

VIA CFTC PORTAL

Mr Christopher Kirkpatrick
Commodity Futures Trading Commission
115 21st Street NW
Three Lafayette Centre
Washington DC 20581

24 January 2020

LCH Limited Self-Certification: Automatic Expiration of FX Option Contracts

Dear Mr Kirkpatrick

Pursuant to CFTC regulation §40.6(a), LCH Limited ("LCH"), a derivatives clearing organization registered with the Commodity Futures Trading Commission (the "CFTC"), is submitting for self-certification minor amendments to its rules regarding the automatic expiration of FX Option Contracts cleared via the ForexClear service. The changes do not apply to ForexClear Clearing Members that are Future Commission Merchants.

Part I: Explanation and Analysis

Under an FX Option Contract, the buyer has the right to exercise its option trade on a given expiry date into an underlying FX spot between itself and the seller. LCH, via its ForexClear service, facilitates the exercise, or otherwise the expiry, of the cleared FX Option Contracts following an instruction received by the Clearing Member that is the buyer.

Following Clearing Members' feedback, in order to facilitate the expiry of ForexClear Option Contracts, LCH is changing its rules to allow the automatic expiry of certain ForexClear Option Contracts that are deemed to be "equal and offsetting". The new functionality would be triggered if a relevant FX Option Contract has not been exercised by the end of the business day immediately preceding the given Expiration Date. ForexClear Clearing Members may opt out of such functionality by providing notice to LCH.

The rule changes will go live on, or after, 6 February, 2020.

Part II: Description of Rule Changes

The Procedures Section 2I (“ForexClear Clearing Service”) have been modified in section 1.17 (“Automatic Exercise of ForexClear Option Contracts”) to set out the new automatic expiry process and the types of FX Option Contracts that would be deemed “equal and opposite” and therefore eligible for such process. For example, where the buyer of one ForexClear Option Contract and the seller of the other ForexClear Option Contract is the same ForexClear Option Clearing Member, both ForexClear Option Contracts would be automatically expired.

Regulation 94 of the General Regulations (“Exercise of ForexClear Option Contracts”) includes a new paragraph noting the new automatic expiry process that will be followed in line with the Procedures noted above. ForexClear Clearing Members will need to notify LCH in order to opt out of the functionality, therefore, the new paragraph specifies that a ForexClear Option Contract subject to automatic expiry on a given Expiration Date will automatically expire and terminate notwithstanding the LCH’s receipt of an instruction to exercise such ForexClear Option Contract.

The text of the changes are attached hereto as:

- **Appendix I: General Regulations**
- **Appendix II: Procedures Section 2I**

Part III: Core Principle Compliance

LCH has reviewed the changes against the requirements of the Core Principles and finds it will continue to comply with all the requirements and standards therein.

Part IV: Public Information

LCH has posted a notice of pending certification with the CFTC and a copy of the submission on LCH’s website at: <http://www.lch.com/rules-regulations/proposed-rules-changes>

Part V: Opposing Views

There were no opposing views expressed to LCH by governing board or committee members, members of LCH or market participants that were not incorporated into the rule.

Certification

LCH hereby certifies to the Commodity Futures Trading Commission, pursuant to the procedures set forth in the Commission regulation § 40.6, that attached rule submission complies with the Commodity Exchange Act, as amended, and the regulations promulgated there under.

Should you have any questions please contact me at charlotte.woodwards@lch.com.

Yours sincerely



Charlotte Woodward

Senior Regulatory Advisor, Compliance,
LCH Limited

Appendix I
General Regulations



**GENERAL REGULATIONS OF
LCH LIMITED**

REGULATION 94 EXERCISE OF FOREXCLEAR OPTION CONTRACTS

- (a) Subject to (b) and (c) below, a ForexClear Option Buyer may exercise the right or rights granted to it pursuant to a ForexClear Option Contract only by giving an irrevocable notice in the manner and at the time specified by the Procedures.
- (b) Subject to (c) below, ~~if~~ a ForexClear Option Contract has not been exercised in the manner and by the time specified in the Procedures, then it will, subject to the satisfaction of any conditions set forth in the Procedures, be deemed exercised in the manner and at the time specified by the Procedures.
- (c) In the event (i) a ForexClear Option Contract (to the extent capable of exercise) has not been exercised by the end of the business day immediately preceding the relevant Expiration Date, (ii) the ForexClear Option Clearing Member party to each such ForexClear Option Contract has not opted out of the Clearing House’s “automatic expiry” service in accordance with the Procedures, and (iii) such ForexClear Option Contract is “equal and offsetting” with another ForexClear Option Contract, as determined by the Clearing House in accordance with the Procedures, the Clearing House shall automatically expire such ForexClear Option Contract at the start of the given Expiration Date. Upon the automatic expiry of a ForexClear Option Contract pursuant to this paragraph, such ForexClear Option Contract shall immediately terminate. For the avoidance of doubt, a ForexClear Option Contract subject to automatic expiry on a given Expiration Date shall automatically expire and terminate notwithstanding the Clearing House’s receipt of an instruction to exercise such ForexClear Option Contract on the Expiration Date.
- ~~(e)~~(d) -If a ForexClear Option Contract has not been (i) exercised, (ii) ~~or~~ deemed to have been exercised or (iii) automatically expired pursuant to this Regulation 94, the right or rights granted pursuant to that ForexClear Option Contract will immediately expire and become void and of no effect.
- ~~(d)~~(e) For the avoidance of doubt, a ForexClear Option Contract may be exercised (or deemed to be exercised) in partial or in whole.

