
EACH response to the CPMI-IOSCO discussion paper on client clearing access and portability

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Introduction

The European Association of CCP Clearing Houses (EACH) represents the interests of Central Counterparties (CCPs) in Europe since 1992. CCPs are financial market infrastructures that significantly contribute to safer, more efficient and transparent global financial markets. EACH currently has 19 members from 15 different European countries. EACH is registered in the European Union Transparency Register with number 36897011311-96.

EACH appreciates the opportunity to provide feedback to the CPMI-IOSCO discussion paper on client clearing access and portability (hereinafter called “the discussion paper”).

Access (Section 2 of the discussion paper)

Design of direct and sponsored access models

Q1. Do you agree with the observation in the discussion paper that the direct and sponsored access models are designed for and generally used more by larger and/or more sophisticated clients?

Direct and sponsored access models may indeed be more generally used by larger and/or more sophisticated clients. Nevertheless, they are also available to small and medium sized clients. Generally, those access models were designed to address specific risk management and resource management constraints faced by clearing members and clients in relation to client clearing services. So greater use by larger/more sophisticated clients is a natural consequence of those constraints. Furthermore, as is always the case when new services are proposed, there is an additional complexity of being a “first mover”. The rate of adoption will depend on individual asset classes and/or the evolution of the models and regulatory requirements. As the model matures, CCPs are expecting the model to see a broader range of clients subscribing to it, providing them with benefits of reduced counterparty risk, improved asset protection and enhanced cash and collateral management services.

Notwithstanding the above, while the use of access models should be enabled to the extent possible depending on the risk profile of market participants, it should again be noted that the demand for access models is a consequence of the risk and resource management of market participants, e.g., regarding some less sophisticated or smaller clients’ capacities/resources to invest may be lower or there may be no use case for them.

EACH Members would also like to highlight that sponsored access is in Europe still at an early stage if compared to the US, where the presence of more sponsor agents and balance sheet benefits ensures more voluntary clearing. For some CCPs, the margin procedures can be executed either by the agent or the sponsored bank, but some others have detected operational concerns with onboarding clients, for instance constraints related to the payment of intraday margin requirements. New onboarded Members would need to consider such

margin calls, leading to an extensive work for both sponsored Members, that would need to put in place some kind of operational control, and the CCP. These new models create new types of risks for the CCP that should be integrated accordingly in the existing CCP's risk management framework, without of course lowering them. As per answer to Q5 below, when developing access models CCPs have therefore installed safeguards to address such new types of risks or risk transmission.

Q2. Could there be any other solutions that would facilitate access, either through greater use of such access models by small and medium-sized clients, or through some other solution?

While as mentioned in our response to Q1 direct and sponsored access models may indeed be more generally used by larger and/or more sophisticated clients, as models mature, we expect to see a broader range of clients subscribing. As per Q1, while the use of access models should be enabled to the extent possible depending on the risk profile of market participants, it should also be noted that the demand for access models is a consequence of the risk and resource management of market participants, e.g., with regard to some less sophisticated or smaller clients' capacities/resources to invest may be lower or there may be no use case for them. Rather, broader access to clearing should always ensure economic viability and operational resilience of the central clearing environment.

Nevertheless, innovation should be further promoted by addressing credit, market, operational, legal and liquidity risk management constraints. For example, if third parties were allowed to cover the day-to-day funding of margin requirements, this would reduce liquidity, legal and operational burdens for client to meet margin requirements. In our answer to Q11, we elaborate on additional aspects which should be taken into account for facilitating access.

Barriers

Q3. Do you agree with the findings in the discussion paper that direct and sponsored access models are used more for certain types of products (eg repos) than for others? Do you agree with the reasons described in the paper for why this is the case? Why/why not?

EACH agrees with the findings that direct and sponsored access models are used more for certain types of products (e.g., repos) than for others. While repo has been the most successful use case due to the benefits of access models in relation to reducing capital requirement constraints, the models are suitable as well to any cleared products. There exist already direct access models that are used for OTC IRS and we expect that the use of access models for OTC derivatives and ETDs may increase, especially against the backdrop of the implementation of regulatory requirements (UMR, Basel III) combined with funding and liquidity constraints.

