



Discussions with the CFTC & SEC

Clearing

**The Goldman Sachs Group, Inc.
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Agenda

- Overview of Central Clearing in OTC Markets
- Clearing House Risk Standards
- Documentation
- Governance and Ownership

Overview of Central Clearing in OTC Markets

■ Key Benefits of OTC Clearing:

- Reduction of systemic risk
- Multilateral netting
- Increased transparency
- Uniform collateral management
- Consistent risk management for all clearing participants
- Centralized management of member default and related consequences

■ Key Considerations:

- Risk management and valuation model implications of more complex products
- Impact on appropriate margin requirements of:
 - Broad range of liquidity for different OTC products
 - Likelihood of lower liquidity during periods of financial or market stress
 - Decentralized and infrequent trading resulting in less reliable price observations
- Connectivity between members, CCPs, clients and middleware providers

■ Management of clearing house position in a member default is complicated by diversity of products (across Futures, Rates and Credit Derivatives) and requires risk-taking participation of clearing members

Clearing House Risk Standards

■ Product level considerations

- Liquidity of different products
- Correlation with events of default
- Concentration of large position with individual clearing members and/or their clients
- Directional bias of clearing member books
- Complexity of overall portfolio
- Inter-market correlation assumptions

■ Margin and Guarantee Fund Requirements

- Margin requirements should meet a minimum standard and adjust to changing market conditions
- Guarantee fund requirements should meet IOSCO standards
- Funded vs. unfunded waterfall obligations

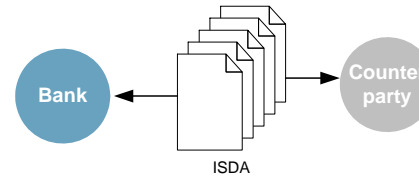
■ Membership criteria and prerequisites:

- Adequate resources and operational capabilities
- Willingness and ability to make markets in diverse set of products, including providing daily pricing
- Sufficient capital, trading expertise and formal commitment to participate in large scale liquidation

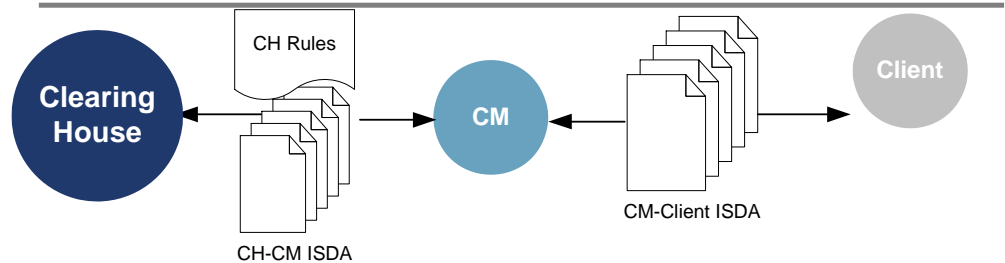
Documentation Issues

Client Clearing Documentation –

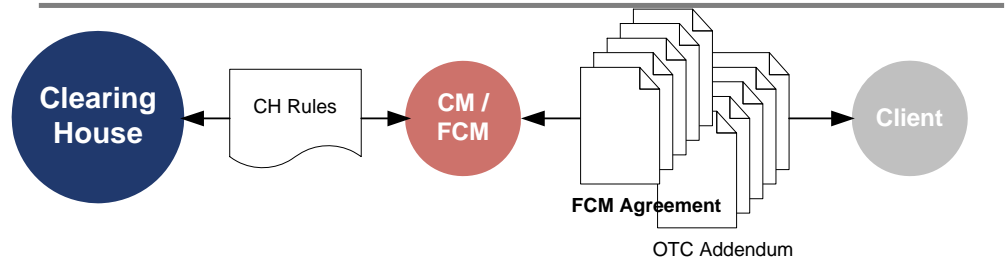
- Bi-lateral OTC derivatives transactions



- “ISDA-based” client clearing model [Planned, never implemented, pre-Dodd-Frank]



- “FCM model”
Post Dodd-Frank, collateral held for US clients who carry cleared derivatives contracts will be required to be held by an FCM



Execution Documentation

- ISDA documentation or a compensation agreement may be required

Give-Up Documentation

- Allocation of risk and responsibilities among the parties, with focus on status of trades that fail to clear

Governance and Ownership

Ownership of Market Infrastructure by Users

■ Governance

- Clearing members have material participation in governance
 - Default management
 - Risk models
 - Rule making
- Non-clearing member representation in product offering, portability, etc.
- Independent directors

■ CCP Structure and Business Model

- Utility-like model focusing on systemic risk reduction over market returns
- Open architecture