

## **CCP for CDS User Requirements**

Meeting of the European Central Bank

Tuesday, 24 February 2009

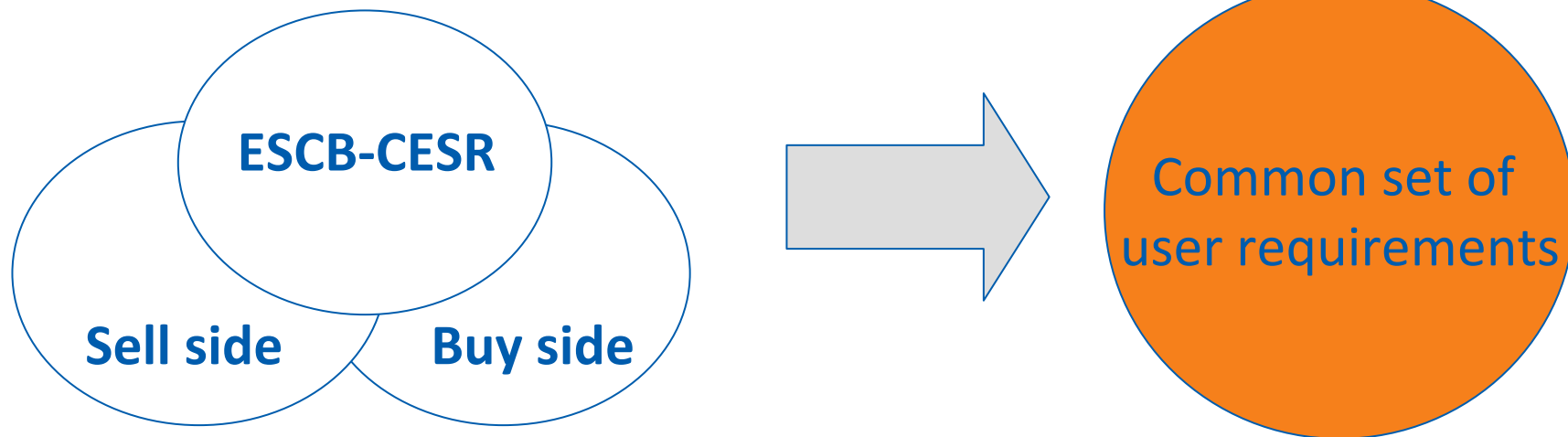
Mr Paul O'Connor

Chairman, EBF Derivatives Task Force  
Head of Wholesale Banking, Irish Banking Federation

## *Representativeness and Expertise*

- The European users' position
- 31 national banking association members = 5,000 banks
- Large and small, domestic and cross-border
- Buy-side and sell-side
- EBF Derivatives Task Force = derivatives expertise drawn from across all the major European financial centres
- Wider accountability to EBF structure = consistency and representativeness of position

