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Submitted via email to: cpmi@bis.org and
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Dear Sirs

IA Response to the Consultative Document "Resilience and recovery of central counterparties (CCPs): Further guidance on the PFMI" dated August 2016

The Investment Association is grateful for the opportunity to respond to your consultative report "Resilience and recovery of central counterparties (CCPs): Further guidance on the PFMI" and related cover note of 16 August 2016 (together, "the CP").

We would like, first, to commend the CPMI and IOSCO for their work to tackle the risks to financial stability posed by a crisis at a CCP, in particular the work to elaborate the PFMI.

This response reflects our members' views as informed by their fiduciary duties to their investors, who – as the counterparties to the derivatives agreements concerned – are directly impacted by the policy proposed in the CP.

End-investors are individuals with savings and pensions and are also tax payers. They have a direct interest in ensuring an effective and fair regime for recovery and resolution of CCPs. They are also major users of CCPs.

As fiduciaries of investors, our members have supported the post-crisis mandatory use of CCPs in the expectation that investors' savings in turn are safeguarded by the infrastructure and their rights are protected.

An effective regime for central clearing can strengthen investor confidence. Investor confidence also underpins financial stability. A loss of confidence leads to reduced investment and investor flight which can exacerbate a crisis. We ask that IOSCO and the CPMI take the end-investor interest fully into account in finalising the policy outlined in the CP.

Yours Faithfully

Angus Canvin

Senior Adviser

ANNEX I
CONSULTATION RESPONSE

ABOUT THE INVESTMENT ASSOCIATION

The Investment Association is the trade body that represents investment managers doing business in the UK. Our 200 or so members collectively manage through their businesses in the UK over £5.7 trillion on behalf of clients.

Our purpose is to ensure investment managers are in the best possible position to:

- Build people's resilience to financial adversity
- Help people achieve their financial aspirations
- Enable people to maintain a decent standard of living as they grow older
- Contribute to economic growth through the efficient allocation of capital

We are the second largest investment management trade association in the world by assets under management (AuM) of our membership.

More information can be viewed on our website.

INTRODUCTION

Asset management, derivatives and CCPs

Investors make significant use of derivatives, which they are rightly permitted to do (e.g. under UCITS legislation), whether for hedging purposes or to express an investment view. At the same time, in the EU EMIR requires mandatory central clearing of many derivative categories, meaning investors – Europe's tax payers saving for life's eventualities and pensioners – must use CCPs for these derivatives. Hence The Investment Association – representing the asset managers, which manage these investors' investments, including in derivatives – takes an interest in the regulation of CCPs, including CCP recovery and resolution ("R&R").

Unlike CCPs and clearing members (CMs), which benefit commercially in several ways from mandatory central clearing[1], CM clients/end investors pay for mandatory central clearing. This has implications for the funding of CCP recovery and resolution. Consistent with the principle that no taxpayer money should be at risk, it has been suggested that the private sector participants, which benefit commercially from central clearing, should collectively bear the cost of CCP recovery and resolution. This rules out the buy-side.

The obvious source of recovery and resolution funding from those that benefit from central clearing is, of course, the CCP's *ex ante* resources: the "waterfall", including initial margin of any defaulting member and default contributions from participants, as well as the CCP's own capital. Each of these layers of protection are provided by the entities who are earning a return for the provision of the clearing services. It follows that CM client/end investor property (e.g. margin) should not fund CCP recovery and should only be available in

[1] For example, CMs earn fees and other income through providing clearing services. They also benefit from the multilateral netting resulting from the CCP becoming the counterparty to every centrally cleared derivatives trade. The commercial benefits to CCPs are self-evident.

resolution consistently with ordinary principles of insolvency, in particular, the principle that no creditor would be worse off than under an ordinary liquidation ("NCWO" principle).[2]

Where a CCP is threatened by CM default(s) (we refer to this sort of crisis as a "CM default crisis" in distinction to a business disruption crisis, such as might be caused by cyber-attack or fraud), the management of that crisis requires careful coordination of the bank recovery and resolution measures taken concerning that CM and the crisis measures for the CCP. Recovery measures for the CCP should avoid contagion to other CMs and not exacerbate the difficulties of the CM(s) under threat. Similarly, recovery measures for the CCP should not threaten financial stability in other ways, such as by embedding perverse "first-mover" or similar incentives through threatening end-investor property in the form of margin.

