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FIA Response to BCBS, CPMI, IOSCO Consultation on Review of Margining Practices

Introduction

On behalf of FIA¹ and its members, we express our appreciation for the opportunity to respond to consultation. We view this consultation as an important milestone in the development of international standards for the regulation and oversight of derivatives clearinghouses.

As the consultation states, the extreme volatility of early 2020 provided the first real-life stress test of the post-crisis reforms to derivatives markets, and in particular the rules intended to drive greater use of central clearing for a wide range of derivatives and thereby reduce systemic risk. Thanks to those reforms as well as greater voluntary adoption of central clearing, most derivatives traded worldwide are now cleared through central counterparties.

During the peak of the Covid-related volatility, the CCPs performed their mission as the architects of those reforms envisaged. They marked to market billions of dollars in risk exposures, they managed counterparty risk very effectively, and they kept markets functioning even amid record-breaking volume and extreme volatility.

Yet the performance was not perfect. As we pointed out in our October 2020 paper², the sudden spike in initial margin requirements created stress for CCP members and their clients by forcing them to immediately post billions of dollars in collateral. The spike was both very rapid and very large, with initial margin requirements on some of the most widely used equity index futures rising by more than 100% in less than a month. As discussed in the consultation, these increases in margin requirements helped drive a 40% increase in the total amount of initial margin held by clearinghouses between February and March, with an even sharper increase within certain asset classes.

The fact that margin requirements increased was not an accident or a mistake, rather it was a logical and sensible response to the increase in volatility. The CCPs correctly recognized that the rise in volatility increased the potential exposure to loss on the derivatives that they clear, and they increased the amount of margin requirement to cover that exposure.

But the size and velocity of that increase raises important questions about margin practices in derivatives clearing and their potential to increase liquidity risk in the global financial markets. We are strong supporters of central clearing, but we believe that this episode demonstrated the need to review margin models and reduce their procyclicality. We therefore welcome the issuance of this consultation

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 <https://www.fia.org/resources/fia-issues-white-paper-impact-pandemic-volatility-ccp-margin-requirements>



on margin practices, and we look forward to working with the international standard setting bodies as well as market regulators, central banks, bank supervisors and other policymakers.

We acknowledge that anti-procyclicality measures may lead to higher margin requirements for some products and some market participants (clearing members and their clients. This is not a small concern for us. Any increase in margin requirements creates a tradeoff. On the one hand, margin is the first line of defense against a loss. On the other hand, higher margin increases the cost of clearing.

We therefore have sought to strike a balance in our recommendations. We are not calling for an across-the-board increase in margin. Instead, we are calling for appropriate coverage for risk through the cycle. A margin model that generates margin requirements that are too low during periods of calm effectively exposes market participants to extreme movements when volatility spikes.

Equally important, we are calling for increased transparency into how margin requirements are set. This will help both clearing members and their clients manage the increase in margin when volatility rises. And we are calling for changes in operational aspects of clearing that we believe will reduce the demand for liquidity during periods of stress.

General findings

- 1. Does the report accurately describe the key market events of the Covid-related period of stress from February to April 2020 and its effects on the magnitude and frequency of the calculation and payment of margin in centrally and non-centrally cleared markets? If not, in what ways are the descriptions not fully representative of the events? Are there any other important events or effects missing? If so, please provide any information or data that are relevant to the missing events or effects to the extent feasible.*

FIA strongly agrees with many of the findings in the consultation. In particular, we commend the members of the working group that drafted the consultation report for the quality of their quantitative analysis, and we agree with their conclusion that requirements generated by CCP margin models were the primary drivers for the increase in initial margin, rather than changes in positioning or changes in market valuations. We also agree that central bank intervention made the period of market stress much shorter than it otherwise would have been, and in our view the strains on liquidity would have been much worse if the central banks had not intervened.

FIA strongly agrees with many of the recommendations for further action and supports the following four goals:

- Reducing the procyclicality of margin models
- Increasing transparency into margin model calculations
- Improving the tools provided by CCPs for forecasting margin requirements
- Encouraging more consistency in the margin requirements set by CCPs for similar products

The consultation correctly notes that ad hoc margin calls create stress for clearing members, but it underestimates both the frequency and the severity of their impact. Ad hoc calls may be relatively small



compared to end-of-day margin calls, but they tend to come at the worst possible time – when markets are at their most volatile and the demand for liquidity is at its peak. And their unpredictable nature makes it more difficult for market participants to source the necessary collateral when they arrive. We recognize that clearinghouses need the ability to make ad hoc calls, but we emphasize that this power should be used only in the most extreme situations, and with appropriate transparency into the drivers of the call(s).

