

VIA CFTC PORTAL

5 July 2019

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

LCH Limited Self-Certification: Rates Service Default Fund Cap Increase

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 changes to its rules related to:

1. Increase the cap of the Rates Services Default Fund from £5bn to £6bn; and
2. Increase the minimum "Tolerance Contribution Amount" (TCA) per member from £3mn to £4mn

Part I: Explanation and Analysis

Rates Service Default fund

LCH is planning to increase the Rates Service default fund cap from £5bn to £6bn. The updated cap is expected to apply from the September fund re-sizing. This means that any changes to individual Default Fund contributions resulting from the change in the cap amount will be effective at close of business on 5 September 2019.

The increase to the cap is required to enable participation in the Rates service to continue to grow, while preserving a fair balance of resources between Initial Margins, the Default Fund and Default Fund Additional Margins.

The current cap has been in place for approximately 6 years, during which time the number of participants and the overall size of positions in the Rates service have both increased significantly. The size and scale of the service is now several times larger than when the cap was established.

Tolerance Contribution Amount

Given the growth in membership, service size and trade activity the Rates service also proposes increasing the proportion of the default fund allocated to facilitate trade registration. As part of this the minimum TCA per member is set to increase from £3mn to £4mn (the maximum aggregate tolerance is also increasing from £400mn to £600mn but LCH does not specify this in the Rulebook). This change should support larger business volumes, especially at or around the opening of the

service. This is especially important as the SwapClear service moves to an earlier opening time (which is planned to take place around the same time as this change).

The rulebook will be updated to reflect these changes and will go live on, or after, 30 August 2019.

Part II: Description of Rule Changes

Section CS1 of Schedule 6 (Rates Service Default Fund Supplement) of the LCH Ltd Default Rules has been updated to highlight that the Cap on the Rates Default Fund is now £6bn. Section S1 of the Rates Service Default Fund Supplement – SwapClear has been updated to highlight that the minimum TCA member contribution is £4mn.

The texts of the rule changes are attached hereto as:

- i. **Appendix I, LCH Limited Default Rules**

Part III: Core Principle Compliance

LCH reviewed the changes against the requirements of the Core Principles and found 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 changes.

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 julian.oliver@lch.com.

Yours sincerely



Julian Oliver
Chief Compliance Officer
LCH Limited

Appendix I
LCH Limited Default Rules

LCH The Markets'
Partner

**LCH LIMITED
DEFAULT RULES**

SCHEDULE 6
RATES SERVICE DEFAULT FUND SUPPLEMENT

CS1. Rates Service Fund Amount

- (a) The Rates Service Default Fund is denominated in GBP, and all amounts referable to it shall be denominated, calculated, called and payable in GBP.
- (b) On each business day, the Clearing House will determine a "**Combined Loss Value**" in respect of each of the 60 preceding business days. The Combined Loss Value for a particular business day will be the sum of: (1) the largest and the second largest daily stress-testing losses incurred during the preceding 60 business days in relation to the SwapClear Contracts and Eligible Listed Interest Rates Contracts of a Rates Service Clearing Member (the "**Combined Loss Value – Limb (1)**"); plus (2) the largest and the second largest daily stress-testing losses incurred during the preceding 60 business days in relation to the Non-Eligible Listed Interest Rates Contracts of a Rates Service Clearing Member (the "**Combined Loss Value – Limb (2)**"), in respect of a given scenario.
- (c) The "**Rates Service Fund Amount**" shall be determined by the Clearing House at the close of business on the first business day of each calendar month, and otherwise in accordance with paragraph (d) below (each a "**Rates Service Determination Date**") and shall be the sum of: (1) the largest of the 60 Combined Loss Values determined under Rule CS1(b); plus (2) an amount equal to 10 per cent of the value referred to in (1); plus (3) the SwapClear Tolerance Amount. The Rates Service Fund Amount shall not be less than £1 billion pounds (the "**Rates Service Fund Floor**") and shall not be more than ~~£65~~ billion pounds.
- (d) The Clearing House may recalculate the Rates Service Fund Amount on any business day if the largest of the 60 Combined Loss Values determined under paragraph (b) above on that day differs by more than 25 per cent. from the Combined Loss Value on which the previous Rates Service Contribution determination was based and, on such business day, the Clearing House shall be entitled to require those Clearing Members whose portfolios have caused the increase in the Combined Loss Value to pay an additional amount in respect of their Contributions.

CS2. Rates Service Fund Amount – Allocation

On each Rates Service Determination Date the Clearing House shall calculate:

- (a) The "**SwapClear Tolerance Amount**" which shall be the value of that portion of the Rates Service Fund Amount which relates to those default fund resources which the Clearing House determines as being required in relation to SwapClear Tolerance.
- (b) The "**Non-Tolerance Amount**" which shall be the sum of: (1) the Combined Loss Value – Limb (1); plus (2) an amount equal to 10 per cent of the Combined Loss Value – Limb (1).

