MINUTES OF THE U.S. COMMODITY FUTURES TRADING COMMISSION'S DECEMBER 17, 2020 MEETING OF THE GLOBAL MARKETS ADVISORY COMMITTEE

The Global Markets Advisory Committee (GMAC or Committee) convened for a public meeting on Monday, December 17, 2020, at 9:15 a.m., via teleconference hosted by the U.S. Commodity Futures Trading Commission (CFTC or Commission). The meeting consisted of two panels. The first panel addressed regulatory developments to advance global derivatives clearing. Panelists presented on a variety of topics, including the CFTC's rulemaking concerning registration with alternative compliance for non-U.S. derivatives clearing organizations, EMIR 2.2, and U.S. client access to central counterparties in the Asia-Pacific region. The second panel looked back at derivatives clearing in 2020, with a particular focus on the impact of the COVID-19 pandemic on global clearing. Panelists discussed, among other topics, the impact of the pandemic on clearing volume, margin requirements, and CCP operations.

GMAC Members in Attendance

Angie Karna, GMAC Chairwoman and Nomura Securities International, Inc., Managing Director, Legal Department and Head of Legal for Global Markets, Americas
Chris Allen, Standard Chartered Bank, General Counsel, Clients & Products
Ted Backer, Morgan Stanley, Global Head of Listed Derivatives Execution
Ashely Belich, RBC Capital Markets, Head of Global OTC Derivatives & Dodd Frank Advisory
Darcy Bradury, D.E. Shaw & Co., L.P., Managing Director
Maria Chiodi, Credit Suisse Securities (USA) LLC, Managing Director
Clive Christison, BP, Senior Vice President Pipeline, Supply & Optimization for Fuels North America
Joseph Cisewksi, Better Markets, Consultant
Jim Colby, Coalition for Derivatives End-Users, Representative
Gerry Corcoran, R.J. O'Brien & Associates, LLC, Chairman of the Board and Chief Executive Officer
Sunil Cutinho, CME Clearing, President
David Goone, Intercontinental Exchange, Inc., Chief Strategy Officer
Paul Hamill, Citadel Securities, Global Head of Fixed Income, Currencies and Commodities
Amy Hong, Goldman Sachs, Head of Market Structure Strategy
John Horkan, LCH Group, Group Chief Operating Officer and Head of North America
Adam Kansler, IHS Markit, President, Financial Services
Robert Klein, Citigroup Global Markets, Managing Director & General Counsel
Agnes Koh, Singapore Exchange Limited, Chief Risk Officer
Ben MacDonald, Bloomberg LP, Global Head of Enterprise Products & President of Bloomberg's SEF and SDR

Erik Tim Müller, Eurex Clearing AG, Chief Executive Officer
Murray Pozmanter, DTCC, Managing Director & General Manager
Thomas Sexton, National Futures Association, President & Chief Executive Officer
Jessica Sohl, HC Technologies, Partner & President
Thane Twiggs, Cargill Risk Management, Chief Compliance Officer
Supurna VedBrat, BlackRock, Managing Director & Global Head of Trading
Masahiro Yamada, JP Morgan Securities, LLC, Managing Director & Head of America's Cross Asset Structuring

CFTC Commissioners and Staff in Attendance
Dawn D. Stump, Commissioner and GMAC Sponsor
Heath Tarbert, Chairman
Rostin Behnam, Commissioner
Dan Berkovitz, Commissioner
Brian D. Quintenz, Commissioner
Andrée Goldsmith, GMAC Designated Federal Officer (DFO)
August Imholtz, Special Counsel, Clearing Policy Branch, Division of Clearing and Risk
Abigail Knauff, Special Counsel, Clearing Policy Branch, Division of Clearing and Risk
Sayee Srinivasan, Deputy Director, Risk Surveillance Branch, Division of Clearing & Risk

Invited Speakers in Attendance
Sean Downey, Executive Director, Clearing, Risk, & Capital Policy, CME Group
Patrick Pearson, Head of Financial Markets Infrastructure, Directorate-General for Financial Stability, Financial Services and Capital Markets Union, European Commission
Nicholas Rustad, Chairman, Board of Directors, FIA
Dmitrij Senko, Chief Risk Officer, Member of the Executive Board, Eurex Clearing AG
Nagaoka Takashi, Deputy Commissioner for International Affairs, Japan Financial Services Agency

I. Opening Remarks

Ms. Goldsmith called the meeting to order.