## *Aims of the Exercise*

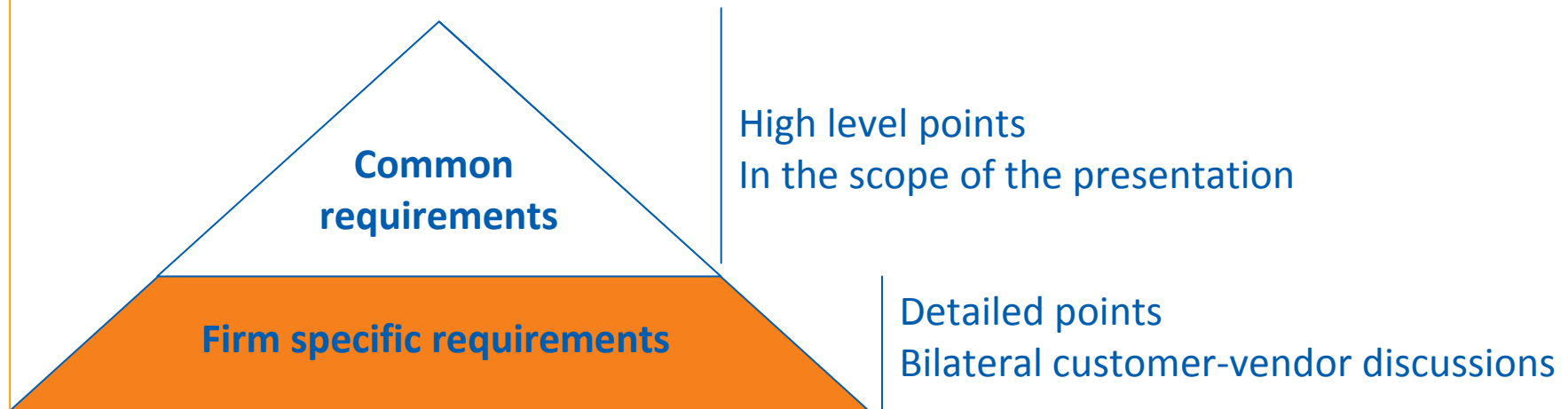


1. To achieve consensus between the buy and sell-sides' requirements
2. To assess the extent to which this is covered by authorities' requirements
3. To deliver a common set of requirements to the CCP providers

- Users' support of CCP clearing of CDS in Europe
  - it provides for regulatory oversight
  - it is an efficient way to support OTC trading
- However, this is a global market so global consistency of approaches and outcomes is all important
- Eligibility of CDS is a key concern, as is the commensurate capital charge applied to CDS not cleared through CCPs
- Users will come to their own decisions on which of the CCP providers best suits their needs

## *User Requirements*

- A. Legal and Regulatory Environment
- B. Governance and Access
- C. Scope
- D. Stability and Resilience of the CCP
- E. Functionality and Efficiency



## A. *Legal and Regulatory Environment*

1. Subject to the Settlement Finality Directive (i.e. recognition as a “securities settlement system”)
2. Subject to the ESCB-CESR Recommendations
3. Governed by European law
  - e.g. in relation to data privacy and securities ownership
4. Overseen by relevant supervisory bodies and compliant with relevant laws applicable to CCPs in the country of location
  - Effective cooperation and coordination between relevant European supervisors
  - Effective cooperation and coordination with relevant supervisors from 3<sup>rd</sup> countries

## *B. Governance and Access*

1. Users are represented in the governance of the CCP, including at Board level
2. Users should be appropriately consulted and in a timely fashion on decisions that may affect them
3. Access criteria should be:
  - objective
  - non discriminatory
  - risk based (according to capital)
  - designed so as not to deter the access of smaller European players

1. The European CCP should cover at least European CDS indices and single names
2. CDS on US indices could also be considered
3. The CCPs' clearing model could be leveraged to include other standardised and eligible OTC derivatives



## *D. Stability and Resilience of the CCP*

1. Segregated accounts for its members and third parties
2. Adequate safeguards and clear rules around collateral management
3. Effective, transparent and documented default process
4. Avoidance of competition on risk management grounds
5. Access to adequate liquidity means
6. Where relevant, separate default fund for CDS