Use of Margin

The role of a CCP is to mitigate bilateral counterparty credit risk. This is achieved through the benefits of multilateral netting and by the collection of margin. In normal market conditions CCPs substantially reduce counterparty credit risks. However, CCPs concentrate counterparty risk in systemic size. Their systemic size makes it vital that there be:

- Clarity as to the point at which they are no longer viable ("point-of-non-viability"/"PONV"); and
- Decisive intervention by resolution authorities at that point.

Once a CCP has exhausted its substantial resources (the waterfall), it will have failed its most important function: modelling risk to a standard that gives the market sufficient confidence to go on using it. Indeed, it is worth considering how realistic it could ever be to "recover" a CCP pushed to insolvency by reason of CM default(s), given the profound failure of the market in the asset class in question that would see the CCP's going-concern/waterfall resources consumed. There would be doubt that any CCP could accurately measure and manage risk arising from that asset class post-recovery.[3]

This is why the Investment Association supports clear resolution measures, but not open-ended recovery attempts. Indeed, beyond utilisation of the waterfall we see very few appropriate recovery measures (e.g. auctioning the defaulting clearing member(s) positions with participation beyond surviving CMs; transfer of non-defaulting CM client/end investor positions to non-defaulting CMs)[4].

The function of initial margin (IM) posted by an end investor in derivatives to its CM is to provide the CCP with protection in the event of default by the CM with respect to transactions initiated by the end investor (the client of the clearing member): it is security for the performance by the CM and the end investor of their contractual obligations. It represents the *potential* change in market value of a derivative. End-of-day margin payable by the CCP to anyone with a mark-to-market gain ("variation margin (VM) gains" - VMG) merely reflects current exposures resulting from actual changes in market prices, i.e. VMG represent the *actual* change in market value of a derivative. Margin is the property of the CM client/end investor and is, therefore, qualitatively different from both CCP capital and CM participation in loss mutualisation, which are both specifically targeted to bolster the CCP's solvency.

As margin covers end investor default (and, by extension, CM default – a double default), it is essential (especially in a time of crisis, when confidence will have been hit hard) that the

[2] NCWO embodies a fundamental human right: protection of property (see e.g. Article 1 of the first Protocol of the European Convention for the Protection of Human Rights and Fundamental Freedoms)

[3] In contrast, recovery is conceptually feasible where a CCP is in difficulty because of cyber-attack, fraud or other operational issue, where "recovery" will involve measures akin to business continuity measures, rather than running through the waterfall.

[4] These are really default management measures. Porting to non-defaulting CMs should have been done BEFORE the CCP is in distress (it is unclear what good it could do subsequently) and the auction process is often done before the assessments are allocated to the clearing members.

IM and VMG of non-defaulting CMs - and of CM client/end investors - are protected from confiscation ("haircutting") in any crisis response. Otherwise, segregation of margin would be in vain and all margin – CM and end investor – would be commingled in the sense that all would be similarly available for seizure.

It is not possible to predict the size of any shortfall at a CCP threatened by CM default(s), nor, therefore, the amount of margin at risk of haircutting, because you would be dealing with a systemically unstable situation. Assuming that the CCP had modelled its waterfall properly (including meeting the IOSCO standard), a failure would in practice arise from the collapse of several CMs, meaning additionally that other CCPs would be in trouble simultaneously, as well as, potentially, other market participants (including other CMs). Imposing an uncapped liability on end-investors (via open-ended haircutting of IM and/or VMG) at such a time would exacerbate that systemic uncertainty. That prospect would incentivise investors not only to run from a CCP that was perceived to have any weakness relative to others, but also to re-evaluate their exposures in other capital markets – and this at a time of profound financial crisis - potentially propagating the crisis throughout the financial system.

