

VIA CFTC Portal

March 7, 2019

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

Dear Mr Kirkpatrick

Non-deliverable swaps (ND IRS) denominated in Thai Baht (THB), Taiwanese Dollar (TWD), Brazilian Real (BRL), Chilean Peso (CLP) and Colombian Peso (COP)

Pursuant to CFTC regulation §39.5(b), LCH Limited (“LCH”), a derivatives clearing organization (“DCO”) registered with the Commodity Futures Trading Commission (the “CFTC”), is submitting Non-deliverable swaps (NDIRS) denominated in Thai Baht (THB), Taiwanese Dollar (TWD), Brazilian Real (BRL), Chilean Peso (CLP) and Colombian Peso (COP) for determination of whether mandatory clearing should apply.

Background

In April 2018, LCH launched clearing of non-deliverable swaps in three Asian currencies (Korean Won (KRW), Indian Rupee (INR) and Chinese Renminbi (CNY)). This proposed extension covers the liquid South American markets (Brazil, Chile, and Colombia) and the most liquid remaining markets in Asia (Thailand, Taiwan). SwapClear will settle all flow related to these products (whether notional, interest, fees and variation margin) in USD. The transformation from currency to USD is derived from the prevailing FX rate. The maximum maturity (based on existing liquidity) is 11 years for THB, TWD and BRL, and 15.5 years for CLP and COP. As part of this proposal, LCH also intends to increase the maximum clearing eligibility on KRW NDIRS to 15.5y (the current maximum tenor is 11y). KRW is the most actively traded NDIRS market and members have provided feedback that there is liquidity and demand for clearing beyond the current maximum.

Factors for determination

The existence of significant outstanding notional exposures, trading liquidity, and adequate pricing data

Based on the statistics of the latest Triennial Survey of the Bank for International Settlements¹, the daily average turnover in the five new ND IRS currencies represents c.2% of that in USD denominated OTC interest

¹ <https://www.bis.org/publ/rpfx16.htm>

rate swaps in the overall market. All market data is from existing sources i.e. Bloomberg and Reuters using the most liquid (industry standard) instruments at each tenor point.

The availability of rule framework, capacity, operational expertise and resources, and credit support infrastructure to clear the contract on terms that are consistent with the material terms and trading conventions on which the contract is then traded

LCH has a well-developed rule framework and support infrastructure for clearing interest rates swaps. LCH intends to leverage this existing operational capability when extending its offering to new ND IRS currencies.

In order to prepare for the launch of this product, LCH will perform testing to ensure that it is able to clear these products in a manner which is consistent with the terms on which they are traded.

Further to this, LCH have notified its Clearing Members of a number of minor changes to the procedure documents, which will be made in order to support the clearing of ND IRS in the above mentioned currencies. The changes have been submitted for self certification to the CFTC and are available on the LCH website.

The effect on mitigation of systemic risk, taking into account the size of the market for such contract and the resources of the DCO available to clear the contract

The NDIRS product does not introduce any novel risks to LCH, as the operational capability to manage the product is already in place.

LCH expects current SwapClear Clearing Members to start clearing these new NDIRS, once the service is live.

Based on the statistics of the latest Triennial Survey of the Bank for International Settlements, the daily average turnover in the five new ND IRS currencies represents c.2% of that in USD denominated OTC interest rate swaps in the overall market. Therefore, the introduction of ND IRS eligibility is unlikely to have a significant impact on the risk profile or total resources held by the SwapClear service. As such, the systemic risk profile of LCH remains unchanged as a result of the new product offering.

The effect on competition, including appropriate fees and charges applied to clearing

CME Clearing, Singapore Exchange Derivatives Clearing (SGX-DC) and OTC Clearing Hong Kong Limited (OTC Clear) currently offer clearing services for ND IRS in all or a subset of currencies that LCH plans to clear (as well as other emerging markets' currencies) and at similar tenors.