Challenges related to direct and sponsored access models

Q4. Do you agree that direct and sponsored access models have the potential to diversify the risk profile of the direct clearing participant basis of a CCP by introducing new types of direct participants? Why/why not?

Yes, direct access models can diversify the risk profile of the CCP, and the current models are an important first step in achieving these goals.

Q5. Do you think that CCPs have introduced sufficient safeguards to prevent risk transmission from direct participants using direct and sponsored access models? Why/why not? If not, what additional safeguards do you think are necessary?

It is the CCPs' role to establish a robust system of risk management. In doing so, CCPs aim at ensuring amongst other that risk is not transmitted through the system. This applies to all the activities of the CCP, including direct and sponsored access models. When developing access models, European CCPs have therefore installed specific safeguards in coordination with market participants. As the risks in relation to direct access by clients are identical to those arising from a standard clearing membership, CCPs ensured the same high risk management standards for direct/sponsored access and aligned the onboarding process including resources and credit assessment. For instance, the agent takes over the obligation for their clients to provide the default fund contributions and to participate in the default management process (DMP) and the sponsor guarantees their clients' performance to the CCP. Furthermore, CCPs installed safeguards in the default waterfall to cater for a default of a client.

Q6. Do you think that sponsors are properly incentivised to closely monitor the activity of their sponsored participants (i.e. the direct participants)? Why/why not? If not, how do you think sponsors could be properly incentivised?

Yes, considering the safeguards installed and the organization of the client-sponsor-CCP relationship as explained in the previous answer, EACH believes that sponsors are naturally incentivised to not only monitor their clients' activity but also to fulfil their obligation towards their clients.

Q7. Do you think that the number of sponsors is limited? Are you concerned about sponsor concentration risk? If so, is this because it is difficult to find a sponsor? Are there any other reasons?

Yes, the number of sponsors is currently limited. Currently, three agents are offering this model in Europe, of which only one is a global provider. As mentioned in our answers to the previous questions, this is in our opinion due to the fact that the development and adoption of access models is in a very early stage. The availability of sponsors thus reflects the stage of market development. As models and the client clearing market structure mature, there should be no shortage of clearing agents and sponsors considering the competitive landscape for clearing.

Q8. Do you think that CCP rules adequately address the issue of sponsor default? If so, what are the CCP rules that adequately address this issue? If not, what kind of CCP rules are required to address this issue?

Yes, EACH believes that a sponsor default is adequately addressed and managed appropriately as it is treated equivalently to a clearing member default.

Testing

Q8. Have you participated in default management exercises that test direct and sponsored access models?

Yes, CCPs have tested sponsor defaults and regularly run porting simulations.

Q10. Without providing identifying information, what has worked well in such exercises? What has not? Do you have recommendations as to what could be improved for such exercises?

The exercise was successful and proved the robustness of the DMP while raising awareness of challenges in relation to porting client positions. Please also refer to our comments in relation to porting further below, in particular, the possibility to add porting simulations to fire drills.

Additional considerations

Q11. Please describe any additional factors that may be impacting the activity and uptake of direct and sponsored models that are not considered in this paper.

According to EACH Members, additional factors that may be impacting the activity and uptake of direct and sponsored models are the following:

- Improved understanding by market participants of the legal requirements, the set-up and the operational processes;
- Insurance regulation did not envisage the situation of insurers becoming direct members of a CCP through direct access models, and accordingly there is a gap in the regulation preventing insurance firms from using direct access models;
- If policymakers wish to remove any unreasonable barriers to the adoption of direct access models, the Leverage Ratio treatment under Basel III should be equally explicit that unfunded contributions should not contribute to exposure under the measure. Capital charges for unfunded contributions under the Leverage Ratio may materially impact the economics of direct access models, and the business case for adoption.
- Further improvements could also be achieved by addressing the barriers for clients to take on more responsibilities from the clearing members in the default management

process, and by assessing economic incentives in relation to preferential treatments under the Basel framework.

