News From Thomas Murray IDS

Press Release

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Thomas Murray IDS advises global officials on central clearing house (CCP) disclosure standards

The Committee on Payment and Settlements Systems (CPSS) and the International Organisation of Securities Commissions (IOSCO), the joint CPSS-IOSCO body formed of the world's central banks and capital markets authorities, have been developing higher global standards for securities clearing and settlement post-2007. These have taken the form of Principles for Financial Markets Infrastructure, the "PFMIs," now adopted and implemented in a first stage in 28 countries. Thomas Murray IDS was involved in the first public consultations in 2011, and remains at the table in this field where its expertise as an independent analyst and advisor is well recognised. Since the release of the PFMIs, the firm has been working with capital market infrastructure entities on how they should evaluate the state of their institutions' compliance with these Principles.

In addition to these qualitative Principles set for all infrastructures involved in settlement, given the specificity of central clearing, which by its nature concentrates risk, CPSS-IOSCO have gone on to propose additional quantitative disclosures. Thomas Murray IDS commented on the first public draft late in 2013, and so was invited in London on 6 June for a final discussion with representatives of central banks and regulators from around the world.

Asset managers need to bear in mind that clearing banks have been raising questions about their potential liabilities in a risk/cost environment altered by the introduction of OTC contract clearing. It is less straightforward for them, and the questions they raise concern the risk management of the CCP itself as well as that of other clearing members. The difference is that five and more years ago, the assets being centrally cleared were overwhelmingly exchange-priced, and so relatively easy to value and assess margin. There is a greater realisation today that mutualisation of risk implies just that, and there is a heightened sense of dependency on the work of other clearing members at the table. The days of thinking that the clearing house would simply handle the work quietly are gone.

Further, the asset management community is starting to realise that with the heightened capital costs now required, it will be imperative to concentrate business on relatively standardised contracts that can be removed from their books and put onto those of the clearing house. But at the same time, how can they do this safely? Can their assets be frozen, even for a short period of time? Can their specific margin be identified and ported to another clearing bank, or indeed another CCP entirely, and over what period of time? Will their clearing bank be asking them for more capital to put up as margin, because OTC has a different pricing risk for the clearing house? Perhaps different forms of capital will be demanded as collateral becomes more scarce? In short there is no doubt that the asset management community is exposed to the new clearing environment.

CPSS-IOSCO confirmed that new quantitative standards will soon be announced for central counterparty clearing, to be phased in so that clearing houses can develop corresponding IT to meet these disclosure requirements. CPSS-IOSCO believe that additional disclosures in the area of stress testing, margin models and testing, liquidity management, and collateral investment policy will heighten market confidence, and that in a more transparent environment there will be a race to the top in terms of risk management, not a lowering of standards. It is recognised that CCPs by law and asset class remain very different institutions across the world, meaning that direct global comparisons across them are still a long way off. The same stress test will play out differently across jurisdictions in such circumstances, for example, and asset managers will have to accept the lack of direct comparison. For this reason, individual analyses of these infrastructures will remain the norm for the foreseeable future – and this segment of the financial system's nervous system will foreseeably retain the focus of regulators' attention.

Thomas Murray IDS supports this coordination by global authorities to assure greater transparency in these critical infrastructures.

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Notes to editors

About Thomas Murray IDS

Thomas Murray IDS was established in London in 1994. It helps its clients manage and monitor their relationships with service providers including global custody banks, depositaries and fund administrators. Thomas Murray IDS's clients include private and public sector pension schemes, insurance companies, sovereign wealth funds, investment managers, supranationals and foundations in Australasia, EMEA and North America.

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