Commissioner Stump then gave her opening remarks, welcoming and thanking all who were attending. She discussed the GMAC's contributions to the CFTC's work. For example, at the last meeting, the Committee's discussion focused on the Commission's need to better align its global regulatory expectations for margin requirements on transactions not subject to central clearing. Since then, the Commission has acted on a number of recommendations received from the Committee, and continues to consider the GMAC's other recommendations which came up from the Subcommittee on Margin Requirements for Non-Cleared Swaps. Following this, she stated that the focus of this meeting would be to advance clearing in the global derivatives markets. She then introduced the two panels, stating that they would focus on (1) the regulatory developments affecting the global clearing system, and (2) a look back at global derivatives clearing over the course of 2020, with a focus on the impact of COVID-19.

Next, Chairman Tarbert gave his opening remarks. He stated that many of the Commission's achievements were built on the great work of the GMAC under Commissioner Stump's leadership. He stated the Committee was critical in advancing important ideas involving central counterparties (CCPs), clearing more generally, and related issues affecting the global markets. He thanked all on the GMAC for their service.

Commissioner Quintenz then thanked Ms. Goldsmith for her leadership on the staff level, and also thanked Commissioner Stump. He highlighted how the GMAC meetings have focused on topics of critical importance to the Commission and the markets, and how the GMAC meetings have informed certain actions that the Commission has taken. He stated he was looking forward to the panels and that they would address the key issues of home country deference surrounding CCP recognition, examination, and resiliency, while acknowledging that the Commission's regime is based on intermediaries, infrastructure, and registration.

Then, Commissioner Behnam specifically thanked Ms. Goldsmith, Commissioner Stump, Ms. Karna, and all members of the GMAC for their hard work. He highlighted the two main purposes of today's meeting as evaluating clearing in 2020 and planning for the future.

Finally, Commissioner Berkovitz echoed the statements of the other Commissioners and stated that the Committee's work reflects excellence in government decision-making and public participation. He thanked Commissioner Stump for her leadership and the Committee for providing recommendations that are useful to the CFTC and further the objective of harmonization and liquidity in global markets. He also thanked Ms. Karna and Ms. Goldsmith for their contributions.

II. Panel I: Regulatory Developments to Advance Global Derivatives Clearing

Ms. Goldsmith introduced the first panel. Mr. Imholtz and Ms. Knauff gave the first presentation on the CFTC's recent rulemaking concerning registration with alternative compliance for non-U.S. derivatives clearing organizations (DCOs). Mr. Imholtz began by stating that in this rulemaking, the Commission amended its regulations to provide a second registration option for non-U.S. DCOs that clear swaps for U.S. persons, including for futures commission merchant (FCM) customers, if those DCOs meet certain eligibility criteria. He explained that there were two primary considerations that drove this rulemaking. First, the Commission recognized the existence of regulatory overlap for non-U.S. DCOs. Second the Commission recognized that there are significant differences in the extent to which non-U.S. DCOs clear swaps for U.S. persons.

Under the rulemaking, a non-U.S. DCO will be eligible for registration with alternative compliance if the DCO is in good regulatory standing in its home country, there is a memorandum of understanding in place between the Commission and the home country regulator, the Commission determines that the DCO's compliance with its home country regulatory regime will satisfy the DCO core principles in the Commodity Exchange Act, and the DCO does not pose a substantial risk to the U.S. financial system. The Commission may determine that a non-U.S. DCO poses substantial risk to the U.S. financial system if: 1) the DCO holds 20 percent or more of the required initial margin of U.S. clearing members for swaps across all registered and exempt DCOs, and 2) 20 percent or more of the initial margin requirements for swaps at that DCO is from U.S. clearing members. In such circumstances, the Commission could determine that the DCO is not eligible for registration with alternative compliance.