Q12. Please provide any additional comments with regards to the impact that direct and sponsored access models have on access to client clearing.

EACH Members expect direct and sponsored access models to have a positive impact on the clearing landscape because they provide an alternative to traditional client clearing with mutual economic, risk management and operational benefits for agents, sponsors and participants.

Q13. Please provide additional comments with regard to access to client clearing more generally.

No EACH comment.

Porting (Section 3 of the discussion paper)

Risks from not porting

Q14. Are there any additional risks or potential harm associated with not porting following a clearing participant default, which were not described in the discussion paper? If so, please describe such additional risks and/or harm.

Porting is a crucial feature of an adequate default management process and requires a proper regulatory framework and incentives (e.g. upcharges for lack of a back-up CCSP) as well as an insolvency regime that does not prevent the CCP from porting clients of a clearing member (e.g. a gross margining regime – so that there is collateral held in the CCP in order to support a clearing member default – as well as a negative consent regime, even if temporary). The credit and liquidity assessment of the clearing members will be very important to ensure that porting does not create undue risk.

Another important issue would be to remove the need for explicit client consent. Clients always have the option to find another clearing member in the weeks following the default event, but it is crucial to act quickly. Additional useful regulatory intervention could be useful in the area of Know your customer (KYC), Anti-money laundering (AML) and balance sheet requirements for clearing members & CCPs. For more details, please see our answers to the following questions.

Q15. Potentially effective practices. Do you agree with the two tools identified in the discussion paper as potentially successful porting practices? Are there any other tools that should be identified as potentially effective practices?

Yes, EACH agrees with the two tools identified in the discussion paper as potentially successful porting practices: pre-emptively identifying potential alternate CCSPs, and account structures that facilitate fully margined client positions. Regarding the former however, given that client consent is required in the EU, alternate CCSP should come from the client rather than the CCP, as CCPs cannot assume what the client's choice will be.

We also agree with the finding that there are differences in the regulatory frameworks in different jurisdictions which may limit the use of the tools listed in the discussion paper. Indeed, some of them are not applicable to European CCPs.

Further, as previously mentioned in the answer to Q14, capital, KYC- and AML-requirements may prevent swift processes to find back-up CCSPs. To increase the likelihood of successful porting, it may therefore be worth considering allowing for temporary waivers of these requirements for the porting phase.

Q16. What additional approaches do CCPs use to pre-emptively identify a backup CCSP? What incentives can be provided to assist the development of alternative/backup CCSP relationships? Are there any other considerations for alternate/backup CCSPs not set forth in the report?

It may potentially happen that for different reasons clearing members prevent their clients from having secondary relationships with alternative clearing members. We believe that for chances of successful porting to increase, clients should not be prohibited or limited from having secondary relationships.

It is important to note however that clients usually do not have any "back-up CCSPs", but rather have multiple point of access. We are not aware of customers who appointed a back-up clearing member specifically for porting, rather, some clients already have multiple clearing members for other Business as Usual (BaU) reasons, and such alternative clearing member can be used as back-up.

Q17. Are there other considerations for having a game plan that were not described in the discussion paper?

For a game plan to have decent chances of success, the CCP would need to anticipate the decision of various stakeholders, in particular clearing members and all the clients that they serve (likely in the dozens or hundreds of magnitudes). In a regulatory environment where client consent is explicitly required, such game plan has from our point of view low chances of success. We would rather suggest that the clearing members' training and understanding of their clients is improved, given that they have a direct contractual relationship.

Q18. In addition to those outlined in the paper, what attributes of account structures facilitate or impede porting client accounts?

EACH believes that gross margined account structures make it easiest for porting to happen as clients' identification and risk calculations are done individually. In the current European framework, net omnibus accounts require the consent of every client in the account for porting to happen. Given that these clients are often unknown to the CCP, such requirement is unlikely to ever be met within the timeframe of a porting period. This issue can be solved when converging to a regime where client consent is not explicitly required as further outlined in Q21 below.