We also believe that the consultation should have given more consideration of margin breaches at both the portfolio and individual contract level. Margin models are not designed to cover 100% of all possible market moves, but a more detailed analysis of margin breaches could be used to identify persistently insufficient margin requirements. CCPs provide information about margin breaches at the portfolio level, but we believe that information about margin breaches at the individual contract level should also be shared because that information informs decisions around resetting margin levels for each contract.

When evaluating the procyclicality of margin models, it is also important to evaluate not only the models themselves (risk parameters, core margin vs. add-ons, etc.) but also the operational framework under which CCP margin models are implemented. As we discuss later in this paper, operational implementation factors influence the severity of CCP margin procyclicality. Such factors can include but are not limited to: the timing of such calls, the currency in which intraday margin is called, and whether CCPs give credit for margin paid earlier in the day during the end-of-day process or return excess margin when there are variation margin gains.

As a general matter, FIA believes that action on these recommendations is urgent, not only because of the problems exposed by the Covid-related market turmoil but also because of unrelated changes in how CCPs set their margins. At least four large CCPs are embarking on a fundamental shift in margin calculation methodologies, moving from SPAN-based systems to Value-at-Risk-based models. As discussed below in the response to question 10, this shift makes it even more important for CCPs to provide more transparency into how their models generate margin requirements so that clearing firms and their clients can better anticipate margin calls.

Lastly, we think the evolution of risk models highlights a broader issue in the supervision of CCPs. The supervisory analysis of margin practices should not be a one-and-done exercise. The output of these margin models is critically important to the supervisory community in understanding the impact of margin calls on liquidity in the financial system, and we believe supervisors should monitor the performance of margin models on an ongoing basis going forward.

2. Does the report draw appropriate conclusions from the presented observations and analysis of the various aspects of centrally and non-centrally cleared margin during the 2020 stress period? If not, in what cases do you feel the conclusions are not justified by the included analysis? Are there any areas or specific topics of analysis you consider to be missing? If so, please provide any information or data that are relevant to the extent feasible. Please set out your views across the following sections:

a) The drivers of margin calls during the period of market stress covered by the report.

We believe that the report provides appropriate conclusions on the drivers of margin calls during the Covid-19 crisis period. In particular, the static portfolio back testing discussed in Section 3.1 confirmed a



key finding—that the increases in initial margin held by CCPs were driven primarily by the responses of margin models to the increase in volatility, rather than repositioning by market participants.

We also agree with one of the main insights, which is that there were significant differences across asset classes and between exchange-traded and over-the-counter derivatives. As noted in Section 2.2, initial margin for exchange-traded derivatives increased by 62% between the end of February and the middle of March, while initial margin for interest rate swaps increased by just 20%. In our view, the main reason is the differences in margin methodology for these two types of derivatives. For example, the margin period of risk is five days for cleared OTC derivatives, versus one or two days for exchange-traded derivatives.

Another important issue to consider is the relationship between the margin levels going into the March-April period and the size of the margin increase during that period. In our view, setting initial margin requirements at appropriate levels during periods of relative calm would reduce dependency on anti-procyclicality tools to manage the increase during periods of high volatility.

b) The current level of transparency in margin practices by CCPs and intermediaries.

The report confirms that transparency into CCP margins models differs across CCPs and jurisdictions but generally falls short of what is desired by clearing members and their clients. The report also confirms that even in those cases where CCPs provide predictive tools to help market participants anticipate calls for margin, they are not sufficient to meet the needs of clearing members and their clients.

From a clearing member point of view, there are important gaps in the transparency of margin models and practices, particularly around the parameters that CCPs use to calculate initial margin, the calibration of margin add-ons, and the use of ad hoc calls. Stressed margin add-ons are especially problematic. Several CCPs have a framework for charging stressed margin if it exceeds a certain percentage of the default fund. Given that CCPs seldom disclose their stress scenarios, it is difficult for members to anticipate the stress losses on their portfolios and predict if they will be subject to this charge.