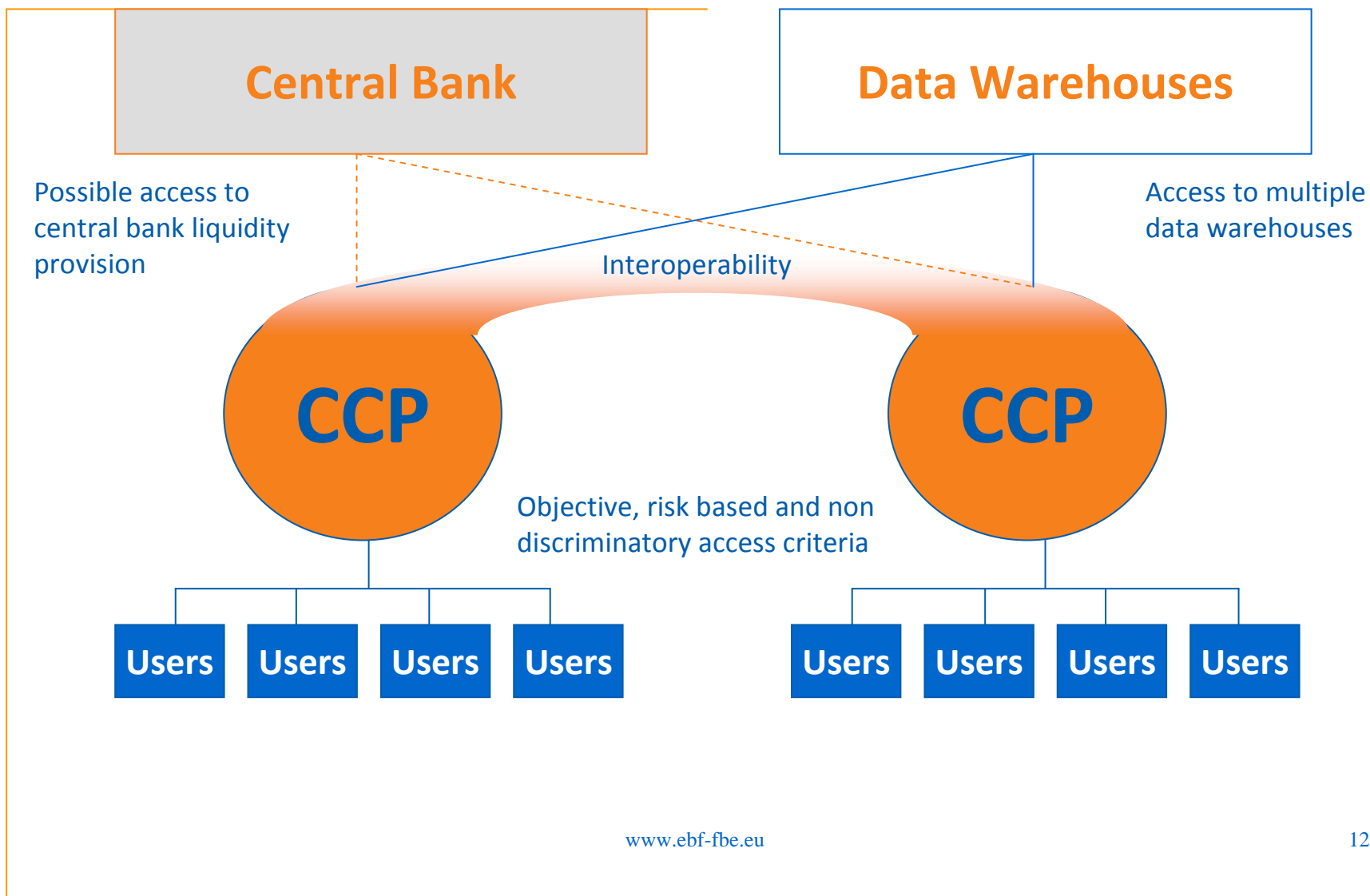
## *E. Functionality and Efficiency I*

1. CCP responsible for:
  - Novation
  - Multilateral netting
  - Position management
  - Valuation
  - Margining
  - Collateralisation of open positions
  - Default management processes
  
2. Back loading of existing contracts must be possible
  - Restructuring credit events
  - Capacity for both cash and physical settlement
  - Trade compressions

## *E. Functionality and Efficiency II*

3. Leverage existing systems as far as possible
  - Open to various OTC matching systems
  - Access to existing data warehouses
4. Clear in multiple currencies
5. Consideration of interoperability possibilities within Europe and globally (balanced against the risk implications)
5. Follow the TARGET2 calendar and opening times
6. Transparency around price calculation methodologies
  - Connect to pricing databases to compliment end-of-day pricing feeds

## Summary - CCP Connections



# Summary – High Level User Requirements

<b>A</b>	<b>Legal and Regulatory Environment</b>	<b>D</b>	<b>Stability and Resilience of the CCP</b>
A1	Settlement Finality Directive	D1	Segregated accounts for members and 3rd parties
A2	ESCB Recommendations	D2	Clear rules around collateral management
A3	Governed by EU law	D3	Effective default processes
A4	European supervisory oversight	D4	No competition on risk grounds
<b>B</b>	<b>Governance and Access</b>	D5	Access to adequate liquidity means
B1	User representation	D6	Separate default fund for CDS (where relevant)
B2	User consultation	<b>E</b>	<b>Functionality and Efficiency</b>
B3	Appropriate access criteria	E1	Core CCP competencies
<b>C</b>	<b>Scope</b>	E2	Back loading of existing contracts
C1	European indices and single names	E3	Leverage existing systems
C2	US indices	E4	Clear in multiple currencies
C3	Extension of clearing model	E5	Interoperability
		E6	TARGET2 calendar and opening times
		E7	Transparency around pricing

- Many considerations to take into account
- Issues are technically complex and the number of dependencies is high
- The users' commitment to central clearing of CDS in Europe is strong – we have come a long way very quickly.

### *Key question*

- What can the CCP vendors now deliver for the users and by when?

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