IM should never be used as a recovery tool in a crisis. Using IM would leave the CCP more vulnerable to further CM default, making problematic their ability to resume business, even if otherwise successfully "recovered" (unless the shortfall in IM was made good, but that would likely only be possible from public moneys – contrary to the understandable reluctance by the authorities to use taxpayer funds to rescue a CCP – given the sort of crisis that would be underway). Taking IM off the table would also provide additional protection against contagion to other CMs.[5]

VM is also the property of end users; it does not represent gains that accrue to the CCP or CM. Haircutting VMG introduces unlimited liability at a point in time when the CCP has proven to be incapable of modelling risk, because neither the quantum of VMG nor the number of haircuts to VMG are knowable *ex ante* and may be very large given the potential market moves in the sort of financial crisis that would bring down a CCP. VMG haircutting also unfairly penalises end-investors as against CMs, for it is in practice these end-users of CCPs – with their directional positions in derivatives – that would suffer loss from haircutting VM. CMs, by contrast, will tend to have a "flat" book, as their role as intermediary naturally gives rise to more risk-position offsets. To the extent that the pension and insurance fund end-investors use derivatives to hedge exposures on underlying investments, haircutting VMG will increase their market exposure. This could exacerbate the crisis, as these end-investors sought to support their ability to meet their liabilities.

Therefore, VMG haircutting should only be considered as a measure of last resort subject to the following comprehensive layering of protections to protect against real-economy losses[6]:

1. CCP resilience is rigorously regulated and supervised
2. strict limit on the time for "recovery" measures after the exhaustion of the waterfall: a matter of days only (depending on the product concerned, CCP and other relevant factors);
3. an *ex ante* cap or limit on the potential loss to end investors;
4. a commitment to compensate those investors (which must be robust, i.e. sure to be paid by viable stakeholder(s)); and

[5] CCP recovery measures should not inadvertently increase risks to financial stability. Threatening margin not only incentivises stability-threatening behaviour by end investors, it may threaten the viability of CMs, at precisely the time – in the midst of an extreme financial crisis – that protection of CMs would be an important financial stability imperative.

[6] VMG haircutting poses additional problems for use of derivatives by UCITS: use of UCITS assets for securing third parties' obligations is prohibited; how could a prospectus describe the risk of VMG haircutting?

5. the CCP's resolution authority controls any VMG haircutting and is tasked to take account of the interests of investors/end-users in exercising this control

In summary:

IM haircutting

1. IM is calibrated to cover own default risk, not that of other participants
2. IM would need to be replenished very swiftly (within days), in order for the clearing service concerned to continue
3. This might further destabilize CMs, end-users and the entire financial system, in a CM default crisis
4. IM haircutting creates liquidity and procyclicality risk on the CCP participants
5. CCP have unilateral ability to increase IMs in an unlimited way. IM haircutting risk would be neither measurable nor manageable for participants.
6. CCP R&R should not disincentive clearing over bilateral transactions. Under bilateral transactions, IM is protected through pledges and custodian agreements. Haircutting IM on cleared transactions would strongly disadvantage clearing over bilateral OTC
7. Therefore, IM haircutting should be taken off the table

VMG haircutting (VMGH)

8. Variation "margin gains" are actually the profit of a given end-investor such as a pension fund
9. Participants with VMG are not better off than those bearing losses; derivatives are used for hedging purposes, so any VM hedging gain would compensate underlying loss and vice versa
10. Therefore, VMGH is not neutral for participants (as it leads to temporarily unhedged positions)
11. End-investors who fear they will be subject to profit appropriation through VMGH will rationally seek to rapidly close out positions, which is potentially destabilising on a system-wide basis
12. VMGH also risks cascading defaults as participants expecting VM payments to cover hedging or other costs may not be able to fund the unexpected shortfall
13. It should never be available to a CCP as a recovery tool, but should only be available to resolution authorities
14. VMGH are only measurable and controllable to the extent they are be capped or limited in time (to allow for assessment of gap risk)
15. 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
16. VMGH risks perversely incentivizing CMs: to push the CCP to use VMGH once the default fund is exhausted (or close to exhaustion), in order to recover gains from client VMGH during the auction process

