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Secretariat of the Committee on Payments and Market Infrastructure
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Basel, Switzerland

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Submitted via email to: cpmi@bis.org and consultation-2016-091@iosco.org

RE: Response to Consultative Report of the Committee on Payments and Market Infrastructure and International Organization of Securities Commissions re: Resilience and recovery of central counterparties (CCPs): Further guidance on the PFMI dated August 2016 (“CPMI-IOSCO Consultative Report”)

BlackRock welcomes the opportunity to comment on the Consultative Report of the Committee on Payments and Market Infrastructure (CPMI) and International Organization of Securities Commissions (IOSCO) regarding the resilience and recovery of central counterparties (CCPs). BlackRock commends CPMI-IOSCO for the publication of the Principles for Financial Market Infrastructures (PFMI) in 2012 and reviews subsequent to their publication. The PFMIs have become the benchmark standard by which CCPs are measured and are therefore essential to strengthening and preserving financial stability whilst protecting the end-investor through clearing.

We believe central clearing brings many benefits, including increasing transparency for regulators and market participants and eliminates many of the counterparty risks inherent in bilateral OTC transactions. However, along with generating these benefits, central clearing results in certain risks being concentrated in a handful of Central Clearing Counterparties (CCPs). Throughout this response we put the focus on the perspective of the end-investor - the ultimate user of CCPs - committing capital through investment and is required to pay fees to access the benefits of central clearing.

There are a number of ways in which end-users could be protected through clearing, principally through ensuring their protection against losses in the event of CCP recovery or resolution. We welcome a global focus on CCP resilience and strengthening the first line of defence through the ongoing work of CPMI-IOSCO. We have recommended that CCPs strengthen their resources and the resources of the default waterfall; that they are subject to rigorous standardised stress testing and that stress test results are partially disclosed to the market at a similar level of granularity to what is currently provided for banks. These resilience issues are ultimately connected to undertaking to create a global framework for recovery and resolution of CCPs.

1. Executive summary

Resilience

Resilience requires that CCPs strengthen their lines of defence. The CPMI-IOSCO consultation includes aspects that will enhance resilience, specifically with respect to stress testing and assigning specific responsibility for key risk management decisions within a CCP's risk governance structure. We believe additional steps still need to be taken to adequately strengthen a CCP's resilience; specifically regulators should develop specific

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CCP capital requirements, specify how much of that capital needs to be dedicated to default loss absorbing resources, and require improved information disclosure to reinforce investor confidence.

Financial resources and CCP capital

The very purpose of a CCP is to mitigate credit risk in a default, and its success in doing so depends upon the layers of protection it has in place, including initial margin and other loss absorbing resources. How these resources are sized and the incentives created by the various layers are important considerations for market participants. Specifically, risks and rewards need to be aligned such that CCPs will act rationally to both prevent and/or minimize losses in the event of a market disruption.

Most CCPs make or commit to make modest contributions to the loss absorbing resources, often referred to as “skin in the game” (SITG). However, many market participants have questioned whether the current level of these contributions is sufficient to properly align incentives, and some have put forward suggestions on how to think about optimal sizing (e.g., as a simple percent of the overall default fund or calculated to cover an expected shortfall, among others).

Despite these efforts, there has been no meaningful change to the level of CCPs’ contribution to loss absorbing resources, nor has there been any further development in the regulatory framework. In addition, beyond that required under EMIR¹, there is no regulatory determination on what the SITG commitment should be, leaving CCPs to make this determination themselves, when the incentive for a profit-seeking enterprise is to limit its commitment. We encourage global regulatory bodies such as FSB, CPMI-IOSCO to undertake rigorous quantitative impact studies around modeling the optimal level of CCP capital and its specific allocation to SITG, and to communicate its position to the market. We would then expect the relevant CCP regulators to act upon this information.

