

Via CFTC Portal

23 February 2023

Mr Christopher J. Kirkpatrick
Office of the Secretariat
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street NW
Washington, DC 20581

Re: Proposed amendments to LCH SA Liquidity Risk Model Framework:

Dear Mr. Kirkpatrick,

Pursuant to CFTC regulation §40.6(a), LCH SA ("**LCH SA**"), a derivatives clearing organization ("**DCO**") registered with the Commodity Futures Trading Commission (the "**CFTC**"), is submitting for self-certification the proposed amendments to its Liquidity Risk Modeling framework (the "**Proposed Rule Change**").

The Proposed Rule Change for its effectiveness is contingent upon LCH SA's receipt of all necessary regulatory approvals expected for early March 2023, however, in no event, will either be implemented earlier than 10 business days after the proposed changes are filed with the CFTC.

The text of the Proposed Rule Change is attached hereto as Appendix.

Part I: Explanation and Analysis

The purpose of the proposed fee changes is for LCH SA CDS Clear to update its Liquidity Risk Modeling framework (the "**Framework**"), which describes the framework by which the LCH SA Collateral and Liquidity Risk Management ("**CaLRM**") team assures that LCH SA has enough cash available to meet any financial obligations, both expected and unexpected, that may arise over the liquidation period for each of the clearing services that LCH SA offers. The Framework is part of LCH SA's Risk Management Procedures (the "**Procedures**") and it is consistent with LCH group liquidity risk policy to which LCH SA shall comply.

Part II: Description of Rule Changes

The Framework is one of several well-developed policies and procedures that LCH SA maintains to manage its liquidity risk, i.e., the risk that LCH SA will not have enough cash available, in extreme but plausible circumstances, to settle margin payments or delivery obligations when they become due, in particular upon the default of a clearing member. Such policies and procedures include, among others:

a) the Group Liquidity Risk Policy which ensures that each CCP of the LCH group has enough liquid resources on hand to meet all the expected and unexpected financial obligations that arise during the course of the day. The policy lays out how a CCP will measure whether there is enough available liquid resources;

b) the LCH SA Liquidity Plan that sets out the principles and procedures for liquidity management within LCH SA. Its main objectives are to:

- Ensure the liquidity adequacy of LCH SA at all times in accordance with policies set by the appropriate governance authority monitored and reported by Risk Management;
- Ensure that liquidity management and resources are aligned with LCH SA operational requirements to meet payment obligations as they fall due under Business as Usual and stressed liquidity conditions;
- Ensure effective liquidity risk identification and escalation within Collateral and Liquidity Management (“CaLM”) service and other relevant departments with LCH SA.

c) the Group Financial Resource Adequacy Plan which details the standards by which financial resources should be assessed against member exposures. This includes Variation Margins, Initial Margins, Margin Add-Ons for liquidity risk, concentration risk, wrong way risk where appropriate, as well as the sizing and re-sizing of the default funds across the LCH Group CCPs;

d) the Group Collateral Risk Policy; which sets out the standards for the management of collateral risk across the LCH Group CCPs and ensures that CCPs must have a robust mechanism in place to process and control the collateral posted by members;

e) the Group Investment Risk Policy which sets out the standards for the management of investment risk across the LCH Group CCPs;

f) the LCH SA Collateral Control Framework which describes the actions undertaken by the CaLRM team to implement the collateral limits laid out in the Group Collateral Risk Policy and to ensure that the prices integrated on a daily basis by margin team are accurate and fairly priced.

In brief, the Framework: (i) identifies LCH SA’s sources of liquidity and corresponding liquidity risks; (ii) identifies LCH SA’s liquidity requirements with respect to its members and its interoperable central counterparty (“CCP”); (iii) describes the metrics and limits that LCH SA monitors; and (iv) describes the scenarios under which these metrics are computed.

As specified in Appendix A, LCH SA is proposing to amend the Framework as follows.

(i) Default Fund reduction and intraday injection of liquidity in the settlement platform to be considered in operational target.

As per a recommendation from LCH SA’s independent risk model validation department, LCH SA is proposing to amend the Framework in order to address more accurately its liquidity requirements in the event of a Default Fund (“DF”) scheduled reduction or an extraordinary intraday liquidity injection in the settlement platform.

Before any DF change there exists a latency between the final approval of the new DF total amount and the settlement of the new contributions. To properly reflect the decrease of the DF in the calculation of the operational target until the settlement of the contributions the new proposed framework will include the following enhancements.

- The DF recomputed is compared to the DF actually paid and in the account of LCH SA.

- The amount that will reported will be the following.
 - o only global drain of liquidity will be considered and added to the operational target because they represent a scheduled liquidity outflow that needs to be covered by adequate liquidity resources by the CCP,
 - o Eventual negative amounts will be reported in the operational target for all the days from the beginning of the month till settlement date.

Moreover, according to the current internal fails monitoring operating mode, a threshold of 1 bln Euro is set to request a formal approval by the LCH SA Chief Risk Officer and the Head of LCH SA CaLM or their delegates, before allowing the LCH SA Operations team to inject extraordinary liquidity intraday in the settlement platform.

