

# Central Counterparty Global Conference 2008

## Panel: Market Participants Drivers and Needs

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MF Global Hong Kong

**April 17, 2008**

CCP 12 Conference  
April 16-18, 2008  
Tokyo, Japan



# Roles, Models & Requirement



## - **There are numerous models**

- Exchange ownership e.g. CME
- User ownership e.g. DTCC
- Hybrid – Exchange owned, user controlled e.g. OCC
- Hybrid – mixed ownership, heavy exchange ownership e.g. LCH

## - **FCM role**

- Contracting party – open interest technically a contractual relationship between FCM and CCP.
- Responsible for paying CCP fees and charges.
- Contribute the default fund risk capital that allows CCP to operate.

## - **FCM requirements**

- Operational integrity – that the CCP is open for business every day
- Risk management – that the default fund is properly protected.
- Fees and charges – that these are reasonable and not subject to abuse arising from monopoly position.
- Innovation – that the CCP is constantly looking to improve and extend its services.

- **How does CCO ownership and governance affect these requirements**
  - In relation to operational integrity and risk management, probably very little. Regardless of structure, CCPs strive for excellence in these areas - as do their regulators!
  - In terms of innovation, Exchange owned CCPs claim that they have greater control over development. Evidence of this (in comparison to non Exchange owned) is not strong – LCH introduced swap, repo and equity clearing during a phase of user ownership and governance.
  - In relation to fees and charges, Exchange ownership can lead to conflicting interests.
  
- **Nature of conflicting interests**
  - An analyst recently described an Exchange as “a regulatory protected monopoly with a barrier to entry called clearing”
  - This is at the heart of the potential conflict of interest. Whilst Exchange ownership of clearing is generally accepted to be operationally neutral, it can lead to higher prices and other practices that are unchallenged by competing forces. This can also be the case if independent CCPs offer ringfencing to the business of their Exchange customers.

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- **What would FCMs prefer to see:**

- It is a case of striking the right balance
- CCPs should not be part of an Exchange's financial strategy but instead should offer totally neutral, value for money, risk centred services
- But if owned by an Exchange, for improved development resource and time to market (as is usually the given reason), CCPs should ensure that there is sufficient FCM involvement in the formation of pricing and risk policy – the key elements that FCMs fear monopoly Exchange owned CCPs could abuse through ownership of a 'cash cow'.

**In other words the Exchange owned CCPs should:**

- If this is not the real rationale, go out of their way to demonstrate that improvement of the Exchange top and bottom lines and market valuation is not at the forefront of their *modus operandi*
- Involve to the maximum extent the FCM community at the heart of their governance arrangements.