Following the launch, scheduled for March 11th 2019, ND IRS in BRL, CLP and COP will be the subject of a fee holiday until 1st October 2019 after which a fee plan specific to this product will be applied. The fees will differ according to the tariff chosen by Members and may consist of an annual charge

or a charge per trade. Members will also be charged for fees related to the client clearing of ND IRS. Clearing Members will be notified of the fee plan ahead of the product's launch.

The existence of reasonable legal certainty in the event of the insolvency of the relevant DCO or one or more of its clearing members with regard to the treatment of customer and swap counterparty positions, funds and property

The level of legal certainty around the clearing of NDIRS contracts is in all material respects the same as that of the products already cleared in the SwapClear service at LCH.

Insofar as legal certainty in the event of the insolvency of the DCO is concerned, LCH would be wound up under English law.

Further information §39.5(b)(iii-viii)

Product terms for ND IRS are market standard and follow **2006 ISDA Definitions** and the **1998 FX and currency option ISDA Definitions**. ND IRS are also part of the Financial products Markup Language (FpML) standard (specifically <http://www.fpml.org/coding-scheme/floating-rate-index> published on 21st December 2017), which is a protocol for sharing information on derivatives and other products. The participant eligibility standards for ND IRS are the same as those for existing SwapClear Clearing Members.

As noted above, all market data is from existing sources i.e. Bloomberg and Reuters using the most liquid (industry standard) instruments at each tenor point.

No material revisions to the existing risk models/parameters and/or liquidity management framework are required for LCH to offer the clearing of the product; however the following adjustments have been made:

- **Stress Testing Methodology**: New historical scenarios will be added and existing historical scenarios will be extended. Further, the existing FX-inspired scenarios will be extended and new ones will be added. The interest rate parity scenarios are also added where applicable. The theoretical scenarios are updated using the same methodology as Phase I in order to accommodate the new currencies.
- **Additional Margins**: Basis risk and liquidity add-ons will be applied consistent with existing swaps. For BRL an additional charge will apply to capture the on-shore/off-shore basis risk. Sovereign risk add-on (as used in SwapClear for NDIRS Phase I) will be applied to the new proposed currencies.
- **Default Management Approach**: LCH will add a new representative for Latin American ND IRS. No changes are proposed for the Asia Pacific currencies.

LCH will make a number of minor changes to its Rulebook to enable clearing of ND IRS in THB, TWD, KRW, BRL, CLP and COP in the following sections:

- FCM Product Specific Contract Terms and Eligibility Criteria Manual
- Product Specific Contract Terms and Eligibility Criteria Manual
- FCM Procedures
- Procedures Section 2C

The rule changes have been submitted to the CFTC pursuant to §40.6(a), following consultation with LCH Clearing Members.

LCH engages its Clearing Members in the design and testing of new products at an early stage, through regular meetings and working groups. Clearing Members have been formally notified of the changes which LCH is required to make to its Rulebook.

Notice of this submission under CFTC regulation §39.5(b) was given to SwapClear Clearing Members on February 18, 2019 and a copy of this notice is provided at Appendix A. Furthermore, this submission is publicly available at: <http://www.lch.com/rules-regulations/regulatory-responses>

LCH intends to launch these products with its Clearing Members and clients no earlier than March 11, 2019.

Should you have questions please contact me at julian.oliver@lch.com.

Yours sincerely



Julian Oliver
Chief Compliance Officer
LCH Limited

Appendix A

Notice of this submission provided to SwapClear Clearing Members

Memo

| | |
|---------|---|
| To | SwapClear Clearing Members |
| From | David Horner, Head of In-Business Risk Rates |
| Date | 18 February 2019 |
| Subject | ND IRS (THB;TWD;BRL;CLP;COP) submission for determination of clearing requirements |

Pursuant to CFTC regulation §39.5(b), LCH Limited (LCH), a derivatives clearing organization (DCO) registered with the Commodity Futures Trading Commission (the CFTC), is submitting Non-deliverable swaps (ND IRS) denominated in Thai Baht (THB), Taiwanese Dollar (TWD), Brazilian Real (BRL), Chilean Peso (CLP) and Colombian Peso (COP) for determination of whether mandatory clearing should apply.

