

## Stephen Morris Talks With *Risk.net* on CFTC Clearing House Recovery Rules

September 27, 2023

*Risk.net* spoke with Financial Markets and Funds partner Stephen Morris regarding the Commodity Futures Trading Commission's (CFTC) recently proposed rule concerning recovery and orderly wind-down plans for derivatives clearing organizations. While some executives in the clearing industry have suggested that adequate margin models are a better solution, Stephen calls attention to the consequences when margin models are inadequate. Using the London Metal Exchange (LME) crisis in March 2022 as an example, he states: "[LME] knew for certain that at least some of those clearing members were going to default if they made those margin calls, [because] some of the clearing members are fairly thinly capitalized. So the only thing the LME can do is cancel the day's trades." As the question of whether the LME had the power to cancel trades is being decided in court, Stephen "strongly suspects" the clearing house will be vindicated.

Asked whether the CFTC has the authority under the Commodity Exchange Act to go further than what has been proposed and to require clearing organizations to commit their own capital against default risk (often referred to as "skin in the game"), Stephen notes that under the Commodity Exchange Act, the CFTC has the power to promulgate such rules and regulations as, in its judgment, "are reasonably necessary to effectuate any of the provisions" of that Act. Moreover the Act requires derivatives clearing organizations to have "adequate financial, operational, and managerial resources, as determined by the CFTC."

"Under those statutory standards and with that statutory authority," says Stephen, it would be questionable to argue the CFTC "does not have a leg to stand on were it to promulgate a skin in the game regulation".

["CFTC's clearing house recovery rule splits industry,"](#) *Risk.net*, September 25, 2023

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