Please note that the comments expressed herein are solely my personal views

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30 August 2013

- 17 CFR Parts 39, 140, and 190
- RIN Number 3038-AE06
- Derivatives Clearing Organizations and International Standards

Dear Ms. Jurgens.

Thank you for giving us the opportunity to comment on your Notice of proposed rulemaking: Derivatives Clearing Organizations and International Standards.

You are proposing amendments to your regulations to establish additional standards for compliance with the derivatives clearing organization (DCO) core principles set forth in Section 5b(c)(2) of the Commodity Exchange Act (CEA) for systemically important DCOs (SIDCOs) and DCOs that elect to opt-in to the SIDCO regulatory requirements (Subpart C DCOs). SIDCOs and Subpart C DCOs would be required to comply with the requirements applicable to all DCOs, which are set forth in the Commission's DCO regulations on compliance with core principles, to the extent those requirements are not inconsistent with the requirements of the regulations in this proposed rule. The proposed amendments include: Procedural requirements for opting in to the regulatory regime as well as substantive requirements relating to governance, financial resources, system safeguards, special default rules and procedures for uncovered losses or shortfalls, risk management, additional disclosure requirements, efficiency, and recovery and wind-down procedures.

In general I support the proposed amendments. The proposals will promote market integrity, improve transparency and reduce the risks associated with the OTC derivatives market, particularly systemic risk. It is clear that DCOs are a core feature of the financial market infrastructure, and it is therefore important that the DCOs are themselves robust, safe and risk managed. This will be even more relevant as consolidation will lead to few super-DCOs, which are themselves systemically important financial institutions. These proposals improve consistency with the Principles for Financial Market Infrastructures (PFMIs) published by the Committee on Payment and Settlement Systems and the Board of the International Organization of Securities Commissions (CPSS–IOSCO).[1]

Definition of "activity with a more complex risk profile"

I agree with proposed § 39.2 that defines "activity with a more complex risk profile" to include specified instruments, such as credit default swaps, and any other activity designated as such by the CFTC under § 39.33(a)(3), whose wording closely follows the PFMIs. I also support the principles-based wording under § 39.33(a)(3), and the inclusion of wrong-way risk as a complex risk. This will result in higher financial resources requirements for such activities, which should improve the robustness of DCO clearing systems and help to protect the financial system from contagion.

Liquidity risk management

I support proposals which would require DCOs to conduct internal cash flow projections and liquidity stress tests. Liquidity stress tests should consider market stress, idiosyncratic stress and combinations thereof. Importantly, liquidity stress testing should consider the potential actions of other market participants that would experience the same liquidity stresses. In extremity, assets used to offset projected funding needs should be discounted to reflect their credit risk and market volatility.

Annual model validation

Proposed § 39.36(e) requires an annual validation of the financial and liquidity risk management models.[2] I support this. For consistency with the general PFMIs I would add that the validation should not be carried out by the persons responsible for the development, implementation or operation of the systems and models being tested.[3]

Yours sincerely

C.R.B.

Chris Barnard

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[1] Available at: http://www.iosco.org/library/pubdocs/pdf/IOSCOPD377.pdf

[2] Minor point: § 39.36(e) refers to "liquid risk management model"; I think this should be changed to "liquidity risk management model".

[3] This would be more consistent with, for example, PFMIs paragraph 3.2.16 concerning Model Validation.