A robust CCP capital framework and requirement for SITG would further strengthen CCP resilience and by doing so render the possibility of CCP failure even more remote. Market participants could tolerate a small but predictable increase in the cost of clearing that may accompany heightened capital requirements in order to mitigate the possibility of an uncertain liability they would otherwise face if a CCP were to fail.

Disclosure

We appreciate the strides made with respect to the CPMI-IOSCO PFMI disclosures and the more recent Quantitative Disclosures (QDs). The QDs are the first instance where market participants have mostly standardised quantitative disclosures across global CCPs and while market participants welcome these QDs, more work needs to be done to better standardize the disclosures, provide assurances of accuracy through annual audits, and enhance management discussions of CCP risk profiles.

Recovery

A CCP that fails in its resilience mandate may need to enter recovery. Recovery of a CCP may be needed if the financial resources available to the CCP are insufficient to cover losses from a CM default. Recovery is a process set out in, and governed by, CCP rule books. To cover losses from a clearing member default, a CCP will generally follow a “waterfall” in a predefined order. The recovery stage is generally considered to be in effect

¹ Under EMIR, CCP skin in the game is mandated at 25% times the minimum capital (including retained earnings and reserves) held in accordance with Article 16 of Regulation (EU) No 648/2012 and Commission Delegated Regulation (EU) No 152/2013

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either once all of the defaulter's resources have been exhausted or once the non-defaulting members' prefunded contributions have been exhausted. We encourage global regulators to mandate CCPs to set out the clear and predictable critical path towards recovering a failing CCP with the resources it has at its and its Clearing Members' disposal

Regardless of the trigger, once these specified resources are exhausted, the CCP must allocate default losses in other ways. Loss allocation tools that are already in some CCP Recovery plans set out in their rulebooks, or under discussion to be added are Variation Margin Gains Haircutting (VMGH) and Initial Margin Haircutting (IMH), both of which are particularly problematic due to both their destabilizing impacts on the market and their inherent inappropriate application to end-users.

Destabilising impact of margin haircutting

VMGH takes cash paid by market participants and diverts it to cover outstanding losses caused by a CM default. The expected recipients of the cash payments are "haircut" and only receive a fraction of what is owed to them. Similarly, IMH takes margin paid in by market participants and takes a portion of it to cover losses caused by a CM default. CCP customers who fear they will be subject to such profit/ property appropriation will seek to rapidly close out positions, which is potentially highly destabilizing. Some may voluntarily default by not meeting VM calls, preferring to lose their positions than continue to pay margin that is subject to haircutting.

Inappropriateness of margin haircutting

VMGH and IMH are tools that enable CCPs, which are largely for-profit businesses, to allocate losses to its customers, including end-users. When applied in Recovery, this loss allocation tool allows the CCP to force end-users to pay for it to stay in business. There is no precedent for users of a service, who pay fees to access a service, to also be responsible for keeping that service in business after it has failed in its core mission, which for a CCP is the provision of credit risk mitigation. While CCPs are a critical part of the market infrastructure, they are also businesses who provide the service of credit risk mitigation in exchange for fees.

CCP-led recovery vs. resolution authority led-recovery

While a CCP-led recovery is preferred by most market participants, this preference shouldn't preclude the early intervention of resolution authorities in the recovery process. A clear distinction between recovery and resolution tools would be helpful. Importantly in the first instance the supervisory authority approves the rulebook, and should examine closely the incentives created by recovery processes in these rulebooks and the ways in which the end-investor would be protected from losses in such a process. Just as importantly, the resolution authority should be the sole entity responsible for overseeing any losses to market participants in Recovery. A CCP led recovery should be limited to private sources of voluntary capital. If private sources of capital are depleted, and no further providers of capital are willing to invest in its continued operation, we firmly believe this is the point where the resolution authority must take control. The RA may determine to recover the CCP or to wind it down, which is a topic that will be further addressed in our response to the FSB's consultation on Resolution.

