



16 August 2016

**Cover note to the CPMI-IOSCO consultative report on the  
Resilience and recovery of central counterparties (CCPs):  
Further guidance on the PFMI**

The Committee on Payments and Market Infrastructures (CPMI) and the International Organization of Securities Commissions (IOSCO) are today publishing for public comment further guidance on the principles and key considerations in the Principles for financial market infrastructures (PFMI) regarding financial risk management and recovery planning for CCPs.

The draft guidance in this report is intended to provide a more granular description of how CPMI-IOSCO expect CCPs to implement the PFMI to further improve their resilience and recovery planning. It is also intended for use by authorities for regulation, supervision and oversight of CCPs. The guidance addresses several of the resilience and recovery priorities identified in the joint CCP workplan<sup>1</sup> of the Financial Stability Board, CPMI, IOSCO and the Basel Committee on Banking Supervision.

In developing this guidance, CPMI and IOSCO have considered input from industry workshops, a stocktake of current CCP practices, papers submitted by industry groups and the findings from the Committees' Level 3 assessment of financial risk management practices for a selected group of CCPs.

The report sets out guidance in six main areas: (i) governance and disclosure relating to the CCP's risk management framework; (ii) credit and liquidity stress testing; (iii) coverage of credit and liquidity resource requirements; (iv) margin; (v) CCPs' contribution of their own financial resources to losses; and (vi) recovery planning.

CPMI-IOSCO are soliciting comment on all of the guidance proposed in the report. In addition, the Committees request views on the specific questions noted below. Please support your comments with detailed arguments and evidence, where applicable.

## **1. Governance**

Chapter 2 of the report sets out guidance on the responsibilities of a CCP's board in overseeing the CCP's risk management framework. A CCP's governance arrangements play an important role in ensuring the CCP's overall resilience and recovery planning. Thus, the guidance on governance reinforces the guidance provided in other areas discussed in the report.

*Is the guidance provided on CCPs' governance sufficient and appropriate?*

The report includes guidance on the need for CCPs to disclose adequate information to stakeholders.

*Is the current level of public disclosure by CCPs appropriate? In particular, is there a need for further disclosure related to margin and stress testing methodologies? If so, would the disclosure of the items included in the list (or a subset of the list) suggested by an industry group and attached as an Annex be appropriate and sufficient for disclosure and feedback purposes?*

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<sup>1</sup> See <http://www.bis.org/cpmi/publ/d134b.pdf>.



## 2. Stress testing

Chapter 3 of the report provides guidance on the rigour of the credit and liquidity stress tests expected in the PFMI, as appropriate to the systemic importance of CCPs.

*Is the guidance provided on stress testing sufficient and appropriate?*

*In the light of the potential for member positions and market prices to change significantly during the day, is the proposed guidance on capturing intraday positions and price movements in stress tests appropriate and sufficient?*

## 3. Coverage

CPMI and IOSCO have analysed the adequacy of the coverage standards in the PFMI regarding a CCP's current and future exposures. In particular, the committees reviewed the standard for CCPs to cover at least the one or two largest potential aggregate credit exposure(s) in extreme but plausible market conditions (the "Cover 1/Cover 2 minimum standard").

CPMI and IOSCO found no reason to change the Cover 1/Cover 2 minimum standard and no further guidance in this respect is deemed necessary at this time. However, this standard will continue to be monitored and could be reviewed in the future in the light of market developments.

Nonetheless, the Committees wish to highlight that the Cover 1/Cover 2 standard is a minimum. A CCP should determine the total required amount of financial resources it needs to maintain in order to cover its exposures adequately. In doing so, a CCP's governance arrangements play an important role due to the board's responsibilities for setting the CCP's risk tolerance. Accordingly, a CCP's required amount of financial resources may need to exceed the Cover 1/Cover 2 minimum standard in the PFMI if it is to manage adequately its risk exposures.

In reviewing coverage requirements, CPMI and IOSCO have decided, at this time, to emphasise the need to (i) maintain the required amount on an ongoing basis; (ii) consider the exposure of clearing participants as well as their affiliates; and (iii) enhance the rigour of stress testing to determine the level of prefunded resources as mentioned above.

*Is the guidance provided on coverage sufficient and appropriate?*

*Is the current two-tiered Cover 1/Cover 2 minimum standard still appropriate in relation to the guidance in the report?*

## 4. Margin

Chapter 5 of the report outlines guidance on margin systems. This guidance is intended to assist a CCP in its ongoing efforts to implement and maintain margin systems that are effective in addressing the risks and particular attributes of each product, portfolio, and market served.

*Is the guidance provided on margin sufficient and appropriate?*

*Is the guidance provided on procyclicality appropriate and sufficient?*

*The PFMI do not explicitly address margin add-ons. Is the guidance provided on margin add-ons adequate to ensure sufficient coverage by the margin system and other prefunded financial resources in line with the PFMI?*

*The PFMI do not prescribe a minimum margin period of risk or closeout period. Is further guidance in this area needed?*

## 5. CCP contribution to losses

Chapter 6 of the report contains guidance on a CCP's contribution of its own resources to losses resulting from a participant default and from custody and investment of participant assets. This chapter is intended to provide further guidance for a CCP when determining an appropriate contribution of its own resources towards these types of loss, in order to enhance the confidence of stakeholders that the FMI's design, rules, overall strategy and major decisions appropriately reflect the legitimate interests of its direct and indirect participants and other relevant stakeholders as outlined in Key Consideration 7 of Principle 2.