The current liquidity framework does not take into consideration eventual extraordinary liquidity injection in the settlement system in the calculation of the operational target. The revised liquidity framework, while maintaining consistency with the current procedure, will require a rerun of the operational target anytime a significant amount (bigger or equal than 1 bln Euro) of liquidity is injected intraday. Eventual intraday injection will be subtracted from the liquidity resources available that are compared against the operational target to ensure that LCH SA has adequate liquidity to satisfy the needs related to the operational management of the CCP

(ii) Committed credit line.

LCH SA is proposing clarifications to the Framework to reflect the final closure of one committed credit line that took place the December 15th 2021. The committee credit line has been replaced by a multi-currency overdraft facility of €10 million with an International bank. In addition, the CCP put in place a secured committed intraday credit line with Norges Bank to cover the non-Euro VM payments for the Euronext Oslo listed derivatives activity. The amount of the Norges bank credit line is flexible and is determined on a daily basis based on the collateral deposited with Euroclear Bank.

Finally, in accordance with what is defined in the SA liquidity Plan, it has been reported in the Framework the list of options that LCH SA has to address in a default situation any liquidity shortfall in a currency different from EUR. These are:

- The non EUR cash deposited as collateral
- The sale of the non EUR securities of the defaulting member
- Repo transactions
 - o Bilateral Repo transactions (Non Euro cash taker and Non Euro collateral giver)
 - o Cross-currency Bilateral Repo (Non Euro cash taker and Euro collateral giver)
 - o Cross-currency Triparty Repo (Non Euro cash taker and Euro collateral giver)
- The use of the multicurrency overdraft facility with an International Bank
- Use of the FX spot market transactions
- ECB weekly tender in USD (last resort). Given its banking status, LCH SA has access to the ECB Open market operations in USD.
- Replace LCH SA's liabilities in non EUR by EUR as per clearing rulebook

(iii) Updated figure of maximum limit of liquidity injected in the settlement system to ease settlement

In the section of the Framework that describes how the settlement of physical securities is made and how such activity impact the liquidity of the CCP, LCH SA is updating the maximum level of liquidity to be injected daily in the settlement system to ease settlement flow.

In particular, the CCP have defined for each Central Securities Depository (CSD) in which settlement takes place an amount of liquidity that is injected every day to ease the settlement flow and such liquidity consumption is monitored by Operation team during the settlement cycle that occurs throughout the day.

The updated figures have been defined as a function of the actual settlement activity observed by Operations team to optimize the management of the CCP liquidity.

Moreover, in the same section of the Framework, it is described the mechanism of auto-collateralization which is a feature of T2S that enables to obtain the liquidity necessary to the finalization of transactions by pledging the security underlying the transaction at the Central Bank to get cash. It has been clarified that LCH SA successfully managed to test the transfer to its 3G pool (central bank liquidity) of securities coming from settlement for Italy, Spain and Germany transactions.

Part III: Core Principle Compliance

LCH SA reviewed the introduction of the Proposed Rule Change against the requirements of the Commission's regulations and DCO Core Principles and has concluded that its compliance with all the requirements and standards therein and in particular with the following principle and Commission's regulations including, but not limited to § 39.11 would not be adversely affected by the proposed amendments.

DCO Core Principle B – Financial Resources. LCH SA has determined that the Proposed Rule Change is consistent with the DCOs requirements of CFTC Regulation 39.11 requiring a DCO to maintain financial resources sufficient to cover its exposures with a high degree of confidence and to enable it to perform its functions in compliance with the core principles set out in section 5b of the Act. A derivatives clearing organization shall identify and adequately manage its general business risks and hold sufficient liquid resources to cover potential business losses that are not related to clearing members' defaults, so that the derivatives clearing organization can continue to provide services as an ongoing concern. The proposed amendments will assist LCH SA in defining more accurately its liquidity requirements by assuring that LCH SA will maintain appropriate levels of liquidity. As described above, the proposed change in the operational target enhance the ability of LCH SA to manage its liquidity during the daily services it provides by properly anticipating potential scheduled needs (Default Fund reductions) as well as ensuring that the liquidity available is always sufficient to continue the clearing and settlement operations also in the event of extraordinary intraday liquidity injection in the settlement systems. As a result, LCH SA believes that the Proposed Rule Change is consistent with the requirements of Core Principle B and Commission Rule 39.11.

Part IV: Public Information

LCH SA has posted a notice of pending certifications with the CFTC and a copy of the submission on LCH's website at: <https://www.lch.com/resources/rulebooks/proposed-rule-changes>

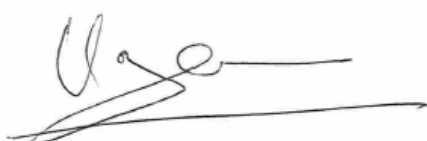
Part V: Opposing Views

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

Certification

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

Should you have any questions please contact me.

A handwritten signature in black ink, appearing to read 'Carole Uzan', with a long horizontal line extending to the right.

Carole Uzan

Chief Compliance Officer

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APPENDIX A

Proposed Rule Change to LCH SA Liquidity Risk Modelling Framework (V5.6) **(to be filed separately with the CFTC under Confidential Treatment request)**