As per CFTC regulation §39.5(b)(viii), LCH is required to notify members of its submission. This note does not constitute a notification that the products are live for clearing. A notice announcing the live date and arrangements for the formal product launch will be published separately.

NDIRS contracts require counterparties swapping fixed interest payments for floating rate payments on the same underlying notional principal, on fixed dates over the life of the contract, with the net cash settled in USD.

In April 2018, LCH launched clearing of non-deliverable swaps in three Asian currencies (Korean Won (KRW), Indian Rupee (INR) and Chinese Renminbi (CNY)). This proposed extension covers the liquid South American markets (Brazil, Chile, and Colombia) and the most liquid remaining markets in Asia (Thailand, Taiwan). SwapClear will settle all flow related to these products (whether notional, interest, fees and variation margin) in USD. The transformation from currency to USD is derived from the prevailing FX rate. The maximum maturity (based on existing liquidity) is 11 years for THB, TWD and BRL, and 15.5 years for CLP and COP. As part of this proposal, LCH also intends to increase the maximum clearing eligibility on KRW NDIRS to 15.5y (the current maximum tenor is 11y). KRW is the most actively traded NDIRS market and members have provided feedback that there is liquidity and demand for clearing beyond the current maximum.

Factors for determination

The existence of significant outstanding notional exposures, trading liquidity, and adequate pricing data

Based on the statistics of the latest Triennial Survey of the Bank for International Settlements², the daily average turnover in the five new ND IRS currencies represents c.2% of that in USD denominated OTC interest rate swaps in the overall market. All market data is from existing sources i.e. Bloomberg and Reuters using the most liquid (industry standard) instruments at each tenor point.

The availability of rule framework, capacity, operational expertise and resources, and credit support infrastructure to clear the contract on terms that are consistent with the material terms and trading conventions on which the contract is then traded

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LCH has a well-developed rule framework and support infrastructure for clearing interest rates swaps. LCH intends to leverage this existing operational capability when extending its offering to new ND IRS currencies. In order to prepare for the launch of this product, LCH will perform testing to ensure that it is able to clear these products in a manner which is consistent with the terms on which they are traded.

Further to this, LCH will notify its Clearing Members of a number of minor changes to the procedure documents, which will be made in order to support the clearing of ND IRS in the above mentioned currencies. The changes will be certified with the CFTC and be made available on the LCH website.

The effect on mitigation of systemic risk, taking into account the size of the market for such contract and the resources of the DCO available to clear the contract

The new ND IRS currencies does not introduce any novel risks to LCH, as the operational capability to manage the product is already in place.

LCH expects current SwapClear Clearing Members to start clearing ND IRS, once the service is live. Based on the statistics of the latest Triennial Survey of the Bank for International Settlements³, the daily average turnover in the five new ND IRS currencies represents c.2% of that in USD denominated OTC interest rate swaps in the overall market. Therefore, the introduction of ND IRS eligibility is unlikely to have a significant impact on the risk profile or total resources held by the SwapClear service. As such, the systemic risk profile of LCH remains unchanged as a result of the new product offering.

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The existence of reasonable legal certainty in the event of the insolvency of the relevant DCO or one or more of its clearing members with regard to the treatment of customer and swap counterparty positions, funds and property

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LCH engages its Clearing Members in the design and testing of new products at an early stage, through regular meetings and working groups. Clearing Members have been formally notified of the changes which LCH is required to make to its Rulebook.

Further information will form part of the full §39.5 filing which will be publicly available on the LCH website. LCH looks forward to working with Clearing Members and the CFTC in the determination of clearing requirements. Please do not hesitate to contact me regarding any questions raised by this information.