We find it quite significant that only 20% of CCPs offer predictive functionality that lets users estimate what their margin requirements would be in different volatility scenarios. Although some CCPs offer "what-if" tools, these generally are limited to prices from the close of the previous day, and they do not allow any type of predictive estimates based on current prices or future scenarios. This may be sufficient during calm conditions, but when volatility picks up, they cannot be used to estimate what today's portfolio will generate for tomorrow's call.

We strongly believe that the greater availability of predictive tools, and improvements in the usefulness of those tools, would have a significant impact on the ability of market participants to anticipate demands for liquidity. This in turn would reduce the potential for margin calls to put a strain on funding markets.

As noted in Section 2.2 of the report, the size and speed of initial margin increases differed not just across asset classes but also within asset classes. We find it difficult to understand why different CCPs would set significantly different margin requirements on the same or similar products. Although each CCP uses a different mix of components in its margin methodology, the output for a given quantity of



risk should be roughly the same. For example, if two CCPs are clearing a futures contract based on the same equity index, the initial margin requirements should be roughly the same.

This should also be true with the responsiveness of margin models to increases in volatility. When similar products encounter similar increases in volatility, they should face roughly similar increases in initial margin. Just to be clear, we are not advocating for convergence in margin models. Diversity in margin models is healthy for risk management. But we encourage the supervisory authorities to examine situations where margin requirements are far apart and consider why there are such differences.

The report also does not examine or provide granular data on anti-procyclicality behaviors within asset classes. This was the case with exchange-traded derivatives, which the report treated as one "asset class." Different categories of ETD experienced different levels of volatility during the crisis period. Commodity futures, for example, behaved very differently from equity futures. Taking a closer look at more granular data within the ETD asset class may provide more insight into margin levels and the appropriateness of various APC measures.

- c) *The preparedness of intermediaries and clients for meeting the increased margin calls seen during the period of market stress covered by the report.*

We agree that central bank interventions played a role in stabilizing markets during the period March – April 2020.

Most intermediaries had sufficient liquidity resources to meet margin calls, as shown by the data presented in section 5.1 of the report. The impact of margin calls on clients, on the other hand, was more complex. A majority experienced "no significant increases" in liquidity demand for margin calls, according to section 5.2, but a number of clients indicated that their liquidity needs "were materially greater than expected."

The report also found that some clients "increasingly used repo in March and asset sales in March and April" to meet their margin requirements. We believe that for those clients who needed to rely on repo markets and sovereign debt markets to raise cash, the central bank interventions played an important role in assuring that those markets continued to function cost-effectively as sources of liquidity for the clearing system.

We believe that the report does not provide enough information to fully assess the strains created by the spike in margin calls. Although margin calls were met in time, the survey responses showed that smaller clients had more difficulty in meeting the calls, and we have little to no visibility into their ability to liquidate collateral.

- d) *The relationship between margin demands and other liquidity demands during the period February–April 2020.*

The report provides some valuable insights on the relationship between margin calls and liquidity constraints during the Covid-19 period. As the report states in section 6, the extraordinarily large margin calls in March and April 2020 took place in "a context of impaired market liquidity" and appeared to have "further propagated the stress across the system."



We note that sudden margin increases can trigger liquidity constraints not only for clearing members but also for their clients. Although the rapid response of central banks eased the strain on liquidity during this period, we should not assume this will always be the case, nor should CCP margin models be predicated on central bank intervention, and this is why we believe that stronger anti-procyclicality measures should be a priority.

We understand that there is a separate work stream on the impact of the Covid-related turmoil on funding markets. A [report published by the International Capital Markets Association](#) found that many market participants encountered difficulties in using the European repo market for collateral transformation during that period of time. We urge policymakers to examine in greater detail the linkages between repo markets and the margin calls generated by clearinghouses.

Increasing transparency in centrally cleared markets

- 3. Do you agree with the proposals for further international work regarding good practices, metrics and disclosures concerning procyclicality in CCP IM models? Are there other aspects of CCP IM where additional disclosures should be prioritised for further work?*

We agree on the need for further work on metrics and disclosures regarding procyclicality in initial margin models, but the proposed recommendations are not precise enough.