*Is the guidance provided on a CCP's contributions to financial resources to cover losses sufficient and appropriate?*

## 6. Recovery planning

Chapter 7 of the report reiterates certain aspects of the recovery guidance previously published by the CPMI and IOSCO in the report on *Recovery of financial market infrastructures* (Recovery Report).<sup>2</sup> This guidance is intended to facilitate a CCP's development of its recovery plan in a number of areas.

*Is the guidance already provided on recovery planning in the Recovery Report sufficient and appropriate?*

### Other considerations

In preparing this report, other topics came to light. CPMI-IOSCO would like to solicit input on the following items in this consultation.

The PFMI recognise risk committees as part of the overall functioning of the board (Principle 2 on governance). However, CPMI-IOSCO are not proposing specific guidance on the role of risk committees.

*Is there a need for further guidance on the role of risk committees as an effective means of achieving proper corporate oversight and for receiving input from persons representing stakeholder interests?*

The PFMI discuss the interplay between risk management arrangements and a FMI's ownership structure and organisational form (Principle 2 on governance). The consultative report does not address the implications of the organisational (legal) structure of the CCP for the effectiveness of its governance arrangements.

*Is there a need for guidance regarding governance and the organisational (legal) structure of the CCP?*

The report contains no guidance on the allocation of default fund requirements among clearing participants, and in particular, whether CCPs should consider rules to allocate clearing participants' contributions to the default fund proportionally to the risks brought to the CCP.

*Is there a need for further guidance on the allocation of default fund requirements among clearing participants?*

The report contains no specific guidance on how CCPs should structure their participants' prefunded financial resources into margin and default fund contributions.

*Is there a need for further guidance on the composition of prefunded financial resources?*

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<sup>2</sup> This report can be found on the websites of the [BIS](#) and [IOSCO](#).



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Comments on the report (supported with detailed arguments and evidence, if available) should be sent by 18 October 2016 to [cpmi@bis.org](mailto:cpmi@bis.org) and [consultation-2016-01@iosco.org](mailto:consultation-2016-01@iosco.org). As noted above, comments are welcome on any aspect of the report and need not be restricted to the indicative questions that are highlighted in this cover note.

All comments may be published on the websites of the Bank for International Settlements and IOSCO unless a respondent specifically requests confidential treatment.

After the consultation period, CPMI and IOSCO will publish a final version of the report in 2017, taking into account the comments received. The Committees expect that CCPs will promptly identify any areas where changes are necessary to support full observance of the PFMI and will develop a course of action to address them as expeditiously as practicable, taking into consideration the relevant timelines for any necessary regulatory approvals. The implementation of such changes should be completed no later than the end of 2017.

CPMI and IOSCO will closely follow developments of other international workstreams that may affect the resilience of CCPs and the guidance provided in this report.



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## Annex: Items that an industry group suggested be disclosed for feedback purposes

- A. CCPs should *publicly disclose* the following items:
1. **Scenarios:** All historical scenarios and the assumptions, risk factors, and shock levels for hypothetical/theoretical scenarios.
  2. **Inputs:** For both historical and hypothetical/theoretical scenarios, all relevant pricing data, correlations and liquidity conditions.
  3. **Guarantee fund:** The size of the guarantee fund for that particular clearing service (assuming limited recourse).
- B. CCPs should provide *additional information to clearing members and other market participants* who make a request for the following items:
1. **Stress results:** Information on stress losses in the form of quarterly reports, including trend data on daily CCP uncollateralised stress losses (the single largest and the aggregate of the two largest uncollateralised stress losses) and the following information, arranged in each case from highest to lowest:
    - i. the largest uncollateralised stress loss for each clearing member (across scenarios), without identifying the scenario or the clearing member, to determine an approximate distribution of maximum clearing member stress losses;
    - ii. the largest uncollateralised stress loss for each pair of clearing members (across the stress scenarios), without identifying the scenario or either clearing member, to determine an approximate distribution of maximum stress losses for two members defaulting simultaneously; and
    - iii. the distribution of uncollateralised stress losses across all clearing members for each scenario, without identifying the scenario or clearing member.
  2. **Assessments:** Clearing members, other market participants, and other CCPs should have the same ex ante understanding of all the powers and authorities that a CCP may exercise in a time of crisis.
  3. **Reverse stress-testing results:** For each stress-testing scenario that the CCP applies to each particular clearing service, the number of clearing member defaults that would result in exhaustion of all pre-funded and pre-committed resources for that clearing service.
  4. **Validation:** CCPs should disclose: (i) the name of the independent party; (ii) a summary of the qualifications of that party; (iii) the validation approach taken by that party; and (iv) the results of such validation.