PART A

RATES SERVICE DEFAULT FUND SUPPLEMENT – SWAPCLEAR

S1. SwapClear Contributions to the Rates Service Fund

Each SCM's SwapClear Contribution (other than any SwapClear Unfunded Contribution or any Supplementary Contribution) shall be determined by the Clearing House in accordance with the following provisions:

- (a) determinations will be made by the Clearing House at the close of business on the first business day of each month, and otherwise in accordance with paragraph (n) below (each a "**SwapClear Determination Date**") on the basis of information available as at close of business on the immediately preceding business day and notified to such Member as soon as practicable after such determination in accordance with the Procedures. In addition, the amount payable in respect of the SwapClear Contribution of an SCM which is a New Member will be determined on the date that the relevant New Member joins the SwapClear Service. Notwithstanding the foregoing, following a Default, any determinations on a SwapClear Determination Date and any such SwapClear Determination Date which might otherwise have occurred under this Rule S1 shall be suspended for the duration of the period (the "SwapClear Default Period") commencing on the date of such Default and terminating on the later to occur of the following dates:
 - (i) the date which is the close of business on the day falling 30 calendar days after the Rates Service Default Management Process Completion Date in relation to such Default (or, if such day is not a business day, the next succeeding business day); and
 - (ii) where, prior to the end of the period referred to in sub-paragraph (i) above (or such period as has already been extended pursuant to this sub-paragraph (ii)) one or more subsequent Defaults (each a "**Relevant Default**") occur, the date which is the close of business on the day falling 30 calendar days after the Rates Service Default Management Process Completion Date in relation to a Relevant Default which falls latest in time (or, if such day is not a business day, the next succeeding business day).
- (b) the "**SwapClear Tolerance Weight**" of an SCM (other than an SCM which is a New Member) shall be calculated by dividing (x) the average SwapClear Tolerance Utilisation of the relevant SCM during the 20 business day period preceding the relevant SwapClear Determination Date in respect of all SwapClear Contracts to which such SCM is a party, which average shall be calculated by adding together the peak SwapClear Tolerance Utilisation of such SCM for each relevant business day and then dividing such sum by 20, provided that for SCMs where the peak SwapClear Tolerance Utilisation does not yet exist or is otherwise unavailable in respect of a business day the Clearing House shall estimate the relevant peak SwapClear Tolerance Utilisation by reference to the actual or expected level of clearing activity of the relevant SCM in relation to SwapClear Contracts; by (y) the total of such

average SwapClear Tolerance Utilisations of all Non-Defaulting SCMs other than SCMs which are New Members;

- (c) the value of the "**SwapClear Tolerance Contribution Amount**" of: (x) an SCM (other than an SCM which is a New Member) shall be calculated by multiplying the SwapClear Tolerance Amount by the SCM's SwapClear Tolerance Weight, provided that (i) where that calculation results in a value which is less than or equal to ~~£3-4~~ million pounds, or in the case of a New Member, the value of the relevant SCM's SwapClear Tolerance Contribution Amount shall be ~~£3-4~~ million pounds; and (ii) where that calculation results in a value which is greater than or equal to £30 million pounds, the value of the relevant SCM's SwapClear Tolerance Contribution Amount shall be £30 million pounds; and (y) a New Member shall be ~~£3-4~~ million pounds PROVIDED FURTHER that where, as a result of the adjustments in individual SCM SwapClear Tolerance Contribution Amounts as described in this paragraph, the aggregate of the SwapClear Tolerance Contribution Amounts is greater or less than the SwapClear Tolerance Amount the Clearing House will adjust SCMs individual SwapClear Tolerance Contribution Amounts such that the aggregate of the SwapClear Tolerance Contributions equals the SwapClear Tolerance Amount;
- (d) the "**SwapClear Non-Tolerance Amount**" shall be the value of that portion of the Rates Service Fund Amount – SwapClear after deducting the SwapClear Tolerance Amount;
- (e) the value of the "**SwapClear Non-Tolerance Contribution Amount**" for a given SCM (other than an SCM that is a New Member) shall be calculated by multiplying the SwapClear Non-Tolerance Amount by the SCM's SwapClear Non-Tolerance Weight;
- (f) the "**SwapClear Non-Tolerance Weight**" of an SCM shall be calculated by dividing (i) the Uncovered Stress Loss associated with such SCM's SwapClear Contracts by (ii) the total Uncovered Stress Loss applied to all Non-Defaulting SCMs with respect to their SwapClear Contracts, in each case where the SwapClear Contracts are (A) entered into on the SCM's own behalf or with respect to a SwapClear Clearing Client or an FCM Client and (B) open and outstanding during the 20 business day period preceding the relevant SwapClear Determination Date. An SCM's "**Uncovered Stress Loss,**" as determined in accordance with the foregoing, shall be determined by the Clearing House (and notified to each SCM) from time to time by, *inter alia*, deducting the amount of eligible margin held by the Clearing House with respect to the relevant SwapClear Contracts from the stress loss associated with such SwapClear Contracts, **provided** that the Clearing House may, in determining the Uncovered Stress Loss of an SCM, take into account, *inter alia*, the number of alternative SwapClear Clearing Members that clear SwapClear Contracts with respect to that SCM's SwapClear Clearing Clients or FCM Clients. The provisions of this sub-paragraph (f) shall not apply to New Members and, for the avoidance of doubt, New Members shall not constitute Non-Defaulting SCMs for the purposes of limb (ii) of this sub-paragraph;