CCP resilience and resolution are key

Of course, we share with other stakeholders (CMs and CCPs) and the public authorities the goal that a CCP should have sufficient ex ante resources/ waterfall in place ahead of any crisis: the CCP must be resilient to crisis. In addition, CCPs need to be incentivised further to protect the interests of their users (CMs and end investors). CCP "skin in the game" (or capital; SITG) should be substantial, therefore, even if this gives rise to higher clearing costs, which should of course be measured against the monopolistic revenue-making ability of a CCP.[7] The quantum of capital/TLAC for CCPs is best sized through a well-designed stress-testing regime (incorporating a better understanding of the scenarios in which they would face difficulty).

[7] However, there is a tension between CCPs providing a market utility (suggesting utility-level revenues) and the cost of central clearing.

But above all, there needs to be a plan to close any CCP that was discredited, with losses shared fairly and definitively.

The resolution regime should give the resolution authority(-ies) significant discretion as to how they close a failed CCP (or failing clearing service, if just one service is affected and the rest of the CCP can be saved)[8], but always subject to NCWO.

When a CCP has failed, it should be required to implement a resolution plan quickly – subject to oversight/control by the resolution authority – with a clear and rapid process to limit end-user losses and contagion to the real economy, along with a timely and orderly repayment of margin (subject to NCWO). Time would clearly be of the essence (as it is for recovery post waterfall exhaustion).

End-investors might best be protected through the transfer of their positions (and related IM and unpaid VMG) to a viable CCP(s). This approach – prioritising "position good" and minimising replacement of positions in stressed market conditions – might best promote the wider public interest. It requires that both CCPs and CMs are able to transfer non-defaulting positions rapidly in a crisis.

The "position good" approach would avoid, in a stressed market, re-hedging by end investors that might increase systemic risk (and would be very difficult under crisis conditions). In contrast, a close-out approach would lead to substantial unhedged risks in investor portfolios (potentially in breach of risk, capital or regulatory constraints).

Alternatively, the public interest might be better promoted by rapid close-out of positions to minimise end-user loses and contagion to the rest of the system – a so-called "money good" approach. Resolution authorities will need the flexibility to deal with the crisis at hand.

The resolution authority should have the power to suspend the mandatory clearing obligation[9] – as, indeed, should the authorities managing a crisis threatening the CCP, even ahead of the waterfall being exhausted – so as to allow market participants the greatest flexibility to manage their risks (e.g. through bilateral derivatives, if they so choose). This should be financial stability enhancing, as it gives market participants – including end investors and their asset managers – timely opportunity to mitigate their risks.

CP RESPONSE

Governance

The CCP's core function is to manage the risk it takes on in becoming the seller to every buyer and the buyer to every seller in the derivatives that it clears. Consequently, the risk management function is of central importance and the governance of that function must be assured. The audit function is important to assure the quality of risk management, so the independence of the internal function – including through direct reporting line to the CEO – is crucial.

We welcome the proposed guidance, subject to the following comments on 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.

[8] Or implement some other resolution action, such as transfer to a "bridge CCP" or another existing CCP(s).
[9] As implemented by "EMIR" in the EU

- Market participants require a full explanation of the CCP's risk profile, in order to do their due diligence on a CCP. The PFMIs are a step forward in this direction, but disclosure is insufficiently frequent (only every 2 years) and 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 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.

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 recognises the importance of end-investor views being represented in the CCPs' risk committees. There should be specific guidance introduced on the broader topic of disclosure and transparency.

Stress testing

We support annual mandatory standardised stress tests conducted by the 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 framework that includes idiosyncratic stresses on basis and higher order risk exposures embedded within individual CCP portfolios.

Stress tests should incorporate liquidity and credit stresses. The stress test must appropriately consider the gross risks to the CCP, allowing for the possibility that an unmatched book emerges in the crisis scenario.

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 stakeholders in central clearing.

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 that our members 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.

Coverage

As part of its core risk management function a CCP seeks to mitigate credit risk in a default, through the layers of protection it has in place, including IM and other loss absorbing resources. Market participants have a direct interest in the size of these resources. Specifically, risks and rewards need to be aligned such that all participants are incentivised both to prevent losses and to minimise losses in the event of a market disruption.