Appendix II
Procedures Section 2I



LCH LIMITED

PROCEDURES SECTION 2I

FOREXCLEAR CLEARING SERVICE

compression run of the result of such compression procedure. A notification received after the relevant cut-off time shall be treated as if such notification was submitted on the following day.

- 1.15.4 Following the compression process described above and as further set out in Regulation 95, the applicable ForexClear Clearing Member shall promptly notify the Clearing House if it believes that any errors have occurred in the compression process or if its books and records do not reconcile with those of the Clearing House in respect of the compressed ForexClear Contracts as notified to the ForexClear Clearing Member by the Clearing House.

1.16 Exercise and Expiry Agent

- 1.16.1 ForexClear Clearing Members may facilitate or communicate the exercise of (or intent to exercise) ForexClear Option Contracts to the Clearing House via an exercise and expiry agent. The Clearing House may determine, in its sole discretion, the form and manner of any instruction pursuant to this Section 1.16.
- 1.16.2 In the event that an exercise and expiry agent is not able to facilitate or communicate the exercise of (or intent to exercise) a ForexClear Option Contract for any reason whatsoever, and the Clearing House becomes aware of such failure to facilitate or communicate, the Clearing House will notify the relevant ForexClear Clearing Members of such failure and may provide details of one or more alternative exercise methods.
- 1.16.3 Exercise and expiry agents may be designated by the Clearing House from time to time and such agents shall be published on the Clearing House's website.
- 1.16.4 Neither the Clearing House nor any other member of the LCH Group shall have any liability whatsoever to any ForexClear Clearing Member or any other person, including any Clearing Client, in contract, tort (including negligence), trust, as a fiduciary or under any other cause of action in respect of any liabilities, damages, losses, costs or expenses of whatsoever nature suffered or incurred by a ForexClear Clearing Member or any other person, including any Clearing Client, as a result of (a) any failure by the Clearing House to provide notice pursuant to Section 1.16.2 or (b) any failure of an exercise and expiry agent to communicate the exercise of (or intent to exercise) a ForexClear Option Contract to the Clearing House.

1.17 Automatic Exercise of ForexClear Option Contracts

- 1.17.1 Subject to Section 1.17.5, in relation to a ForexClear Option Contract, if, at the Expiration Time on the Expiration Date of that ForexClear Option Contract, the ForexClear Option Contract has not been exercised by the relevant ForexClear Clearing Member or the Clearing House, as the case may be, then it will be deemed exercised as of that time if the In-the-Money Amount of that ForexClear Option Contract at the Expiration Time equals (in the case of a Call) or exceeds (in the case of a Call or Put) the product of:

- (a) the number of basis points as published on the Clearing House's website from time to time as being applicable to the ForexClear Currency Pair referenced in that ForexClear Option Contract; and
 - (b) the Call Currency Amount or the Put Currency Amount, as appropriate, in each case as calculated at or immediately prior to the Expiration Time on the Expiration Date of the given ForexClear Option Contract.
- 1.17.2 For the purposes of Section 1.17.1, the Clearing House may change the number of basis point applicable to any ForexClear Currency Pair by giving three Business Days' prior notice to the ForexClear Option Clearing Members (or such shorter notice period as determined by the Clearing House following consultation with ForexClear Option Clearing Members).
- 1.17.3 Subject to Section [1.17.5], if the Clearing House receives an instruction from a ForexClear Clearing Member, including via any third party intent agent or middleware provider, before the applicable Expiration Time on the Expiration Date such instruction will in all circumstances be acted upon notwithstanding any administrative, systems or processing delays that may affect the Clearing House immediately taking the action required upon receipt of such instruction. If the Clearing House receives an instruction from a ForexClear Option Clearing Member at or after the applicable Expiration Time on the Expiration Date then Section 1.17.1 shall in all circumstances apply and the Clearing House shall have no regard to such instruction.
- 1.17.4 The "**In-the Money Amount**" in relation to a ForexClear Option Contract shall, in respect of the Exercise Date, be equal to:
- (a) in the case of a Call, the excess of the FX Spot Reference over the Strike Price, multiplied by the Call Currency Amount, where both the Strike Price and the Settlement Rate are quoted in terms of the amount of Put Currency to be paid per one unit of Call Currency; and
 - (b) in the case of a Put, the excess of the Strike Price over the FX Spot Reference, multiplied by the Put Currency Amount, where both the Strike Price and the Settlement Rate are quoted in terms of the amount of Call Currency to be paid per one unit of Put Currency.
- 1.17.5 In order to facilitate the expiry of offsetting ForexClear Option Contracts, the Clearing House will automatically expire ForexClear Option Contracts that are "equal and offsetting". ForexClear Clearing Members may opt out of such automatic expiry of their ForexClear Option Contracts by providing notice to the Clearing House (the form and manner of such notice shall be prescribed by the Clearing House from time to time), and such opt out shall become effective at such time as notified by the Clearing House to the given ForexClear Clearing Member.
- 1.17.6 Two ForexClear Option Contracts shall be deemed "equal and offsetting" to each other where:

- (a) the Buyer of one ForexClear Option Contract and the Seller of the other ForexClear Option Contract is the same ForexClear Option Clearing Member; and
- (b) the ForexClear Option Contracts have the equivalent or equal (1) Call Currency and Put Currency, (2) Call Currency Amount and Put Currency Amount, (3) Strike Price, (4) Expiration Date and (5) Settlement Date.