Clearing members need details on the design and usage of anti-procyclicality controls so that they can anticipate how initial margin calls will trend during stress periods. To enable this, CCPs should disclose the following:

- CCPs' risk appetite for procyclicality of margins similar to requirements under EMIR Guidelines³ and performance relative to the appetite
- The extent of usage of anti-procyclicality tools in their IM so that market participants can predict IM calls during stress periods – e.g., knowing whether margin levels are model driven vs. floor driven, and to what degree margin buffers are being used
- Specification of adjustments made to address procyclical behavior, such as volatility floors or scaling schemes (decay factor)
- Analysis of how margins would react to extreme volatility scenarios (e.g., 10%, 20% or 30% increase in volatility) that are specific to each of the significant products cleared by the CCPs.

Details on how CCPs calculate base initial margin and margin add-ons would also better enable clearing members to anticipate how initial margin may react during periods of volatility.

In addition, the quantitative public disclosures published by CCPs should include more granular information on initial margin performance and this information should be published more frequently than quarterly. These disclosures have proven to be an important source of quantitative information regarding CCP financial resources, risk exposures and risk management practices. Many clearing firms, asset managers and other market participants use the information in these disclosures in their evaluations of counterparty risk in their relationships with CCPs. Clear, accurate, comparable, and

³ Guidelines on EMIR Anti-Procyclicality Margin Measures for Central Counterparties, 15/04/2019



consistent disclosures are critical to these evaluations, and we urge regulators to work with all stakeholders to improve these disclosures. In addition to the increased data, clearing members believe it is important that the CCPs maintain frequent communication with the clearing members, particularly during times of stress. Some CCPs occasionally provide an alert to clearing members to expect outsized margin calls but most do not. This type of notice from the CCP allows the clearing member to start preparing for such calls.

4. *Does the report identify appropriate aspects of transparency in centrally and non-centrally cleared markets for further international work, including identifying data gaps, enhancing disclosures to clearing members and increasing margin model transparency?*
 - a) *What specific areas of transparency would be most helpful? What (if any) are the barriers to providing those points of transparency?*
 - b) *Should any other areas of increased transparency be considered?*

Enhanced transparency and predictability would significantly assist participants in preparing for and managing margin calls. In particular, we believe the following four areas of transparency would be the most helpful:

- One of the most critical pieces of information required from a clearing member perspective is documentation on risk methodologies – i.e., details on CCPs' margin framework, back testing and stress testing framework. This would benefit participants by enabling them to conduct in-depth what-if analyses and allow an understanding of their membership risks and how liabilities may evolve in a variety of stressed market scenarios where margin and default fund resources may be inadequate. Although some CCPs provide some of this information, there is little consistency across CCPs, and access to the information is not always straight forward.
- Another critical area of transparency would be calibration of various margin add-ons and how these interact with intra-day margin frameworks so that members can better anticipate potential margin calls. Margin add-ons are usually a “black box” that makes it difficult for clearing members to determine why there is an add-on and which client or clients are triggering this requirement. For example, the scenarios used by CCPs to calculate stressed margin add-ons are not disclosed to clearing members, making it impossible to predict these charges.
- We believe the report should recommend more transparency into the breakdown of margin calls, particularly ad hoc calls. For example, it would be very helpful if CCPs clearly separated the initial margin and variation margin components of their margin calls, and if they clearly identified margin calls driven by clearing members' proprietary activity vs. client activity.
- We believe CCPs could provide more granular information about the impact of stress scenarios. CCPs are likely to know the "stress test loss over initial margin" (STLOIM) for each clearing member in each of their stress scenarios. CCPs therefore could provide anonymized aggregated reporting on STLOIM ratios. For example, such reporting could include how many members would consume certain amounts of the default fund under each scenario.



- Another important improvement would be disclosure of back testing results and margin breach information at both the account level and the contract level. This could include the frequency of margin breaches, the largest relative margin breach, and they average relative margin breach. These metrics should be calculated against the same baseline, such as 1-day profit/loss, for comparability across CCPs with different margin periods of risk. For significant products, these metrics should be expanded to include margin breaches over 1-d/2-d/5-d periods as well as maximum 1-d/2-d/5-d/1-month margin increase over the prior quarter with a comparison of volatility change in the same period. Some CCPs currently offer this analysis.⁴ Margin breach transparency will equip participants to better evaluate the effectiveness of margin models and ensure core margins are calibrated appropriately. The consultation's observation in section 3.2.4 that margin exceedances showed "no clear relationship" with IM changes is counter-intuitive, and suggests that some CCP models discount core margins, shifting disproportionate burden of uncovered risk to clearing member financial resources rather than aligning risk incentives via adherence to the "defaulter pays" principle.

