

CRD IV

4 May 2012

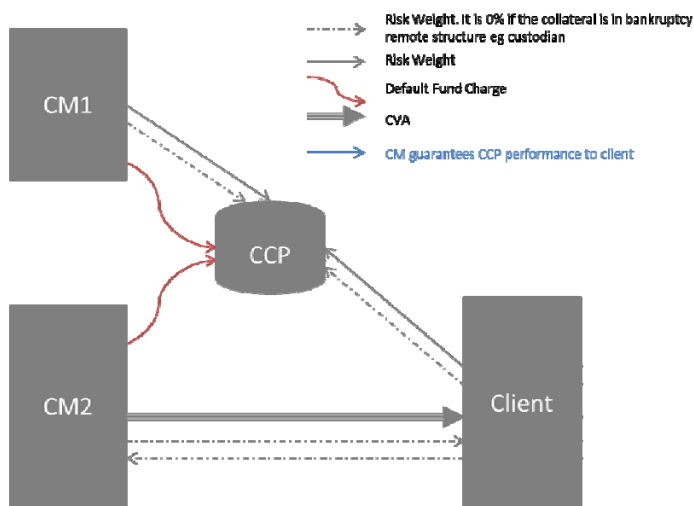
Central Counterparties (CCPs) - Non-finalised Capitalisation Rule on Exposure to CCPs

The Issue

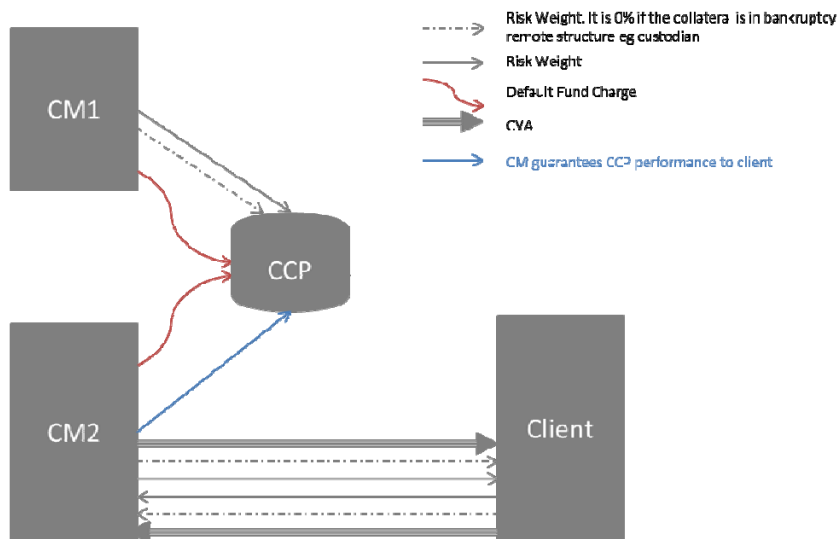
The recent consultation from the Basel Committee on capital requirements for exposure to CCPs closed for industry comments on 25 November 2011, and the final requirements are yet to be published.

The proposed capital charge for exposure to CCPs can be illustrated in the diagrams below:

Client trades identifiable & portable, and collateral segregated from loss



Client trades and collateral not segregated and portable



As you can see, the Clearing Members are subject to two charges: 1) a risk weight between 0% and 4%; and 2) Default fund charge which is partially based on the hypothetical capital calculated by the CCP using the Current Exposure Method

An illustrative study based on realistic assumptions¹ has proven that the current exposure method which is used to calculate the CCP's hypothetical capital is risk insensitive and does not reflect the true risk of a CCP. This implies that this new capital requirement will discourage the propagation of central clearing, in contrast to the policy objective stated by the G20. It could also potentially result in a misallocation of capital and liquidity on a macroeconomic scale with strong pro-cyclical effects when market conditions become distressed. In addition, the final Basel text has yet to be published and it is likely to be changed.

AFME has proposed a new article to adopt further changes through the legislative process, and to allow these provisions to be adjusted at a later point, e.g. to deal with unintended consequences. Consideration could be given to allow the CRD IV text to be adapted through the legislative process in order to deal with developments that occur at the Basel level. These provisions should also be flexible e.g. to be able to deal with the unintended consequences. An observation period could also be introduced before the final capitalisation rules apply to the banks exposures to CCPs. This will provide the industry, including CCPs, the time to implement the necessary changes to produce capital figures in compliance with regulatory reporting deadlines. It would also provide the regulators the opportunity to review the CCPs' models, and to make improvements where necessary.

¹ "Joint associations' letter on Basel Committee on Banking Supervision ("BCBS") Consultative Document: Capitalisation of bank exposures to central counterparties ("CCPs")", 25 November 2011, Page 3
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