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. Rather, dynamic margin calculations, risk-based CCP contributions, capped CM 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.

Cover 1 and 2 are minima, so all CCPs should maintain resources above these minimum requirements. CPMI-IOSCO's guidance should provide further clarity on the "additional resources", which CCPs applying Cover 2 must maintain. Moreover, Cover 2 should be observed continuously and any breaches of the Cover 2 principle should be disclosed (though not necessarily at the time of the breach, but through annual / semi-annual reporting).

We support the formulation of Cover 1 and Cover 2. However, further work is required to assess how coverage might reflect different participation (viz. proprietary transactions vs. client transactions) and different kinds of clearing and segregation models, reflecting that:

- Typically the volume of client transactions to be cleared via a CCP is subject to a limit set by the CM on an individual basis (indirectly also limiting potential risk a CCP might face in that regard)

- In contrast to the proprietary transactions of CMs, the client clearing claims, which the CCP has against its CM, are typically backed (e.g. via a pledge) by the corresponding claim, which that CM has against its client. Under such a scenario a CCP faces a significantly lower risk. A CCP would only face losses in case of a double default (CM and client) combined with a collateral shortfall

- Different segregation models impact the volume of collateral that is available: individual segregated client accounts require more collateral to be posted.

However, 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."

Further 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 a CCP must have prefunded and committed resources to cover the possibility that its largest two CMs will fail and either provide additional cover or demonstrate that "Cover 2" is sufficient. Cover below Cover 2 is insufficient to protect CMs' customers from a CCP failure and, under certain circumstances, Cover 2 is insufficient. For example, a CCP that has many smaller CMs will have more broadly distributed risks for which its two largest CMs would be disproportionately small given the total exposure.

Margin

We agree that a CCP should expose a portion of its own resources to losses related to CM default and also to non-default losses. Stakeholders derive comfort from the fact that the CCP has "skin in the game" in respect of such losses

We welcome the additional guidance on margin suggested in the CP. We suggest that a CCP should "expose a separate amount of its own resources to remaining losses concurrently or after allocating a portion of such losses to its participants." Currently the guidance only states that a CCP "may also choose" to expose a separate amount of resources.

We understand the concern about increasing IM in a period of market stress. However, this procyclicality risk is mitigated by the benefit to market confidence from the knowledge that additional assets are supporting open positions. In addition, raising IM is less pro-cyclical than VMG haircutting, which would incentivise directional market participants to close-out at the earliest signs of CCP distress.

The Margin Period of Risk (MPOR) should be based on the risks specific to the derivative contract concerned 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.

We emphasise 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.

CCP contribution to loss

The buy-side interest in the allocation of loss as between CCP and CMs is to ensure that the rules maximise the incentives of both the CCP and the CMs to protect the CCP from failure. Moreover, the CCP and its owners are responsible for the financial liabilities that can arise from running the business.

In our preliminary comments we outlined the issues with VMGH. It follows that losses from running the clearing business should not be allocated to the CCP's customers through VMGH: customer's money should never be appropriated to support the continued operation of a failing business.

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 avoid the possibility of an uncertain liability they would otherwise face through VMGH, if a CCP were to fail.

Recovery Planning

Our preliminary comments make clear that policy should 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. For this reason, CPMI-IOSCO should prohibit the use of VMGH at any point prior to resolution.

VMGH is a misleading term. 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, only 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 close out positions rapidly, which is potentially destabilising on a system-wide basis, i.e. procyclical and crisis-propagating.

VMGH disincentivises 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, our preliminary comments set out the conditions that should apply.

CCPs should never be permitted to use customer margin to address their liquidity needs. We recommend that CPMI-IOSCO prohibit 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.

We also believe that additional guidance regarding broadening auction participation would help CCPs in re-establishing a matched book post a CM default. 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. Asset managers, for example, are already incentivised the right way and can only improve the auction process. Proposals for asset managers or their clients to contribute capital fail to recognise 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. 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.