1.17.7 Except where a ForexClear Clearing Member has opted out of the automatic expiry of their ForexClear Option Contracts in accordance with Section 1.17.5, at the start of a given Expiration Date, the Clearing House shall automatically expire and therefore terminate all equal and offsetting pairs of ForexClear Option Contracts of each ForexClear Option Clearing Member.

1.17.8 In the event the Clearing House receives an instruction from a ForexClear Option Clearing Member, including via any third party exercise and expiry agent or middleware provider, with respect to any ForexClear Option Contract that is subject to automatic expiry on a given Expiration Date, the Clearing House shall disregard such instruction and in all circumstances such ForexClear Option Contract shall be expired on the given Expiration Date.

~~1.17.5~~1.17.9 Capitalised terms used in this Section 1.17 and not otherwise defined shall have the meanings specified for such terms in (i) the ForexClear Option Contract Terms applicable to that ForexClear Option Contract, and, if not defined therein, (ii) the 1998 FX and Currency Options Definitions (including Annex A thereto) as published by the International Swaps and Derivatives Association, Inc., the Emerging Markets Trade Association and The Foreign Exchange Committee.

1.18 CLS Payment Procedures

1.18.1 In connection with ForexClear Spot Contracts, ForexClear Deliverable Forward Contracts, ForexClear Option Contracts and ForexClear Swap Contracts, where applicable, FXCCMs are required to meet the following requirements with respect to CLS:

Time	Action or Requirement
00:00 CET	Clearing House to provide FXCCMs expected CLS funding requirements.
01:30 – 02:00 CET	Clearing House to provide FXCCMs final CLS funding requirements. FXCCMs required to make such payments by 08:00 CET.
06:00 – 08:00 CET	FXCCMs required to make payments to cover all short positions in all currencies.
08:00 CET	CLS to issue payments to FXCCMs per settlement instructions for each relevant FXCCM.

08:00 – 10:00 CET	Clearing House to initiate and complete liquidity provisions.
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~~1.1.1.1.18.1~~ 1.18.1 In connection with ForexClear Spot Contracts, ForexClear Deliverable Forward Contracts, ForexClear Option Contracts and ForexClear Swap Contracts, where applicable, the following Relevant FX Liabilities are payable to CLS by FXCCMs in accordance with the Procedures and/or instructions from the Clearing House:

- (a) Initial Exchange Amounts, Final Exchange Amounts and amounts owed under the Economic Terms of ForexClear Spot Contracts and ForexClear Deliverable Forward Contracts; and
 - (b) Premiums under ForexClear Option Contracts,
- 1.18.2 in each case net of any return of aggregate variation margin or NPV Payments denominated in the same currency and due on the same day.
- 1.18.3 Each ForexClear Option Clearing Member warrants that the Relevant FX Liabilities that are paid to CLS pursuant to Section 1.18.2 are transferred free from any proprietary, equitable or other similar interest of any person.
- 1.18.4 Each ForexClear Option Clearing Member shall at all times maintain complete and accurate written records of all Payment Transfer Orders given by it (or on its behalf) to its Member Settlement Bank(s) in respect of all amounts under all of the ForexClear Contracts (other than ForexClear NDF Contracts) registered in its name from time to time. Upon demand by the Clearing House, a ForexClear Option Clearing Member shall immediately provide all such records to the Clearing House.

1.19 Settlement Limits for ForexClear Option Clearing Members

- 1.19.1 Subject to the Regulations and Section 1.19.2, the Clearing House shall from time to time determine the (i) Settlement Position Limit and (ii) Settlement Exposure Limit in respect of each ForexClear Currency and each ForexClear Option Clearing Member.
- 1.19.2 A ForexClear Option Clearing Member may request, in such form and manner as the Clearing House prescribes from time to time, that the Clearing House set a Settlement Position Limit for a given ForexClear Currency below the limit determined pursuant to paragraph (a) above, provided that such requested limit meets the Clearing House's risk tolerance, as determined by the Clearing House in its sole discretion. Upon the Clearing House notifying the ForexClear Option Clearing Member that such requested limit is approved, including the time at which such limit shall take effect, such limit shall be considered the "Settlement Position Limit" for the given ForexClear Currency for the relevant ForexClear Option Clearing Member.
- 1.19.3 Notwithstanding the acceptance by the Clearing House of a revised Settlement Position Limit pursuant to Section 1.19.2, the Clearing House may increase or