

Via CFTC Portal

25 June 2020

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

Re: Proposed LCH SA CDSClear initiative – Clearing of iTraxx MSCI ESG Screened Europe index contracts

Dear Mr. Kirkpatrick,

Pursuant to CFTC regulation §40.6(a), LCH SA, a derivatives clearing organization (“**DCO**”) registered with the Commodity Futures Trading Commission (the “**CFTC**”), is submitting for self-certification the amendments to the Reference Guide: CDS Margin Framework (the “**Rules**”) in order (i) to make conforming and clarifying changes to allow the clearing of iTraxx MSCI ESG Screened Europe index contracts and (ii) make a number of minor clarifications and enhancements to some aspects of the CDSClear risk framework and service.

The intended date of implementation is July 20, 2020, subject to any relevant regulatory review or approval process duly completed and in no event, the changes will be implemented earlier than ten (10) business days after the formal filing with the CFTC.

The submission changes made to the Rules are attached hereto as Appendix¹.

Part I: Explanation and Analysis

LCH SA is proposing to amend its Reference Guide: CDS Margin Framework in order to introduce clearing of the iTraxx MSCI ESG Screened Europe index CDS transactions.

Markit launched the iTraxx MSCI ESG Screened Europe Index (“**iTraxx ESG Index**”) on March 20, 2020.

This index is a subset of the iTraxx Europe Main index. The constituents of the iTraxx MSCI ESG Screened Europe index must meet various Corporate Responsibility Criteria. The first series that launched on March 20, 2020 (Series 33) has 81 constituents; all are constituents of the iTraxx Europe Main index Series 33.

¹ All capitalized terms not defined herein have the same definition as the Rule Book, Supplement or Procedures, as applicable.

Part II: Description of Rule changes

In order to permit participants to submit for clearing **iTraxx ESG Index** contracts, LCH SA needs to modify its Reference Guide: CDS Margin Framework.

In this regard, LCH SA has made the following changes:

- (i) removing references to specific indices in the document and replacing them with a generic reference to an index in sections 2.3.3, and 3.8.1.3,
- (ii) removing the fixed 24% value and changing the spread shock formula for it to be applicable more generically to both iTraxx Main index and any of its sub index including financial Single Names.

Clearing of the new **iTraxx ESG Index** contracts will not require any other changes to LCH SA CDS Clearing Rule Book or risk management framework or other policies and procedures constituting rules within the meaning of the CFTC Regulations.

LCH SA is also taking this opportunity to make the following changes which are unrelated to the clearing of iTraxx MSCI ESG Screened Europe index contracts:

- (i) removing the list of Dealers in section 2.3.3 as LCH SA may contact a broader list of Dealers than that currently listed in this section;
- (ii) correction of the worst 5 day P&L value per date and the worst P&L value aggregated per date formulae in section 3.5.6. to reflect the fact that the same date is selected to calculate the portfolio P&L for all contracts in the portfolio;
- (iii) the 9M curve has been removed from the Interest Rate Risk Margin calculation in section 3.6, reflecting the change of interest rate curve imposed by ISDA within the framework of the risk-free rate benchmark review;
- (iv) the Wrong Way Risk formulae in section 3.8.1 were incomplete, the second value "0" to be used to derive the maximum resulting from these formulae has been added;

At the request of LCH SA Risk Model Validation team so that the Reference Guide: CDS Margin Framework can be better assessed, LCH SA is making the relevant clarifications specified under the below subsections (v) to (ix),

- (v) adding a note in section 3.8.1.2 that clarifies that the recovery rate for Senior Unsecured Debt / Foreign Debt for Sovereigns (SNRFOR) and Senior Loss Absorbing Capacity (SNRLAC) seniorities are considered as if they were two different instruments;
- (vi) adding a note in section 3.8.2 to explicit the calibration of the shocks displayed in the table;
- (vii) adding a note in section 4.1.3.1 to describe the parameters used in the formula;

- (viii) the Average Liquidity Score formula has been amended and a note inserted in order to clarify which days are used to compute the Average Liquidity Score;
- (ix) the net notional for the index basis product p , tenor t used in the formula for the sum of the 5Y equivalent notional has been amended to an absolute value;
- (x) in view of the upcoming supervisory/regulatory transition from the Euro Overnight Index Average (EONIA) to the new Euro Short-Term Rate (ESTER or €STR) and the Fed Funds to the Secured Overnight Financing Rate (SOFR), references to the interest rate applied to the Price Alignment Interest in section 5.2 have been removed;
- (xi) the name of the Excess Margin per Legal Entity in section 6.2 has been changed to Legal Entity Identifier Margin in order to align this margin name with the member reports.

Part III: Core Principle Compliance

LCH SA will continue to comply with all Core Principles following the introduction of this change and has concluded that its compliance with the Core Principles would not be adversely affected by this change.

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/rules-and-regulations/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 rules.

Certification

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

Should you have any questions please contact me at: françois.faure@lch.com

A handwritten signature in blue ink, appearing to read 'Faure', with a long horizontal stroke underneath.

Francois Faure
Chief Compliance Officer
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APPENDIX

- LCH SA Reference Guide: CDS Margin Framework **(to be filed separately with the CFTC under Confidential Treatment request)**