A resolution authority led-recovery could be orchestrated if the Authority determines the continuation of the CCP's services meets a public interest standard. While this outcome is theoretically possible, we believe the lack of further private capital sources is likely to coincide with a lack of market confidence in the CCP, and that most participants will seek to close out positions. In the unlikely event that there is a viable business to recover, the RA should have additional tools to allocate losses, which could include additional (though limited) cash calls on members or a limited amount of VMGH. We don't support the use of

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IMH in any loss allocation scenario. Any application of VMGH in this process must be subject to a public interest standard and subject to strict limitations in terms of number of days it is applied, and an overall cap on the amount of haircut that can be taken. Participants subject to VMGH should receive a senior claim against the CCP and its successors for the full amount of the VM taken from them in the same way CCP would hold a claim over defaulting participants.

2. Governance

Chapter 2 of the proposed guidance provides some welcome specificity with respect to board accountability for risk management and the importance of establishing communication channels with indirect market participants, who are the end-investors. We are supportive of 2.2.18, which recognizes the importance of end-investor views being represented in the CCPs' risk committees. The chapter makes several references to disclosure mechanisms and transparency, which we believe are key to maintaining a resilient CCP. We therefore believe there should be specific guidance introduced on the broader topic of disclosure and transparency.

We appreciate the strides made with respect to the CPMI-IOSCO PFMI disclosures and the more recent Quantitative Disclosures (QDs) as well as the results of the ESMA CCP Stress Tests, which were published in April early 2016. The QDs are the first instance where market participants have mostly standardised quantitative disclosures across global CCPs and while market participants welcome these QDs, more work needs to be done. We also appreciate the specificity of the recently issued CFTC Guidance, which provides additional rigor to the CCP stress testing process.

Proposed CPMI-IOSCO guidance for governance

We welcome the proposed guidance, but further discussion and consideration should be given to the following specific points regarding information disclosure:

- The disclosures should be formally standardised. While we appreciate that most CCPs are following an agreed upon format not all CCPs are following it. Regulators should step in if necessary to require all CCPs to use the agreed format.
- The disclosures should be reviewed by auditors (at least annually), consistent with what is expected from bilateral counterparties. This would address several issues with the current disclosures, ranging from divergent interpretations of required disclosure, data entry errors, and formatting inconsistencies.
- There should also be additional disclosure and discussion required, similar to what is provided in a "Management Discussion & Analysis" in a typical bilateral securities offering disclosure context. For market participants to adequately do their diligence on a CCP, there needs to be discussion that explains the CCP's risk profile and any changes that have occurred thereto. The PFMIs are a step forward in this direction, but they are impeded by frequency of disclosure (only every 2 years) as well as the actual content of the disclosure.
- Risks to end-users need to be more explicitly outlined in relevant documentation. A number of market participants, particularly end-users, presume that central clearing eliminates credit risk, and some may also mistakenly base this presumption on a belief that a CCP has an explicit or implicit government guaranty. CCPs the Clearing Members) should be required to explicitly disclose how a customer may still face credit risk, not only in the event of a Clearing Member default, but also in the event of a CCP default.

3. Stress testing

BlackRock supports annual mandatory standardised stress tests conducted by resolution authority with input from the college. A standard stress test framework, albeit one that can accommodate the specificities of individual CCPs, should be mandated by regulators for all CCPs. CCPs would need to comply with this baseline set of macro-assumptions, which would be part of a broader required framework that includes idiosyncratic stresses on basis and higher order risk exposures embedded within individual CCP portfolios.

Stress test results should be made available in whole or in part. Stress tests should be partially disclosed to the market - similar to what is provided for large banks - and disseminated in full to CCP risk committees. A consistent, disclosed scenario-based framework, along with the disclosure of results, will create CCPs that are more resilient and transparent, fostering confidence in CMs and their end-investor clients, settlement banks, liquidity providers and other participants in the central clearing ecosystem.

