



Commodity Futures Trading Commission

Office of Public Affairs

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Q & A – Staff Supervisory Stress Test of Clearinghouses

Why is this exercise relevant?

The reforms agreed to by the G-20 leaders in 2009 heightened the importance of clearinghouses in the global financial system, and regulators around the world are working to ensure that clearinghouses remain safe. This test is an important new part of our efforts to ensure that clearinghouses are strong and resilient.

What does this say about clearinghouse safety?

The test shows that, for the one day and the specific extreme scenarios tested, clearinghouses met or exceeded the required resilience standards with pre-funded resources. It also showed that clearing members' positions (or risks) were diversified across clearinghouses and scenarios. That's good news. But this is only one test and we need to continue to develop and conduct such tests, as the key to clearinghouse safety is continued vigilance. Stress testing, both by the clearinghouses themselves and by regulators, is an important part of that vigilance, as are other supervisory tools and risk surveillance. We also note this test does not address other types of risk that clearinghouses face, such as liquidity risk, operational risk or cyber risk.

Were there differences across clearinghouses?

All clearinghouses met or exceeded the required resilience standards for the day tested—that is, all met or exceeded “Cover 2.” We do not believe differences in the results beyond that measure are necessarily indicative of the relative safety of one clearinghouse over another because of the differences among clearinghouses. They clear different types of products and are structured differently to account for the characteristics of different products.

Are all clearing members included in this analysis?

The exercise covered 23 corporate groups, which include the 15 largest clearing members at each clearinghouse. To determine which firms would be included in the exercise, CFTC staff ranked clearing members at each clearinghouse according to the amount of initial margin required on the test date. If a clearing member was in the top 15 clearing members by amount of initial margin required at any clearinghouse, it was included in the analysis for all five clearinghouses to allow for an analysis of the impact of a default by that clearing member across all clearinghouses. The 23 corporate groups represent 88% of the total margin at the five clearinghouses. Therefore, although they are not all clearing members at all of these clearinghouses, they represent most of the activity and are the ones that create the greatest exposure.

Can you provide more detail on what it means to say clearing member risk was diversified among scenarios as well as among clearinghouses?

A majority of clearing members did not have the same risk profile, either at an individual clearinghouse or across clearinghouses. That is, under any given scenario of the 11 scenarios tested, the 23 clearing members experienced different levels of losses or gains at each clearinghouse. In addition, if a clearing member had a loss at one clearinghouse under a given scenario, it did not necessarily have losses at other clearinghouses; it may have had gains. By losses, we mean shortfalls in excess of the posted margin; gains generally mean remainders after application of margin (or in some cases actual gains).

How do these tests differ from the stress tests that clearinghouses are required to conduct under CFTC rules?

An individual clearinghouse conducts stress tests on a daily basis that cover the positions of its own clearing members. This type of test is used to estimate potential losses under extreme but plausible market events and helps to evaluate the sufficiency of financial resources available to the clearinghouses to meet its obligations. But a clearinghouse does not know what positions its clearing members are holding at other clearinghouses.

Supervisory stress tests have different objectives. Because we have access to data for all of the clearinghouses, the supervisory stress test was able to see how clearing members fared across all five clearinghouses. The test was designed to assess the impact of certain extreme but plausible stressful scenarios across clearinghouses, as well as across firms that hold clearing memberships at more than one clearinghouse.

What are the resources that clearinghouses have to address possible defaults?

The test looks at whether the pre-funded financial resources held by the clearinghouses were sufficient to cover losses under a series of extreme stress scenarios applied to actual positions and financial resources. Those resources are margin, the guaranty fund, and capital. Clearinghouses “mark to market” all positions daily. To prevent mark to market losses from accumulating for more than one day, clearinghouses collect “variation margin” for all positions daily from members, to cover losses and pass the variation margin through to those members with gains. Clearinghouses also hold initial margin from their clearing members as a performance bond to cover potential future losses in the value of open positions. The clearinghouses included in this exercise also have at least one guaranty fund, which is a mutualized pool of resources that is available to cover defaults. It is pre-funded by clearing member contributions. Each of the clearinghouses included in this exercise has committed a specified amount of its own capital for use in covering a default as well.

Clearinghouses have additional tools and resources to use in the event these pre-funded resources were ever exhausted. But it should be remembered that no clearinghouse in the United States has ever even drawn on its guaranty fund to cover a default, let alone exhaust it.

These tests also make an extreme assumption that no clearing member would post any additional margin in any scenario.

Do the results mean that clearinghouses are collecting too much margin or that guaranty funds are too large?

No, we would not draw that conclusion. This is one set of stress tests for one day. Clearinghouses will continue to conduct daily stress tests to ensure that both margin and guaranty funds remain at appropriate levels.

Why is the data anonymous?

The data is anonymous because we are legally prohibited from disclosing data that would reveal the positions or transactions of market participants, including clearinghouses and clearing members. Additionally, while we recognize the importance of transparency, this test is the first of its kind in which clearing member positions across multiple clearinghouses are aggregated and analyzed. There is continued discussion among regulators and market participants about what kind of stress tests clearinghouses and regulators should perform and what information should be public regarding clearinghouses and clearing members.

Does staff have plans to conduct future exercises of this nature?

Yes. It is important to do this regularly. In addition, there are many types of enhancements that can be incorporated into the program in the future. For example, there are risks that have not been included in the eleven scenarios covered in this exercise, such as non-parallel shifts in the interest rate curve or changes in the correlations among energy products, as well as liquidity, operational and cyber risk. International regulators also continue to discuss standards for both clearinghouse and supervisory stress tests and we expect to incorporate any standards that are agreed to. Among the other enhancements we will consider are tests that cover a longer time period, test that encompass positions and margin from multiple dates, and tests performed together with other domestic and international regulators.

What are the other elements of the CFTC's clearinghouse oversight program?

In addition to supervisory stress tests, staff performs daily risk surveillance of individual clearinghouses, clearing members, and large market participants. CFTC staff performs periodic compliance exams of clearinghouses. Staff reviews clearinghouse rules, including rules relating to margin and risk management procedures, for compliance with statutory requirements. Staff also develops and implements regulatory standards for clearinghouses and their members. Staff has also been reviewing recovery rules of systemically important clearinghouses as well as working with them as they develop their recovery and wind-down plans. Staff has been working with FDIC staff on resolution planning for those clearinghouses as well. CFTC staff also participates in or leads several domestic and international regulatory initiatives related to clearinghouse strength and stability to establish standards affecting clearinghouses and their participants, to coordinate and harmonize regulatory activities. These include co-chairing a working group on enhancing the international standards for clearinghouses by providing more granularity for these standards; examining resolution planning for clearinghouses, including international coordination; and examining the interdependencies among global clearinghouses and major clearing members.