Ms. Knauff then presented on the regulatory requirements and procedures associated with the alternative compliance framework. She highlighted two notable differences between the alternative compliance framework and the original registration framework. First, those DCOs subject to the alternative compliance framework could comply with the DCO core principles through compliance with the applicable legal requirements in their home country. Second, the Commission has exempted these DCOs from the rule submission requirement in Part 40, with the exceptions of rule filings related to customer protection and swap data reporting. All registered DCOs, including those DCOs registered under the alternative compliance framework, must comply with the Part 45 swap data reporting requirements, the Commission's customer protection regime regulations, and those requirements which are designed to protect the safety of funds and assets belonging to clearing members and their customers. If the home country regulatory regime lacks legal requirements that could correspond to a particular core principle, the applicant will need to explain how it would satisfy that core principle. The order for registration for DCOs registered under the alternative compliance framework will contain conditions that it must comply with, and these DCOs will have periodic and event-specific reporting requirements. The Commission shall also retain the discretion to modify the terms and conditions of alternative compliance.

Ms. Karna then introduced the next panelist, Mr. Pearson, who presented on the finalization of EMIR 2.2. He discussed how, just like the CFTC, the European Union (EU) has been looking at how to consider risk posed by non-EU CCPs operating in their markets. The EU identified specific risks that would be relevant in determining if a CCP from outside Europe could operate in their markets. These include the nature of the transactions cleared (in particular, the complexity, risk profile, and maturity of the transactions), the effect of a failure or disruption of a third-country CCP on the stability of the EU's financial markets, the structure of a CCP's membership (in particular, the level of transparency and diversity of membership), the extent to which a CCP's business would involve trades denominated in the Euro or in other EU currencies, whether there would be alternative CCPs offering similar services to those offered by a non-EU CCP in the European markets, and how exposed EU participants and clients would be to a third-country CCP

Mr. Pearson stated that they also learned a great deal from the CFTC and other regulators in determining the EU framework for third-country CCPs. What they learned informed their decision to include quantitative thresholds for determining whether a third-country CCP would pose a systemic risk to the European Union. Mr. Pearson explained that, with regard to those CCPs that are not deemed systemically important in the EU, the EU will continue to apply full mutual recognition and deference. On the other hand, for third-country CCPs that are deemed systemically important in the EU, there are certain additional requirements that must be met in order for the CCP to continue operating in the EU. Mr. Pearson explained that the EU has not identified any U.S. DCOs as systemically important in the EU. He also stated that the European Commission has set up a new supervisory authority within ESMA to apply and implement the new rules and requirements.

Ms. Karna then introduced Mr. Nagaoka. Mr. Nagaoka stated that the past year and volatility related to COVID-19 have reconfirmed the importance of the role CCPs play within the financial system. Mr. Nagaoka noted that, as part of the Japanese presidency of the G20, market fragmentation was one of the top priorities, and that Japan has been working through IOSCO to identify sound practices regarding deference of regulation and supervision between jurisdictions. IOSCO's market fragmentation follow-up group published a report in June 2020 that included best practices to mitigate such fragmentation.

Next, Mr. Nagaoka discussed Japan's initiatives regarding foreign CCPs. Japan has a two-tier system for allowing foreign CCPs to operate their clearing business in Japan. Generally, foreign CCPs are required to obtain a license prior to their operation in Japan. However, there is also an exemption system where foreign CCPs may be exempted from licensing if a default by that CCP would have a minor impact on Japan's capital market. With regard to licensing, the requirements applicable to foreign CCPs are more lenient than those applicable to domestic CCPs. With regard to the exemption framework, Japan recently made some revisions to the framework to allow exemptions to be granted without time limitation, on the condition that cooperation arrangements are in place with the exempted CCP's regulator. The revisions to the exemption system were based on deference to the foreign CCP's home jurisdiction. They have resulted in enhanced accessibility to Japanese markets, and have provided market participants with additional ways to risk manage. In regard to the CFTC's finalized exempt DCO rule, he also emphasized the importance of continued discussion on whether to allow exempt DCOs to clear swaps for U.S. customers.

