FIA Board Member, Ed Pla, speaks at CFTC's MRAC meeting

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Opening Statement of Ed Pla, Global Co-Head of Clearing and Execution for UBS, to the Market Risk Advisory Committee of the Commodity Futures Trading Commission

January 31, 2018, Washington DC - Thank you, Commissioner Behnam, Chairman Giancarlo and Commissioner Quintenz for featuring this important topic in today's meeting of the Market Risk Advisory Committee. My name is Ed Pla and I am Global Co-Head of Execution and Clearing for UBS. Today I speak on behalf of the FCM clearing member community of FIA. Today's agenda explores the manner in which new and novel products are self-certified for listing by exchanges. The recent self-certification of bitcoin futures contracts in December has given this committee a prime example to discuss and consider.

FIA strongly supports the self-certification process as enacted in the Commodity Futures Modernization Act as well as the goals of responsible innovation and fair competition as set out in the CFTC's mission. With that responsible innovation in mind, self-certification provides exchanges with an important tool to come to market with new products after certifying that they have fulfilled their statutory responsibility as set out in the core principles of the Act and CFTC regulations. These core principles require exchanges to attest that important safeguards and requirements are in place before the launch of a product to ensure these contracts are indeed furthering "responsible innovation" and not endangering the marketplace. While Congress provided exchanges with the extraordinary power to self-certify their products, this self-policing authority comes with reciprocal responsibilities that exchanges act in the best interests of the marketplace.

Today I am representing the members of the clearing member community that play a pivotal role in the clearing of these products and the reduction of systemic risk in the markets. By margining and guaranteeing customer trades, contributing to the guarantee funds of clearinghouses and committing to assessment obligations during clearinghouse shortfalls, clearing members are the foundation of the clearing system.

One of the primary benefits of clearing is its socialization of risk through the clearing member default fund. This mutualization of risk protects the integrity of the financial system from contagion but also requires clearinghouses and their clearing members to have strict requirements around the creditworthiness of market participants and the risk management of the products that are cleared. This is due to the fact that clearing members are exposed to the risk of all market participants during a default, no matter whether a specific FCM is clearing the product or not. Clearing members cannot

firewall themselves away from the risk of others in the clearing system. The sharing of fellow customer risk is a basic tenet of clearing that helps disperse risk.

With several exchanges announcing last fall that they would launch bitcoin products, there were various opinions within this industry about the riskiness of these products and how to properly manage this exposure. These were by no means standard product announcements. Even the CFTC and NFA issued public statements regarding the potential volatility of the underlying cryptocurrency products.

The FCM community believes that the launch of these new exchange-traded derivatives in cryptocurrencies would have benefited from more two-way dialogue among regulators, exchanges, clearinghouses and the clearing firms who will be absorbing the risk of these instruments during a default.

Unfortunately, the self-certification process is constrained in allowing for market input and in this instance, there was only minimal and informal discussions with clearing members, depriving the process of critical information on certain key questions, such as:

- Whether a separate guarantee fund for these products was appropriate or whether exchanges put additional capital in front of the clearing member guarantee fund;
- Whether the underlying cash markets are adequately regulated and liquid to support the settlement process for these contracts; and
- Whether these products were properly margined.

FIA applauds Chairman Giancarlo's announcement two weeks ago to improve the self-certification process by requiring exchanges to show that the industry was properly consulted before the launch of such cryptocurrency products. Specifically, exchanges will now be asked to disclose to the CFTC what steps they have taken in their capacity as self-regulatory organizations to gather and accommodate appropriate input from concerned parties, including trading firms and FCMs.

This must be more than a "check the box" exercise and allow for a healthy and rigorous dialogue with market participants. Similar to the process for exchange rules, exchanges and CCPs should be required to include in the self-certification submission the comments received by the industry and how they were addressed. This would add accountability to the self-certification process and provide the CFTC with assurances that the core principles are being met.

We also believe that cryptocurrencies are not the only novel product class that may benefit from further marketplace engagement. We should not artificially limit this discussion to the topic du jour of bitcoin. We believe that clearing members and other market participants should be consulted with any novel product that poses unique risk challenges to the markets and regulators.

It is quite possible that—had these enhancements been in place and the industry was properly consulted—we would have ended up in the same place. However, this added transparency and process would have brought confidence and certainty that these products were adequately designed and risk-managed to succeed.

It is our understanding that the CFTC also plans to look at how exchange governance oversees the launch of these novel products. Just as regulatory oversight committees provide an independent voice on exchange boards regarding *regulatory* issues, it is equally important that exchange governance be constructed to ensure that *risk* issues are properly being debated and addressed.

In conclusion, we do not believe it is the role of government to direct the business decisions of the markets it regulates. However, we commend the Chairman and the commission for their willingness to reflect on the recent bitcoin futures launch, evaluate lessons learned and consider ways to make the existing self-certification process even better.

I appreciate MRAC Chairman Behnam and this Advisory Committee's willingness to discuss this important matter as part of the MRAC agenda.