Proposed CPMI-IOSCO guidance for stress testing

We welcome the proposed guidance. We support the guidance that stress tests should mirror day to day operational practices and that excess funds posted to a CCP should not be considered when looking at available resources. We also welcome the additional guidance that CCPs should include other key participants, such as liquidity providers, settlement banks and investment counterparties, in their credit and liquidity stress testing. We would like the guidance to be further expanded to include disclosure standards; we recommend that the disclosures should be formally standardised. While we appreciate that most CCPs are following an agreed upon format (which is in reality an unformatted spreadsheet) not all CCPs are following it.

The disclosures should also be reviewed by auditors (at least annually), consistent with what is expected from bilateral counterparties. This would address several issues we have experienced with the disclosures, ranging from divergent interpretations of data, data entry errors, and formatting inconsistencies.

The usability of such reports is an important consideration from the risk management perspective. Disclosures should be easily found on a CCP's website and risks to end users/ customers need to be more explicitly outlined in relevant documentation.

There are a number of important issues in the draft guidance where the guidance applying to clearing securities finance transactions (SFT) and OTC derivatives clearing needs to be made distinct.

- Regarding the identification of all liquidity risks, depending on the structure, the asset manager may be considered an indirect participant. For the model to work effectively and deliver the benefits of central clearing to the SFT markets, we recommend CPMI-IOSCO clarifying that such participants would not be required to take on principal risk.
- Regarding the aggregation of results across product categories, the term "collateral" is used loosely here. There should be differentiation between principal collateral typical of any securities loan and margin collateral required for the cleared position.

4. Coverage

The very purpose of a CCP is to mitigate credit risk in a default, and its success in doing so depends upon the layers of protection it has in place, including initial margin and other loss absorbing resources. How these resources are sized and the incentives created by the various layers are important considerations for market participants. Specifically, risks and

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rewards need to be aligned such that all participants will act rationally to both prevent losses and to minimize losses in the event of a market disruption.

Protecting the end-investor through clearing will be paramount to the success of the regulatory framework around CCP resilience. CPMI-IOSCO should provide explicit guidance that CCPs are not permitted to include the margin of non-defaulting customers as a financial resource available to cover the CCP's credit and liquidity risks sized through CCP stress tests. Rather, dynamic margin calculations, risk-based CCP contributions, capped clearing member assessments and standby credit should comprise the available pre-resolution resources to satisfy PFMI Principles 4 and 7 requirements to cover CCP credit and liquidity risks. We recommend that whenever SFT clearing is offered by CCPs they should account for the need to pay repo interest, securities lending fees and rebates when calculating their resource requirements for payment obligations.

Proposed CPMI-IOSCO guidance for coverage

BlackRock supports CPMI-IOSCO's further recommended guidance relating to the stress testing measurements required by PFMI Principles 4 and 7. Pursuant to PFMI Principles 4 and 7, CCPs must cover the credit and liquidity risks measured by stress tests with margin and other prefunded financial resources. We agree with CPMI-IOSCO's recommendations that a CCP should use both historical and forward-looking data to "conduct distinct but consistent stress tests for credit risk and liquidity risk," including stress tests that capture credit and liquidity risks to which the CCP could be exposed in extreme but plausible market conditions, and that the results of these tests should be used to size its respective credit and liquidity exposures. We agree that the stress tests should include bespoke scenarios specific to the CCP. In taking into account client exposures, we agree that "a CCP should make the conservative assumption that no payments will be made on behalf of a defaulting participant's clients unless there are arrangements for direct payments from such clients to the CCP" and that "a CCP should assume that it will be unable to port client positions." While we believe that the viability of porting should be strengthened to achieve this result, porting is unfortunately not a certainty during times of market stress.

Further specific guidance is also required for the available financial resources to cover the risks measured by the CCP stress tests. Specifically CPMI-IOSCO should mandate that all CCPs must have prefunded and committed resources to cover the possibility that its largest two clearing members will fail and either provide additional cover or demonstrate that "cover 2" is sufficient. Cover below cover 2 is insufficient to protect clearing members' customers from a CCP failure and, under certain circumstances, Cover 2 is insufficient. For example, a CCP that has many smaller clearing members will have more broadly distributed risks for which its two largest clearing members would be disproportionately small given the total exposure.

