



14 July 2023

FIA Response to LME consultation on Initial Action Plan and proposed miscellaneous amendments to the LME Rulebook and LME Clear Rulebook

Submitted electronically at consultation@lme.com

To whom this may concern,

On behalf of FIA¹ and its members, we express our appreciation for the opportunity to comment on the consultation on initial action plan proposals and proposed miscellaneous amendments to the LME rulebook and LME Clear rulebook² (the “Consultation”). We generally support the proposed changes but would like to reiterate that some changes we consider potentially significant are classified as “miscellaneous amendments” under the LME Exchange Rulebook amendments. Such changes should be highlighted appropriately.

We have no specific comment in relation to Section A of the Consultation “Action Plan Proposals”, but acknowledge the changes reflect FIA’s response³ to Oliver Wyman during their market-wide engagement exercise to support appropriate level of transparency and governance on stock inventories.

On section B “Miscellaneous LME Rulebook Amendments”, we consider, as stated in paragraph 51, that some changes introduce requirements going beyond these set by other exchanges and poses legal challenges. We recommend the LME to retain its current rules or to implement approach followed

¹ FIA is the leading global trade organization for the futures, options and centrally cleared derivatives markets, with offices in Brussels, London, Singapore and Washington, D.C. FIA’s membership includes clearing firms, exchanges, clearinghouses, trading firms and commodities specialists from more than 48 countries as well as technology vendors, lawyers and other professionals serving the industry. FIA’s mission is to support open, transparent, and competitive markets, protect and enhance the integrity of the financial system, and promote high standards of professional conduct. As the principal members of derivatives clearinghouses worldwide, FIA’s member firms play a critical role in the reduction of systemic risk in global financial markets.

² As notified under the [LME Notice reference 23/090](#).

³ [FIA responds to independent review of LME nickel market disruption | FIA](#)



by other exchanges such as members annual disclosures of adequate systems and controls. Paragraph 86 also raised concerns as it proposes to extend confidentiality agreement to apply to trading on all Execution Venues. Members' compliance with the proposed rules will depend on members interpretation and we recommend further clarification, especially of paragraph 1.12 (c) (b).

Finally proposed changes under section C of the Consultation "Miscellaneous LME Clear Rules Amendments" are generally welcomed. Some of the proposed amendments address FIA's comments shared with Oliver Wyman during the market-wide engagement exercise.

You will find detailed comments on the appendix below on the Consultation and we welcome the opportunity to discuss with you any of the comments and recommendations should you require additional information.

Respectfully submitted,

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FIA

Appendix – Detailed comments

Section B – Miscellaneous LME Rulebook Amendments

Paragraph 51: We communicated this in response to previous LME consultations, it is unfortunate to mark amendments with a potentially significant impact as “miscellaneous amendments” rather than highlighting such changes appropriately. Namely, we are concerned about the proposal in paragraph 51: Obligations relating to the adequacy of Candidates’ and Members’ systems, controls and procedures. The LME proposes amending Regulation 4.3 of the Membership Regulations. The Regulation currently contains an obligation for a Candidate and Member to have adequate systems and controls to address the risk of money laundering and financial crime. These must be substantiated upon request. After amendment, **the Regulation would require the systems and controls to address more generally any applicable legal or regulatory requirements, breach of which would pose risks to the performance of the LME’s functions (in addition to addressing the risk of market abuse, money laundering and financial crime).** As amended, the power would, as with the current power, permit the LME to request details of these systems and controls and/or a reasoned legal opinion, or reasoned opinion from a reputable compliance consultancy, that they are appropriate. Additionally, to reflect the existing substance of Regulation 4.3 of the Membership Regulations more closely, the LME proposes to amend the title to refer to “Systems, Controls and Procedures”.

The proposal goes beyond requirements set by other exchanges and poses legal challenges, legal opinions are typically privileged and cannot be shared with third parties. We propose to retain the current rules, which permit the LME to ask for details regarding the systems and controls or to implement the approach followed by other trading venues, i.e. to ask members for an annual representation that they have adequate systems and controls in place.

