Clearinghouse Benefits and Risks

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A Successful Track Record

1888

- Replacing bilateral trade obligations
- Insulating counterparties from each other; reducing risk of default propagation
- Setting risk management standards on members
- Reducing aggregate risk via netting

2008

- Managing Lehman default

2009

- G-20 identification of clearinghouses as a key component to mitigate systemic risk

2012

- Protecting underlying clients by collateral segregation and portability protocols

2013

- Mandatory clearing in the US

2014

- **Clearinghouses as "systemic risk managers"**

Managing and Mitigating Risk: Avoiding a "Race to the Bottom"

Risk Concentration

Credit | Liquidity | Operational

CLEARINGHOUSE

Risk Mitigation

Clearinghouses

- Initial margin
- Default fund
- "Skin in the game"
- Recovery & resolution

Board Members

- Independent board members

Members / Clients

- Participation on CCP risk committees
- Consultation

Managing and Mitigating Risk

Assessment

- Default fund management
- Initial margin requirements

Monitoring

- Credit risk / CCP member exposure
- Mark-to-market
- Stress tests

Engagement

- Active Board participation by users and independent directors
- New York Fed Payments Risk Committee Transparency Task Force
- Other consultative bodies

Regulation

- Global, coordinated efforts
- Greater transparency and clarity on rules
- Resolution and recovery
- Access to central banks

Conclusion

1. **Risk Management: Quality of risk management must always be paramount**
   - Eligible collateral
   - Initial margin confidence factors and model add-ons
   - Default fund methodologies
   - Liquidity

2. **Governance: Active engagement by users and independent directors on risk committees provides important check and balance to commercial goals**

3. **Transparency: Members, clients, regulators and the public need to understand clearinghouse approach to:**
   - Evaluation and monitoring of clearing members and their clients
   - Margining and default funds
   - Default procedures
   - Collateral structure and segregation / investment
   - Investment balances
   - Liquidity