With regard to SFT clearing, where the service may be offered to end-investors as "direct participants" the guidance should acknowledge that such models do not envision these same end-investors contributing to the mutualised financial resources or to be subject to a same day assessment (4.2.6) as this could contravene standard contractual obligations and prevent the SFT model from working.

What is the optimal level of resources a CCP should commit to the default waterfall? What level of commitment best aligns the CCP's interests with the goal of a resilient CCP? What form should a CCP's commitment take? Should it be entirely prefunded in cash and who should hold that cash? These are all questions that we believe still need to be addressed and regulatory guidance would be welcome.

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Ex-ante end-investor protections afforded by default waterfall should be revised. As for-profit institutions, CCPs can issue equity, debt or a combination thereof to fund its cash and/or cash-equivalent contribution to the guarantee fund. BlackRock also recommends exploring pre-funded CCP resources and/or CCP default insurance schemes. Market participants could tolerate a small but predictable increase in the cost of clearing (i.e. contributions to a pre-fund deposit guarantee-like and/or default insurance schemes) to mitigate the possibility of an uncertain and potentially unlimited liability they would otherwise face if a CCP were to fail.

5. Margin

The calculation, collection and adjustments to initial margin are core elements to the day-to-day risk management of a CCP. The strength of the analytical models supporting the calculations and the ability for market participants to replicate and anticipate changes to IM are important to market resilience.

Proposed CPMI-IOSCO guidance for margin

We welcome the additional guidance on margin suggested in the consultative document. BlackRock agrees that the Margin Period of Risk (MPOR) should be based on the risks specific to the contract and should not be subject to a prescribed minimum, as the market is likely to take that minimum as a de facto standard. CCPs should be required to demonstrate to their supervisory authorities and market participants that the MPOR is appropriate, which could be included as part of its back-testing procedures.

With respect to pro-cyclicality, while we understand the concerns of margin increases during times of stress, we believe that the knowledge that additional assets are supporting open positions should improve confidence in the CCP and carry lower pro-cyclicality concerns than variation margin gains haircutting, which will force directional market participants to close-out at the earliest signs of CCP distress. We believe that such measures will alleviate pressure on clearing members whose viability will be essential to the continuing operation of a CCP facing distress.

Lastly, we again underscore the importance of transparency and disclosure, both to support market confidence in the CCP but also to allow market participants to appropriately plan for potential margin changes. Such disclosure should allow participants to replicate margin calculations (including add-ons) and run scenario analyses to understand the sensitivity of margin requirements to various market factors.

6. CCP contribution to losses

Discussion of CCP resilience is generally accompanied by a discussion of loss allocation. To enhance resilience, a CCP must develop mechanisms to allocate losses that cannot be covered by the defaulter's margin and default fund.

Most CCPs (though not all) will absorb a portion of the losses through their own SITG before turning to other resources. The next layer of loss absorption is most often the prefunded contribution from the CCP's clearing members, the default fund. With this general structure, the owners and operators of the clearing business are rightly responsible for the financial liabilities that can arise from running the business.

Unfortunately, many CCPs, clearing members and regulators have accepted that once committed resources of the CCP and its clearing members have been exhausted, the financial liabilities that arose from running the clearing business may be allocated to their customers through Variation Margin Gains Haircutting. In other words, CCPs, clearing members and regulators have accepted that a customer's money can be appropriated to

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support the continued operation of a failing business. We strongly disagree with this stance and urge regulators to take a more critical view of this practice, particularly in conjunction with establishing guidelines for CCP SITG.

Proposed CPMI-IOSCO guidance for CCP contribution to losses

Most CCPs make or commit to make modest contributions to the loss absorbing resources, often referred to as “skin in the game” (SITG). However, many market participants have questioned whether the current level of these contributions is sufficient to properly align incentives, and some have put forward suggestions on how to think about optimal sizing (e.g., as a simple percent of the overall default fund or calculated to cover an expected shortfall, among others).