Considering the first part of the discussion paper, it is also important to that direct and sponsored access models aim at increasing the likelihood of porting.

Q19. Are some client accounts not suitable for porting?

As per our previous answers, net omnibus client account structures where several clients need to consent on the same replacement CCSP make it more challenging to port clients as opposed to gross margined ones. In this context, as alluded to in the discussion paper, client consent mechanisms represent a hurdle for successful porting, and it may be worth considering revisiting local regimes with a view to increase the likelihood of porting in this regard.

Beyond the account set-up, the nature of the business of the client will also affect the likelihood of a successful porting. In the EU regulatory framework, where client and CCSP consent is necessary, the degree of preparedness of the client is critical to the success of porting. In particular, the client would need to maintain connection through multiple CCSPs and spend adequate resources to assimilate and train the porting process(es). Only large clients whose business require to maintain the positions for a long period of time, will find it economically reasonable to invest in making porting feasible. Porting frameworks should therefore also take differences between types of clients into account. While some models should increase the likelihood of porting as much as possible, it should also be noted that some clients may be better off through orderly and cost-efficient liquidation than through porting.

Q20. Does holding excess collateral and the ability to make direct payments improve the probability that a client will be ported successfully or are there impediments to using this collateral?

Yes, holding excess collateral helps improve the likelihood of successful porting. The CCPs ability to provide enough time for the client to find a replacement clearing member will be directly proportional to the collateralisation of such client. Over-collateralisation, or re-collateralisation during the porting period will help the CCP having comfort giving the needed time without burdening its clearing community with additional risks.

Direct payments may also be helpful to allow for a longer porting period even though this option would have to be set-up early in the process and tested regularly as it cannot be improvised on short notice. Furthermore, it may rather work for more sophisticated clients who have the capacities and resources to invest in such arrangements.

Q21. What is your view of a client consent mechanism that could be used to facilitate porting, if permitted under applicable law?

Subject to permission under applicable law, a negative consent or ex-ante client consent mechanism that would allow the CCP to port the client would contribute to a smoother porting regime. Different to US rules, as mentioned above, in the EU porting depends on client consent and is therefore always initiated by the client. To facilitate porting in the EU, authorities together with the insolvency administrator of the defaulting CCSP, could be allowed to organize and to CCP execute the entire porting process in cooperation with the replacement CCSP, similar to the US LSOC-rules. This would however require a change of EU law. Such procedure would speed up the porting process and would also facilitate the liquidation process for the CCP.

Q22. Are the potentially effective practices described in the discussion paper consistent with prior porting experiences?

No EACH response.

Q23. Are there any barriers to implementing potentially effective porting practices that are not described in the discussion paper.

[EMIR Articles 48\(5\) and 48\(6\)](#)¹ require a 'porting window' immediately after a default is called, during which time the CCP is not allowed to liquidate, hedge or perform any other steps defined in the CCP rulebook to manage the risk of client's positions. According to the feedback provided by some EACH Members, this has the unintended consequence of leaving the CCP exposed to the price movements of clients that may ultimately choose not to port or have even indicated they do not wish to port. This creates a potential risk to the CCP and consequently the default fund and unfunded resources. It is, therefore, important to highlight the trade-off between long porting time (higher porting chances, but higher losses upon failure) and shorter ones (lower porting likelihood, but lower losses upon failure).

¹ [Regulation \(EU\) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositoriesText with EEA relevance \(europa.eu\)](#)

Communication and coordination

Q24. Are there any additional communications by the CCP or the defaulting CCSP that may increase the probability of porting client accounts?

CCPs have established communication with clearing members and clients in case of a defaulting CCSP (note that this is also done where a CCP is offering a direct or sponsored access model). Clearing members proactively contacting CCPs about how to manage their clients together in the event of a default is also encouraged as beneficial practice, but the onus remains on the clearing members to initiate this discussion with CCPs. CCPs also make information available on their websites regarding the description of porting processes and necessary requirements and provide exercises to test those processes to facilitate market participants' preparedness.

