIONER BOWEN: First, let me say
9 that the early finish I don't think is in response
10 to my growling stomach but I think it is a
11 testament to how much hard work and discussion
12 really took place beforehand. So would the
13 chairman or Commissioner Giancarlo like to --

14 CHAIRMAN MASSAD: Just thank you again
15 for not only a very productive, but a very
16 efficient meeting.

17 COMMISSIONER GIANCARLO: Here, here.

18 COMMISSIONER BOWEN: So today's vote
19 obviously is a culmination of two years' worth of
20 work on CCP default management. As we said before
21 at the first MRAC meeting in April 2015, the CCP
22 members presented their default plans and the MRAC

1 discussed the strengths and weaknesses of those
2 plans. As you know, in that discussion two
3 questions arose. One, how can CCPs' plans better
4 reflect the likely market conditions during
5 default? Two, how can CCPs better coordinate
6 their efforts to prevent and manage a participant
7 default? And then in November 2015, the
8 Subcommittee presented draft recommendations in
9 answer to the first question. On June 27, 2016,
10 the Subcommittee presented a draft response to the
11 latter, and now today, the Subcommittee has
12 presented its combined final recommendations to
13 the MRAC and these recommendations have been
14 presented to the Commission.

15 First, let me say that I could never
16 have been more proud than I am today of the work
17 of this Subcommittee and the Full Committee. It
18 is no small task to bring together market
19 participants from such diverse backgrounds to
20 agree on such knotty policy issues. I'm well
21 aware that probably no one got the perfect set of
22 recommendations and everyone probably made some

1 compromises.

2 So I want to give a hearty thank you to
3 the Subcommittee members, particularly Tom Kloet
4 who started this process, and Susan O'Flynn who
5 ably ended it. Susan spent many long days and
6 nights hammering out consensus and we owe her a
7 lot for that. And thank you to the MRAC members
8 overall who thoughtfully and tersely engaged on
9 these issues to arrive at their vote. I also want
10 to thank today's guest speakers and presenters.

11 I also want to take the opportunity to
12 thank the staff, the chairman, and Commissioner
13 Giancarlo again for their continued support of
14 this Committee. And I want to say a final thank
15 you to my staff, to Jason, Justin, Vontrece, and
16 especially Petal, our designated federal officer,
17 for the many hours, numerous phone calls, and
18 artful diplomacy in making sure that everyone not
19 only had a voice but were heard throughout the
20 process. I'm very proud of the work of this
21 Committee that it's done so far, and I look
22 forward to what MRAC can do in the future. We

1 know that there's no shortage of market risk and
2 market structure issues in the derivatives market
3 today. And with that in mind, I invite the public
4 to comment on what issues they believe MRAC should
5 tackle in the upcoming years.

6 Thank you so much again, everyone.

7 (Applause)

8 MS. WALKER: Just a couple of quick
9 logistical things before we need. Please,
10 members, do take your portfolios with you and use
11 them to bring materials back and forth to your
12 future meetings. If there is any paperwork that
13 needs to be handed in, please hand it in before
14 you go. And those going to lunch, please gather
15 over here near the door. Our reservation is now
16 for 12:30.

17 And with that the meeting is adjourned.

18 (Whereupon, at 12:10 p.m., the
19 PROCEEDINGS were adjourned.)

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CERTIFICATE OF NOTARY PUBLIC

DISTRICT OF COLUMBIA

I, Carleton J. Anderson, III, notary public in and for the District of Columbia, do hereby certify that the forgoing PROCEEDING was duly recorded and thereafter reduced to print under my direction; that the witnesses were sworn to tell the truth under penalty of perjury; that said transcript is a true record of the testimony given by witnesses; that I am neither counsel for, related to, nor employed by any of the parties to the action in which this proceeding was called; and, furthermore, that I am not a relative or employee of any attorney or counsel employed by the parties hereto, nor financially or otherwise interested in the outcome of this action.

(Signature and Seal on File)

Notary Public, in and for the District of Columbia

My Commission Expires: March 31, 2017