Despite these efforts, there has been no meaningful change to the level of CCPs’ contribution to loss absorbing resources, nor has there been any further development in the regulatory framework. In addition, beyond that required under EMIR², there is no regulatory determination on what the SITG commitment should be, leaving CCPs to make this determination themselves, when the incentive for a profit-seeking enterprise is to limit its commitment. We encourage global regulatory bodies such as FSB, CPMI-IOSCO to undertake rigorous quantitative impact studies around modeling the optimal level of CCP capital and its specific allocation to SITG, and to communicate its position to the market. We would then expect the relevant CCP regulators to act upon this information.

A robust CCP capital framework and requirement for SITG would further strengthen CCP resilience and by doing so render the possibility of CCP failure even more remote. Market participants could tolerate a small but predictable increase in the cost of clearing that may accompany heightened capital requirements in order to mitigate the possibility of an uncertain liability they would otherwise face if a CCP were to fail.

With specific reference to the Consultative Document, we offer the following points:

- Chapter 6 of the guidance adds limited additional specificity to the topic of CCP SITG. We recommend that 6.2.2 be expanded to include a more targeted CCP SITG requirement as outlined above
- We agree with 6.2.3, that as long as the CCP has discretion over the custody and investment decisions with respect to customer and clearing member assets, then the risks therein should be fully borne by the CCP
- We further agree with 6.2.4, which indicates the CCP should put its own resources ahead of participants’ capital, but would recommend the guidance be expanded to require a more prescriptive amount of resources

7. Recovery

Recovery of a CCP may be needed if the resources in the CCP’s waterfall are insufficient to cover losses from a member default. To cover losses from a clearing member default, a CCP will generally follow a “waterfall” in a predefined order. The trigger for moving into recovery is not universally agreed upon: would it be triggered when prefunded resources are exhausted or when all resources, including member assessments are exhausted? Regardless, once resources are exhausted, the CCP must allocate losses in other ways.

A clear distinction between owners’ funds and users’ funds is important to reflect in global principles. Owners are the CCP itself and Clearing Members. Owners will generally profit

² Under EMIR, CCP skin in the game is mandated at 25% times the minimum capital (including retained earnings and reserves) held in accordance with Article 16 of Regulation (EU) No 648/2012 and Commission Delegated Regulation (EU) No 152/2013

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from central clearing. Users are the firms required to use a CCP by legislation. Users will generally pay for using a CCP.

Proposed CPMI-IOSCO guidance for CCP Recovery

We welcome additional discussion on recovery tools for CCPs and urge law makers to reject the use of end-investor funds in the recovery of a failed CCP. We believe the guidance should specifically limit the use of end-investor funds to either a resolution phase or a resolution authority-led recovery phase. We also believe that additional guidance regarding broadening auction participation would help CCPs in re-establishing a matched book post a clearing member default.

Variation margin gains haircutting

Investor confidence and more broadly systemic stability is built on a foundation of certainty and predictability. If end-users were to have an uncertain liability towards a failing CCP through VMGH being an option in recovery this will undermine investor confidence in clearing, lead to suboptimal investment and could ultimately become an additional source of volatility. CPMI-IOSCO should prohibit the use of VMGH at any point prior to resolution.

VMGH as a term is misleading. What is referred to as “margin gains” is actually profit of a given end-investor such as a pension fund. The CCP would otherwise use these customer profits to cover losses because it failed to manage risks appropriately. VMGH is ultimately a form of loss mutualisation - it also dis-proportionally impacts investors who trade directionally, as compared to dealers who generally seek to be flat at end of day. End-users who fear they will be subject to profit appropriation will rationally seek to rapidly close out positions, which is potentially destabilising on a system-wide basis.

