

LETTERS

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Clearinghouses Can Solve Many Derivatives Problems

*Prof. Mark J. Roe argues that clearinghouses may not be adequate to prevent default on derivatives or may put taxpayers at risk ("Derivatives Clearinghouses Are No Magic Bullet," op-ed, May 6).*

Clearinghouses require minimum capital to be posted for each transaction at the initial acceptance of a trade, then mark-to-market the positions daily, even intraday, and in volatile markets more often than that. The daily settlement of these trades allows for the earliest warning of failure to pay with enough capital in reserve at the clearinghouse, built up by multiple margin calls throughout the life of the contract to buttress a minimum number of days of the severest market declines. When the clearinghouse declares a member firm overdue on its daily settlement commitments, the defaulter's positions can be transferred to another willing clearing member's account.

Those positions are trades originally entered into between counterparties of a defaulting member, and whose obligation to pay was transferred to the clearing house as the central counterparty.

The speedy transfer of positions of the collapsed Refco and Bear Stearns without loss to clients and clearing members is a testament to the success of this method of risk-managing contract markets. The industry comes together to share risk in a clearinghouse which is better than placing the burden on the taxpayer.

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