We recognize that CCPs may be reluctant to release some of this information into the public domain. We therefore suggest that this information could be provided to clearing participants through secure portals with limited access.

Enhancing liquidity preparedness of market participants as well as liquidity disclosures

5. *Do you agree with the proposals for further international work to enhance liquidity preparedness in the NBFIs sector, including the development of appropriate liquidity metrics and disclosures, analysis of liquidity provision robustness and expanded information sharing between intermediaries and clients? Have the proposals identified all key aspects of NBFIs sector liquidity preparedness which should be included?*

The primary way to address this should be through greater transparency to facilitate better preparedness. Specifically, this should include CCPs making information available to clients. This process should not be facilitated by clearing members due to legal barriers and operational complexity.

A large amount of information made available to clearing members is subject to non-disclosure agreements and cannot be disclosed to clients. In addition, establishing disclosure requirements would expose clearing members to legal risk. In our view, the CCPs, as owners of the information, are best placed to determine the information they are willing to share with clients.

For instance, it would be very difficult for clearing members to explain to clients how CCPs calculate positions at portfolio level, apply haircuts and calculate add-ons. Too much discretion is left to the CCPs so having the clearing members pass on information is not efficient nor workable. This reinforces the need for CCPs to offer predictive tools for clients as well as clearing members.

⁴ Eurex provides product-level back testing data for certain products for some of its most heavily traded futures and options as well as certain interest rate swaps. See link: <https://www.eurex.com/ex-en/find/news/Pioneering-CCP-transparency-to-maintain-safer-markets-part-7--2716180>.



Note that the European Systemic Risk Board published in January 2020⁵ a report on mitigating procyclicality with the policy option "limiting the discretion of client clearing services providers towards clients." We disagree with this option.⁶ Just as CCPs need discretion to raise margin during stressed periods to ensure they do not have uncollateralized risk, clearing members should have ability to pass through intraday margin calls or otherwise increase margins to ensure that the risk that they are guaranteeing is adequately covered. This, in conjunction with our earlier anti-procyclicality recommendations, is in line with the "defaulter pays" principle without ignoring valid concerns over liquidity risk in times of stress.

Identifying data gaps in regulatory reporting

- 6. Do you agree with the proposals for further international work to evaluate data gaps in regulatory reporting by banks and non-banks? Are there particular data gaps you would identify as being of material importance? If so, please provide any supporting information and data to the extent feasible.*

We have not identified any data gaps as it relates to the liquidity positioning of banks and broker-dealers in major jurisdictions such as the EU and the US, as these firms already report a significant amount of granular liquidity information to regulators on a daily basis. We do not see any need at this time for further reporting in this area.

Streamlining VM processes in centrally and non-centrally cleared markets

- 7. Does the report identify appropriate proposals for further international work on streamlining VM processes in centrally and non-centrally cleared markets? Should any other aspects of VM processes be included in this work?*

One specific area where international work on variation margin processing would be beneficial is in the use of intraday margin calls.

Clearing firms recognize the need for CCPs to be able to call for additional funds intraday, rather than waiting until the end of the day, in order to maintain sufficient collateral to cover actual and potential losses. Having the ability to make intraday calls is an important part of the toolset used by CCPs to manage risk exposures on a real-time basis and ensure the resiliency of the clearing system.

But intraday margin calls can intensify funding pressures on clearing members in a procyclical manner. This is particularly true for periods of market stress, not only during the stress event itself but also on an ongoing basis, in the form of liquidity that must be kept on reserve even in "calm" periods in case another spike in volatility triggers additional calls. For that reason, FIA believes the use of intraday margin calls should be carefully reviewed as part of the overall effort to reduce procyclicality.

⁵ <https://www.esrb.europa.eu/news/pr/date/2020/html/esrb.pr200109~242bd091d4.en.html>

⁶ The final "[Recommendation of the European Systemic Risk Board of 25 May 2020 on liquidity risks arising from margin calls](#)" concedes that the "soundness of the risk management practices adopted by the clearing members" should not be "materially curtailed" and their resilience not be affected.