Paragraph 86: Confidentiality provisions in paragraph 86 of the Notice and paragraph 1.12 of Part 3 (Trading Regulations), in which the LME proposes that Part 3, 12.4 (confidentiality obligations in respect of trading on LME Select) should be expanded to apply to trading on all Execution Venues.

We are concerned about this proposal because the inter-office market works quite differently from the LME Select market and are often based on long-term relationships with traders taking orders over the phone likely being able to recognise the voice and be able to identify callers, thus the ability of LME members to comply with the proposed amendments will depend on the interpretation of the rules and we would welcome further clarification, especially regarding paragraph 1.12 (c) (b).

Section C – Miscellaneous LME Clear Rules Amendments

Change to the definition of Cash Cover (Rule 1): We welcome the new provision for LME to retain Settlement Payments as Cash Collateral in anticipation of future Margin Requirements should the Member elect to. This provides members with additional flexibility with regards to collateral management and transactions.

We note however that such excess cash collateral information (i.e. collateral deposited beyond current Margin Requirement or 'Excess Member Payment' as newly define under the paragraph 98 of the Consultation) should also be easily accessible to members for reconciliation and cash management purpose. In addition, such cash should also be readily transferable back to the member on its request, as long as the member's Margin Requirements are met.

Significant Disruptions to LME Clear Systems (Rule 2.4.5): We understand LME Clear's intention to take steps to ensure the integrity of the Clearing System, such that in the event of a significant disruption to its systems, it may take discretionary steps to resolve the situation. However, we would suggest that in such circumstances, members should be notified of such issues and informed of the relevant actions taken to resolve such issues as promptly as possible.

Delivery Deferral Power in Default Period (Rule 10.4.1(w)): We understand the introduction of Delivery Deferral Power is to provide an alternative to cash settlement when sourcing warrants in low-stock environment. This would be a preferable method under normal market conditions as the Buyer will ultimately source the underlying. It is understood that such power is introduced in the LME Clear Rules to reflect similar power as the Exchange and to ensure that the same options are available under normal conditions or Member Default condition.

While we support such provision as it allows for some flexibility, we want to highlight that such optionality should be carefully considered in the event of a member's default. We would recommend that LME Clear should have pre-defined criteria as to which option to select in different scenarios to efficiently manage the Default process.

Client assistance in the Default Auction process (Rule 2.6.5 and Default Procedure Part C6.4(f)&(g)): We support LME Clear to formalize the participation of Clients of Members to the auction process as part of the default management process. We appreciate this will encourage and improve the quality of bids received during the auction process. We support that Clients participation should be approved by LME Clear and that confidentiality obligations are being addressed between LME Clear, the member and the clients.

We would like to emphasize that preparedness is crucial when it comes to default management and recommend that client participation approval should be obtained as a matter of normal business and that client participation to default management test is a pre-requisite before participating to a real auction.

Delivery Failure Prevention Service (Rule 7.11): We understand the Delivery Failure Prevention Service addresses issues related to inappropriate management if position going into delivery. We consider this an additional tool for LME Clear to risk manage such situations and therefore we support such change on this basis.

Default Fund Resizing (Default Procedure Part B2.2(b)): We welcome the change to the Default Fund resizing allowing LME to resize the fund intra-month to respond promptly to market risk.

We would note that such change should be carefully considered striking the right balance between risk coverage and procyclicality. And we would recommend providing sufficient notice to members to mitigate any liquidity risks and constraints they might face during period of high market volatility.

Changes that have retroactive effect (Rule 2.2.9), Member Termination Date (Rule 3.6.5), Change to Non-Default Loss reporting provision (Rule 10.14.9), Default Fund Floor (Default Procedure Part B1.2(c)) and Notification Requirements (Membership Procedure Part B7.1): Any clarification updates to rulebooks are usually welcome as it provides members with increased certainty and limits the risk of misinterpretations.

We therefore support the minor, administrative and technical changes regarding the switch from EONIA to €STR, the renaming to “Steel Rebar” and DCVM for monthly average futures. In the same spirit, we support also the clarification relating to Member Termination Date, change to NDL reporting provision, the member notification requirement in case of recovery plan activation, the early margin requirement times, the default fund floor, clarification of the term “retroactive” in the context of forward-looking changes and clarification of liability limits over payment transaction.