



27 May 2024

FIA Response to B3 Clearing Consultation EC 015-2024-VNC on Recovery Plan and Early Settlement Auction

Submitted via email to consultapublicapr@b3.com.br.

FIA¹ and its members appreciate the opportunity to provide feedback on the proposed recovery plan outlined in your consultation document EC 015-2024-VNC. While we acknowledge and support the response letter from the Associação Brasileira de Bancos Internacionais (“ABBI”), we wanted to highlight further recommendations and comments to consider before implementing the proposed rule changes as per the consultation document. FIA and its members stand ready to continue collaborating with B3 on this topic and we remain at your disposition to discuss this letter.

Default Waterfall

CCPs around the globe have established standards, procedures and rules aligned with international guidelines and principles setting out a clear default management framework. Such framework typically includes procedures and governance that a CCP should follow when dealing with a defaulter’s portfolio. While the proposal effectively addresses risks further down the waterfall, i.e., during the recovery phase, formalizing the normal default management process is equally critical. The current rules do not comprehensively cover and address critical steps before the recovery phase to manage a defaulter’s portfolio. For instance, the current rules do not mention any existing auction provision i.e., what an auction is and how auctions are managed prior to activating the recovery plan.

We recommend incorporating these auction provisions as part of the standard business-as-usual (“BAU”) default management procedures into the rules i.e., prior to activating the recovery plan. These BAU procedures should consider any auction incentives, such as introducing voluntary and mandatory auction types with appropriate juniorisation rules. These provisions should be clear and transparent to clearing members and their clients.

¹ FIA is the leading global trade organization for the futures, options, and centrally cleared derivatives markets. FIA’s mission is to support open, transparent, and competitive markets; protect and enhance the integrity of the financial system; and promote high standards of professional conduct. FIA’s membership includes clearing firms, exchanges, clearinghouses, trading firms and commodities specialists from more than 48 countries, as well as technology vendors, lawyers and other professionals serving the industry.

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In addition, we also suggest clarifying further how these provisions integrate with the proposed recovery measures. They should, at a minimum, consider clarifying these aspects:

- Governance:
 - Define the role and responsibility of the Board.
 - Consider the establishment, composition and the role of a Default Management Group (“DMG”) and its responsibilities, such as assisting CCP staff on defaulter’s portfolio hedging and/or liquidation strategy.
 - Test regularly the auction responsibilities and mechanics with clearing members and their clients. B3 should consider the establishment and maintenance of a roster of liquidation broker i.e., a list of clearing participants ready to bid.
- Auction: Define the term auction and establish a clear procedure to manage auctions, including who can participate, the type of auction considered, relevant timing, what is considered as a successful auction and participants incentives.
- Transparency and preparedness: Participants should have a clear understanding of their obligations and risks and the CCP should ensure regular test of the auction process by the relevant participants.

Recovery plan process

The current proposal lacks details on the process around the activation of the recovery plan . Clear governance on the activation of the recovery plan should be documented, describing amongst others who will make the decision to activate the recovery plan and when regulators would be consulted. Adequate and efficient communication should also be considered once the recovery plan is activated to enable effective planning and response by Clearing Members and market participants at large. We suggest B3 reviewing its rules and procedures accordingly and disclose few practical scenarios covering different conditions and timelines to enable participants to better understand the recovery plan process and their involvement and obligations.

Final Auction Incentives

We acknowledge the proposed changes introduce a final auction in the recovery phase , but we would like to emphasize that this deviates from international guidance and practice. Auctions and/or voluntary allocations should be implemented as part of the BAU default management procedures and we recommend that the proposed auction should remain within the scope of such standard procedures and not covered in the recovery plan.

In addition, the proposal does not include incentives for participation in this auction, and rather defines it as a signal that compulsory early settlement (or tear-ups as we understand) will follow if the auction is unsuccessful. We believe that incentives are crucial to ensure active and effective participation, thereby increasing the likelihood of a successful outcome. In addition, we recommend that B3 should define what it considers an unsuccessful auction and how it will generally communicate efficiently outcomes of the auctions with the relevant participants.



Feedback and Collaboration

We appreciate B3's openness to feedback and willingness to collaborate with members and participants at large. We encourage the establishment of a dedicated working group to facilitate ongoing dialogue and collaborative development of the default management process and its recovery plan.

Additional points

- While we acknowledge the reduction of the assessment call from X11 to X8 in response to previous feedback, we are concerned that such a high assessment call cap could create additional liquidity pressures during a stressed market condition and is an outlier within the industry. We suggest that B3 reassesses that cap.
- To the extent clients may participate in auctions, such participation should involve approval by the clearing member of the client. We recommend including such a provision given the continuing guarantee a clearing member would provide to the client, and the existing credit appetite that may exist between the clearing member and the client.
- Finally the absence of provisions for Non-Default Losses in the current rules creates uncertainty and recommend B3 to review and update its rules to clarify the intent that members would not bear losses from non-default losses that are beyond their control.

We look forward to our continuing collaboration on this topic and remain at your disposition should you want to discuss further our response.

Respectfully submitted,

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