VMGH also adds a level of risk to customers that does not exist in a bilateral relationship. Customers who face a bankrupted bilateral counterparty would close out trades (generally at their side of the market) and submit a claim to a bankruptcy judge. That claim is admittedly likely to be reduced by some amount and the customer would suffer a loss. The key differences in the cleared and bilateral worlds are (1) the customer's loss is not enabling a failed business to operate; and (2) the customer (or its agent) chose to have a relationship with the defaulting counterparty, but the customer has limited choice in CCPs, and no choice in the clearing members of that CCP, other than its own clearing broker.

Allowing a CCP to use a VM haircut to recover after all other waterfall resources are depleted will likely discourage market participants from using risk mitigating financial instruments that are subject to mandatory clearing requirements. It could potentially cause cascading defaults as participants expecting such payments to cover hedging or other costs may not be able to fund the unexpected shortfall. Most fundamentally, it is simply unfair to impose what amounts to a tax on some or all market participants – particularly where those participants have been required by law to use a CCP's services.

For these reasons and given the objective the official sector and end-users have in common – namely systemic stability derived from a fair, consistent and predictable regulatory framework – VMGH should only ever be considered as a measure of the last resort in resolution and after CCP resilience is addressed. In the event VM is ever taken from non-defaulting participants by a CCP, we strongly believe that their losses should be capped, limited to one round of haircutting and overseen by resolution authorities. Furthermore, such participants should receive a senior claim against the CCP and its successors for the full amount of the VM taken from them.

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We also feel strongly that CCPs should never be permitted to use customer margin to address liquidity needs of the CCP – we recommend that CPMI-IOSCO prohibits this in the forthcoming global guidance. While this use of customer margin is not raised in the CPMI-IOSCO August 2016 Consultative Report nor the FSB August 2016 CCP Planning Report, the CPMI-IOSCO August 2016 Level 3 Report identifies areas of concern relating to liquidity and suggestions have been made regarding the use of margin to address the liquidity issue. The purpose of posting margin is not to serve as a liquidity backstop for CCPs. Using margin for such a purpose would undermine customer protections and raise issues regarding security and bankruptcy rights. For these reasons, such practices should be uniformly prohibited across all CCPs.

Re-establishing a matched book: partial tear ups and auctions

Partial tear-ups should be on a voluntary basis and subject to the approval of all parties (CCP, CM and end-users). If the recovery process proves unsuccessful, Resolution Authorities should move rapidly to full tear up under resolution. We encourage CPMI-IOSCO to provide guidance to deliver a robust recovery toolbox.

Expanding the participants eligible to bid in the auction process is highly likely to improve auction results. The criteria for broader market participation in the auction process should be established and published as part of the CCP's resolution and recovery plans, which would allow both the CCPs to identify potential participants and allow those participants to take preparatory actions in a measured fashion rather than during the midst of a crisis.

CPMI and IOSCO should require open auctions during recovery as the best process to return to a matched book. While clearing members' participation in auctions impact loss allocation, no similar construct is needed to bring other participants into the process. Asset managers, for example, are already incentivized the right way and can only improve the auction process. Proposals for asset managers or their clients to contribute capital fail to recognize the practical challenges to such a requirement without any corresponding benefit to the auction process. Given that asset managers act on behalf of and for the benefit of their clients, the asset managers' own funds should not be put at risk and practical challenges would arise by having clients put up their own funds individually. For example, would each client send in individual wire transfers? On what basis would the funds not be returned? Asset managers should be encouraged to participate in such a process on behalf of their clients and creating artificial barriers only hurts the process. Expanding the auction to a broader range of market participants increases liquidity and increases the likelihood that the CCP will return to a matched book quickly.

Additionally, end users could be allowed post-default the possibility to substitute ('buy back') their initial margin in the form of securities with cash. This would be beneficial for the CCP because they would have cash available whereas the end-users, which may be unable to transfer their positions to a back-up clearing member and face liquidation of their positions, could preserve their securities and decrease replacement risk.