Ms. Karna next opened the floor for questions. Among other items, topics discussed included: whether the varying approaches to regulatory deference were sound, whether the regulators went far enough in allowing a home country regulator to take the primary role in supervising the CCPs in their own jurisdiction, the level of protection offered by the Japanese client money-protection regime for U.S clients clearing in Japan, the hurdles in determining whether a non-Japanese CCP would get full registration in Japan as opposed to an exemption, and the manner in which clearing requirements are distinguished for CCPs abroad with regard to OTC swaps as opposed to futures.

III. Derivatives Clearing: 2020 in Review

Ms. Karna then introduced the next panel, which included a series of presentations on the impact of the coronavirus pandemic on global clearing.

Mr. Rustad was introduced and presented a clearing member's perspective on CCP margin requirements during the market volatility caused by the pandemic. He explained that the cleared derivatives market withstood the shock during the market volatility due to post-crisis reforms, including with regard to central clearing and counterparty risk management.

Nevertheless, Mr. Rustad stated that three areas could be improved further. First, the procyclicality of CCP margining requirements contributed to the overall level of stress in the financial markets. Second, the steep and rapid increase in CCP initial margin requirements created funding pressures on FCMs and their clients. Third, unscheduled intraday margins were hard to predict and sometimes not transparent, making it hard to plan in advance. He discussed the data at length and emphasized that while each clearing member is responsible for the risk they bring, there is still a need to ensure that appropriate levels of margin are set for the industry as a whole. He stated that two or three margin breaches per contract per year should generally be expected, but that there was much more than that at the start of the pandemic. According to Mr. Rustad, the level of margin increases during the spring volatility was too great, and therefore margin either started too low or ended up too high. One solution to this issue could be to set appropriate margin floors, so that margin does not fall too low during quieter times. He suggested that margin methodologies be further reviewed to see if they could be strengthened, and that margin frameworks be further back-tested to test the potential for a large and sudden increase in margin requirements. He also suggested that the framework for intraday calls should be revisited and offered a number of potential improvements for the framework, including that routine intraday calls be made at the same time every day, intraday calls should clearly separate initial margin and variation margin, and ad hoc intraday calls should be made on a limited basis.

Ms. Karna then introduced Mr. Downey. He agreed with the notion that central clearing performed very well during the COVID-19 pandemic stress, that the key measure to examine is aggregate margin changes during this time period, and that it is very unlikely we will see another event like this during our lifetime. He detailed the CME's analysis regarding the COVID-19 pandemic stress. The CME emphasized the importance of targeted anti-procyclicality measures in CCP risk management. He also noted that clearing members could have met their obligations in U.S. treasuries if they needed cash for other purposes, and that there was not a dash-for-cash at the CME.

Mr. Karna then introduced Mr. Senko, who provided Eurex Clearing's perspective on the crisis. From Eurex's perspective, 2020 was an important year where the financial architecture that was designed in 2010 was put to the test. He suggested there was consensus to back test data in-depth to assess the best trajectory of margins and that Eurex would be happy to contribute to this discussion.

Mr. Karna then introduced Mr. Srinivasan to discuss some of the initial thoughts of the Commission's staff on the pandemic-induced market volatility. Mr. Srinivasan stressed that his group is still analyzing the data and had not reached any conclusions. He began by giving an overview of the Risk Surveillance Branch's three functions: margin model oversight, assessing margin model performance, and doing a qualitative assessment for margin models. He stated that in his group's review so far, his team did see some account-level breaches, but that they were fairly small in number. In looking at these account-level breaches, they did not find anything that would be adverse to the clearing member or CCP. Additionally, the staff examined whether CCPs' margin models were too reactive to the shock, and whether margin calls caused stress in the funding markets and stress among the participants. He discussed some of the data reviewed so far, but stressed that the review is still ongoing.

Ms. Karna next opened the floor for questions. Among other items, topics discussed included: the relative percentage change in open interest and the resulting increased margin requirements and whether that was due to a change in the composition of the market participants, the problems posed by looking at margins as a percentage of notional value, and potential issues with comparisons between the global financial crisis and the pandemic.

IV. Closing Remarks

In closing, Commissioner Stump, Chairman Tarbert, and the remaining Commissioners all expressed enthusiasm for the excellent discussion and stated they were looking forward to future discussions.

Ms. Goldsmith adjourned the meeting at 12:08 p.m.

Angie Karna
GMAC Chair

March 26, 2021
Date