Further education on the porting process for clearing members and clients alike would be beneficial as it would increase the general understanding of the benefits of and the process behind porting, thereby increasing the number of clearing members and clients that would be prepared for such a scenario.

Q25. Are there additional actions CCPs can take following a clearing participant default to coordinate that are not set forth in the discussion paper? Are there any limitations on coordination that are not included in the paper?

See answer to Q24.

Harmonisation

Q26. Are there additional items CCPs can harmonise or standardise during business as usual that are not outlined in the discussion paper? Are there any factors that may impede harmonisation or standardisation that are not provided in the paper?

Harmonization of porting procedure can only be done within harmonized regulatory environment and Default Management Procedure. The porting process is integrated within this procedure, and in particular is accounted for in the MPOR. Different MPOR often implies different porting procedures or reciprocally. Harmonizing for the sake of harmonization might create more problems than solutions if the working hypothesis are different.

Notable issues to consider when developing a porting protocol

Q27. Are there additional regulatory requirements that could impede porting? Can such impediments be addressed or mitigated through action prior to the CCSP's default?

As mentioned in the answers to the previous questions, client consent mechanisms can impede successful porting. Further, capital, KYC- and AML-requirements may prevent swift processes to find back-up CCSPs. To increase the likelihood of successful porting, it may therefore be worth considering allowing for temporary waivers of these requirements for the porting phase and revisiting client consent mechanisms, converging towards US LSOC-rules. Further, please refer to response to Q23.

Q28. Are there any additional factors that should be addressed in testing exercises?

To further enhance participants' readiness, porting could be included into fire drills

Q29. Please provide examples of good disclosure practices from your perspective.

In the case of some EACH Members, porting procedure and legal documentation are publicly available on their website. However, they agree with the statement in the discussion paper that clients are unaware of this fact. The key reason, however, does not seem to be a lack of transparency, but rather that the likelihood that the defaulted clearing member is theirs [the client's] is too low for the client to be willing to invest the required resources to investigate the porting process. This raises the question of how to incentivize clients to take interest and participate in testing exercises. As an illustrative example of the possible timeline of such an exercise, one EACH member noted it took 3 months to organise and run a porting test with one of their largest clearing members (accounting for elements such as simulating dummy portfolios and commercial considerations).

Where regulated entities such as Banks are concerned, these will often have visibility of their risk protocols due to disclosures they make (e.g. quantification of their risk as their value at risk). This in raises the question of whether all these protocols disclose how to handle client clearing and porting exercises. Such disclosures in these risk protocols would be good practice and should be facilitated by Clearing Members first and foremost.

Q30. Are there other arrangements a CCSP can make to ensure that, post default, the CCSP can help coordinate porting at multiple CCPs if the CCSP is a non-defaulter? If the CCSP defaults, what arrangements can the CCSP make to facilitate the porting of its clients?

Please refer to answers to Q24 and Q29.

Suggested next steps

Q31. Please provide feedback on the suggested next steps for consideration. Do you agree that these issues warrant further consideration by CCPs, CCSPs and/or clients? Are there additional issues that may warrant further consideration?

As illustrated in the answers to the previous questions, EACH believes that whilst a lot of attention has been placed on CCPs, the next steps should primarily focus on CCSPs and clients. Please refer to these previous answers for our views on the different next steps for consideration suggested by the CPMI and IOSCO in the discussion paper.

Furthermore, while CCPs might take individual steps to improve where they see fit, harmonization of regulatory landscapes is necessary for any significant improvements in porting procedures on a systemic level. We would appreciate in particular a temporary exemption from AML, KYC and capital requirements during the porting phase as well as review of client consent mechanisms, converging towards the US LSOC-rules, which would require a change to the EU provisions. In addition, the introduction of porting exercises within the EMIR fire drill framework could be considered to further enhance awareness and readiness by market participants.

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