It is important to distinguish between intraday calls that are issued to cover intraday trading losses, and intraday calls that are issued to collect additional initial margin on existing positions. If initial margin models are appropriately calibrated, intraday calls for initial margin should be the exception, not the norm, for existing portfolio risk.

It is also important to distinguish between routine calls to cover intraday price movements and ad hoc intraday calls. Both are important tools for CCPs, but ad hoc calls put far more pressure on the ability of clearing members to fund the calls. Clearing members generally maintain a certain amount of cash and other collateral on hand to meet their liquidity needs, but the unpredictable nature of ad hoc calls makes it more difficult for clearing members to forecast the amount of margin they will need that day and collect collateral from customers before the payment is made.

The consultation correctly notes that ad hoc margin calls create stress for clearing members, but it underestimates both the frequency and the severity of their impact. As stated above in our response to question 1, ad hoc calls may be relatively small compared to end-of-day margin calls, but they tend to come at the worst possible time – when markets are at their most volatile and the demand for liquidity is at its peak.

Furthermore, it is important to consider the size of the CCPs that are issuing these ad hoc calls. The consultation is correct in noting that peak amount for ad hoc calls was "far lower" than the peak end-of-day and intraday calls. But at smaller CCPs, ad hoc calls may be relatively larger compared to end-of-day and intraday calls, which could mean greater strains on liquidity in the markets those CCPs serve.

Aside from ad hoc calls, routine intraday calls can also create stress for clearing members, when volatility significantly increases the magnitude of scheduled intraday calls and factors such as asymmetry and limited netting – described further below – increase the funding burden beyond actual risk.

There are several key points to consider when assessing the impact of intraday calls on the clearing firms' liquidity positions:

- They can be asymmetric; some CCPs call intraday for collateral to cover intraday losses but do not pay out such funds as variation margin on gains. Similarly, some CCPs make multiple intraday calls for gross losses but do not return collateral for gains in customer portfolios. The cumulative impact of these intraday calls during a period of market stress could create serious liquidity issues.
- They are often unscheduled, making it more difficult for clearing members to anticipate the need to fund the calls and adding to the stress on clearing members during periods of market turmoil.
- Intraday calls, even when scheduled, are not necessarily issued at the same time every day. During periods of market stress and volatility, these calls are often issued late in the day, putting further pressure on clearing members' funding requirements. Furthermore, some CCPs that run multiple intraday calls can collect earlier in the day, but not pay back later in the day if the exposures reduce.
- Customers are not always able to meet intraday calls from clearing members, resulting in the clearing members having to temporarily fund customer trading losses until positions are fully marked-to-market as part of the end-of-day margin run.



- In addition, some CCPs do not always allow such funding to be applied against end-of-day requirements, resulting in double funding.
- CCP rules generally grant the CCPs a high degree of flexibility in terms of the amount, frequency and timing of intraday calls while simultaneously placing stringent terms on the obligations of clearing firms to meet them. For example, typically these calls must be met in cash and within one hour, which provides participants with limited ability to understand the drivers and verify the appropriateness of the calls before making margin payments.
- During highly volatile market periods, clearing firms can face a “multiplying” effect where they are called upon to meet large margin calls from multiple CCPs and in multiple currencies almost simultaneously, increasing the risk of systemic liquidity issues.

Clearing firms should hold and do hold liquidity buffers to cover intraday calls. However, during the extreme market volatility caused by the Covid-19 crisis, the size and frequency of calls received was much higher than 'business as usual' levels. Firms had to fund ad hoc intraday margin calls from multiple CCPs almost simultaneously. This stressed the ability of clearing members to source liquidity within the deadlines set by the CCPs. It also presented operational challenges in managing large calls in multiple currencies simultaneously. These issues can be particularly acute when calls are made late in the day. In extremis this could contribute to procyclical systemic liquidity issues due to interdependencies between CCPs and their clearing members and across CCPs with overlapping membership.

We acknowledge that the ability to make intraday margin calls is necessary for the prudent management of CCP risk. But CCPs should limit the number of times that intraday calls are used for trading losses. This limit should be based on when the unsecured level of risk reaches a certain percentage of the total initial margin collected for a clearing member. In addition, in light of the strain that intraday calls can put on liquidity, CCPs should not view intraday calls as replacements or mitigants for appropriate end-of-day margining and appropriately calibrated initial margin models.

