
SPAN®: A New Risk Measurement Model

PRESS RELEASE

The National Depository has transferred to KDPW_CCP all functions related to the clearing of transactions executed on the regulated market and in the alternative trading system and the operation of the clearing guarantee system as of 1 July 2011. KDPW remains responsible for transaction settlement and central securities depository functions. The process implements world-class standards at KDPW and enhances the competitiveness of the Polish capital market. The spin-off of the clearing house from KDPW's structure derives from the National Depository Strategy 2010-2013 adopted in late 2009 and consistently pursued among others to develop a new business model of KDPW.

The launch of KDPW_CCP operations will be concurrent with the implementation of a new clearing guarantee system. The implementation of new solutions in this area will improve the level of offered guarantees by matching the collateral to the generated risk. The new system is based on international standards and solutions used on the biggest financial markets of the world, in particular the SPAN® methodology.

SPAN® (Standard Portfolio Analysis of Risk) enables the estimation of risks of cash and derivative transactions and the calculation of contributions to the clearing fund on that basis. The methodology was designed and implemented by Chicago Mercantile Exchange Inc. (CME) in 1988. Since then, the methodology has been continuously improved in order to maximise and update the range of analysed risks.

Better protection of resources in the clearing guarantee system

Thanks to its complete risk description, SPAN® ensures more precise risk measurement compared to the current methodology. This will make the Polish market more secure and more attractive to investors (in particular, big foreign companies) and KDPW_CCP members.

As an important advantage of the implementation of the complete SPAN® methodology, it will enhance the transparency of the Polish market in terms of applied risk management methods because SPAN® is a standard methodology recognised by large foreign investors and broadly used on the global financial markets.

Concurrent with the change of the risk calculation methodology and, consequently, the method of calculating margins and the clearing fund, the structure of contributions to the overall clearing guarantee fund will also change. This will involve a **shift of the main burden from solidary**

funds (clearing fund) to individual margins, which will not be used in case of another member's default. The main benefit of the change is that each member's margins will be protected.

Standard on more than 50 financial markets world-wide

The SPAN® methodology chosen by KDPW_CCP is used as a tool of calculating required margins by most institutions which offer clearing of derivative instruments world-wide.

Table 1. Selected users of SPAN® methodology

No.	Institution	Country
1	Chicago Mercantile Exchange Inc.	USA
2	Chicago Board of Trade	USA
3	The Clearing Corporation	USA
5	London International Financial Futures Exchange	UK
6	London Clearing House	UK
7	Euronext	FR/B/NL/P
8	LCH.Clearnet	UK
9	KELER	Hungary
10	Eurex Clearing AG	Germany
11	Japan Securities Clearing Corporation	Japan
12	Singapore Exchange	Singapore
13	Taiwan Securities Clearing Depository	Taiwan
14	Hong Kong Exchange	China
15	Shanghai Futures Exchange	China
16	Sydney Futures Exchange	Australia
17	Bombay Stock Exchange Clearing House	India
18	Dubai Gold & Commodities Exchange	UAE

Source: CME

In Europe, the SPAN® methodology in a form very similar to the solution designed by KDPW is used in the risk management system of LCH.Clearnet (the markets covered by LCH.Clearnet clearing include Liffe Financials, Liffe Equities, Liffe Commodities, Liffe Indices, London Metal Exchange, LCH EnClear). The SPAN® methodology is used on all derivative markets in North America as well as in Tokyo, Osaka, Singapore, Hong Kong, Sydney; in total, on more than 50 markets world-wide, by stock exchanges and clearing houses, depending on the adopted model of offering guarantee services.

A high potential solution

Considering the broad range of instruments for which the SPAN® methodology can be used to measure risk and determine required collateral, the implementation will effectively support growth of markets and new instruments to be cleared by KDPW_CCP. Thanks to universal risk assessment tools for various instruments traded on the exchange, transaction clearing and risk management processes for such instruments will be handled in a uniform fashion and will require no modifications (applications, software) on the part of market members.