We also note that the occurrence of frequent intraday margin calls may indicate that a CCP's margin framework is not performing adequately, or that it has a relatively high tolerance for risk. It is also important to note that there is a dynamic interaction between margin floors and intraday calls. If floors are set higher, they will reduce the need for intraday calls.

For these reasons, we make the following recommendations:

1) Intraday margin calls should be scheduled and clearly defined to all participants:

- Routine intraday calls should be made at the same time every day.
- CCPs should make intraday calls as early as possible in the business day and consider setting limits on how late in the day they can be made.
- An intraday call should clearly separate the initial margin and intraday trading loss components of the call.
- CCPs should be transparent about the drivers for intraday margin calls, including whether the margin requirements stem from proprietary house or client activity.
- Where clearing firms affirm that intraday calls are met by using clearing firm resources, the calls should be levied on a net basis (rather than gross) across accounts, where possible.
- Excess collateral held at CCPs should be permitted, where law allows, to cover intraday margin calls. Some CCPs only allow the use of excess cash to meet such calls.



2) Unscheduled or ad hoc calls should be available but only in extreme situations:

- Ad hoc intraday calls should be necessary only in times of extreme market dislocation or when the CCP has a large, uncovered exposure to a member. Margin calculations should be sufficient to ensure that ad hoc intraday calls occur relatively infrequently. Clear limits and thresholds on ad hoc intraday calls also should be considered.
- CCPs should provide full transparency for triggers of ad hoc intraday margin calls. This will assist clearing participants in actively tracking and monitoring liquidity demands.
- When CCPs offer more than one clearing service, an ad hoc intraday call triggered by market conditions affecting one of those services should be charged only to members of that service. For example, when CCPs structure their clearing services by asset class, with each asset class being handled separately from the others, a default in one of these clearing services should be covered by the resources dedicated to that service, and only that service, unless the CCP's rules clearly indicate otherwise.

Evaluating the responsiveness of centrally cleared IM models to market stresses with a focus on impacts and implications for CCP resources and the wider financial system

8. *Does the report identify appropriate proposals for further international work on the degree and nature of the responsiveness of CCP IM models to market stress? Should any other aspects of CCP margin models be included in this initiative?*

We strongly agree that further work should be done on this topic. The primary drivers of margin increases are IM models, and setting appropriate controls on their procyclicality is essential to managing demands for liquidity during periods of stress

We strongly endorse the proposal to explore appropriate ways to analyze, compare and set baseline expectations as to procyclicality in various settings.

We also strongly support the proposal for additional work to review IM levels in non-stress times and review the effectiveness of tools that lessen the procyclicality of margin models and the consistency of their use.

We agree that this work could help inform and/or complement existing international standards and guidance as to anti-procyclicality, and we urge policymakers to consider the merits of additional guidelines for supervisors' assessments of model attributes that can determine responsiveness to volatility. This could include lookback periods, identification of stress periods, decay factors, anti-procyclicality measures and MPOR.

It is important to note that most CCPs already have anti-procyclicality measures in place, as recommended by the CPMI-IOSCO Principles for Financial Market Infrastructures (PFMIs) and largely implemented since the GFC. But it is not clear that these measures are effective. During the COVID period of volatility, margins rose higher relative to pre-crisis rates than they did during the financial crisis of 2008 and as markets recovered, they have fallen faster.

It is important to note that the European Markets and Infrastructure Regulation (EMIR) sets anti-procyclicality requirements for CCPs subject to EU supervision. These requirements are the most



stringent in the world. However, the increases in margin rates at some EU CCPs demonstrates that even these were not adequate to sufficiently address procyclicality.

- The 25% erodible buffer is simply not large enough, and many CCPs lack a procedure to allow it to erode.
- Margin floors (set by a 10-year flat HVAR) were low, as the 2008 financial crisis rolled out of the lookback window in the year preceding the COVID crisis.

We also note that the quantitative analysis in Section 3.2.3 of the consultation shows that the reactivity of IM models differs quite substantially among CCPs. The chart in that section shows an extreme divergence in the reactivity of IM models in exchange-traded derivatives. It appears that two ETD CCPs experienced a 300% change in volatility, but their IM models produced dissimilar changes to IM rate – one at 100% and the other at 250%.

For all of these reasons, we strongly believe more work is needed to strengthen the controls against procyclicality. This work should cover not only standards to guide regulators but also disclosures of standardized metrics so that market participants can better assess and compare IM models.

For example, to address the shortcomings in IM requirements, we believe that:

- CCPs should utilize 5–10-year lookback periods – 1-year lookbacks are inadequate. In this context, it is worth noting that the report included a graph in Figure 14 showing significant
- variations across CCPs. In the ETD category, several CCPs had lookbacks in the 5–10-year range but the majority used significantly shorter lookbacks.
- Base margin calculations should consider and provide appropriate weightings to stressed periods relevant for the specific products. Strengthening base initial margin models reduces the need to rely on specific anti-procyclicality measures.
- Margin floors should be calibrated using stressed lookback periods.
- The process for setting IM requirements should be more transparent, with more consultation with market participants and more disclosure of CCP risk appetites.

Evaluating the responsiveness of non-centrally cleared IM models to market stresses

9. *Do you agree with the proposals in the report to evaluate the degree and nature of responsiveness of non-centrally cleared IM models to market stresses, remediation of IM shortfalls and the level of disclosure of non-centrally cleared IM model performance? Should any other aspects of non-centrally cleared IM models be included in this initiative?*

(no response).

10. *Are there any other important aspects not covered by the report which should also be prioritised for further international work or policy development?*

Move to Value-at-Risk (VaR)



As mentioned in the response to the first question above, at least four large CCPs are preparing to shift to Value-at-Risk-based models for calculating initial margin requirements. This shift reflects advances in risk measurement methodologies in the financial services industry, and the new margin models are expected to measure risk more accurately than the older generation. This is a positive development, but the new models are more complex than the SPAN-based systems that they will replace, partly because they measure risk by portfolio rather than position, and particularly because the calculations are based on a much larger number of scenarios.

SPAN is more than three decades old, and its approach is relatively crude, but it has one signal advantage – it generates a single number for each contract, and that number is updated only when there is a step-change in volatility. Many market participants have built internal systems that replicate SPAN and use these systems to estimate the margin requirements for their positions. VaR-based models, on the other hand, calculate margin requirements based on all the positions in a portfolio and update the calculations daily. This makes it more difficult for market participants to anticipate margin calls and manage their liquidity requirements accordingly.

We therefore believe that the consultation's recommendations on transparency will become even more relevant as VaR replaces SPAN. In particular, the complexity of VaR-based models will increase the need for CCPs to provide a) more transparency into how these models work and b) better tools for members and clients to estimate their margin requirements.

Equally important, the development of these models provides policymakers with an ideal opportunity to review the model parameters before they take effect, apply the lessons learned from the review of the Covid-related market turmoil, and strengthen the controls against procyclicality.

Consult on Margin Frameworks

We also believe that there is a general need to enhance clearing member participation in the development of margin frameworks. CCPs should institute a mechanism to solicit feedback, allow members to provide feedback on margin frameworks, and to ensure that this feedback process is working, they should demonstrate how they are taking that feedback into account.

CCP Access to Central Bank Accounts

FIA also recommends that global authorities consider and study the importance of CCP access to central bank accounts. This type of account is safest and most liquid place to hold client margin that is collected and paid on daily basis. During times of stress and increased market volatility, access to deposit accounts for all CCPs will improve liquidity across the cleared derivatives ecosystem and reduce the interconnectedness of the central counterparties and banks. It will also protect customers and end-users using the derivatives markets to hedge risk. Most central banks allow domestic CCPs to deposit local currency in central bank accounts. We strongly urge all central banks expand this access to non-locally domiciled CCPs. Some of them have enormous amounts of client collateral in the domestic currency of the central bank and those accounts should be allowed for all CCPs not just those within the jurisdiction of the central bank.



FIA looks forward to speaking with the global regulators about our view expressed in this consultation response. If you have any questions or would like to discuss, please contact Jacqueline Mesa at jmesa@fia.org or 202-772-3040.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'Jacqueline Mesa', is written over a light grey rectangular background.

Jacqueline Mesa
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FIA