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Via Electronic Submission

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Re: Streamlining variation margin in centrally cleared markets –examples of effective practices

Dear Sir/Madam,

Cboe Global Markets ("Cboe") appreciates the opportunity to provide comments on the above-referenced report (the "Report") on variation margin ("VM") in centrally cleared markets.[1] The Report outlines approaches to streamline VM practices across central counterparties ("CCPs") with the aim of fostering market participants' preparedness to meet above-average VM calls.

The Report is pertinent to Cboe's wholly owned clearinghouse affiliates including Cboe Clear Europe (CCE), a pan-European CCP licensed by the Dutch National Bank clearing cash equities, depositary receipts, ETFs, ETNs, ETCs and equity derivatives and Cboe Clear Digital, a CFTC-licensed designated clearing organization clearing derivatives on digital assets. While our VM call and collection practices are in line with industry practices and work well for our clients ("clearing members" or "CMs"),[2] we understand large, unexpected swings in VM can generally be a challenge for market participants.

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1 See Basel Committee on Banking Supervision (BCBS), the Committee on Payments and Market Infrastructures (CPMI), and the International Organization of Securities Commissions (IOSCO), February 2024, "Streamlining variation margin in centrally cleared markets – examples of effective practices," available at: https://www.bis.org/cpmi/publ/d221.htm

2 See "Cboe Clear Europe N.V. Clearing Rule Book," November 2023, available at, https://cdn.cboe.com/euroccp/resources/Cboe-Clear-Clearing-Rule-Book-effective-6-November-2023.pdf; also see Cboe Clear Digital, LLC Rulebook, Last Updated April 11, 2024, available at, https://www.cboedigital.com/wp-content/uploads/2024/04/Cboe-Clear-Digital-Rulebook-20240411.pdf

The Report attempts to highlight specific ways that CCPs can improve the predictability and manageability of VM calls for market participants, including by scheduling more frequent intraday ("ITD") margin calculations, offsetting VM calls against other obligations, and evaluating excess collateral and collateral eligibility policies among other examples.

Cboe supports IOSCO's efforts to improve market participants' preparedness, but we do not believe the highlighted practices will be "effective" in all instances. In fact, rote implementation of these practices across jurisdictions, CCPs, and asset classes, may in some instances introduce liquidity, operational, and legal burdens in addition to being unnecessary or in some cases unfeasible.

We understand and appreciate the report is not intended to introduce new standards or guidance. However, we urge IOSCO to continue to support CCPs' ability to design risk management practices that effectively manage the risks brought by their clearing members, particularly during periods of stress. Our responses to select items in the consultation are contained in the appendix to the letter.

We appreciate the opportunity to comment on this report.

Sincerely,

Angelo Evangelou
Chief Policy Officer
Cboe Global Markets

Appendix I

Frequency, scheduling, and timing

1. *Increasing the predictability of ITD margin calculations and collections to the extent practicable. This could be achieved by using, or increasing the frequency of, scheduled ITD margin calculations and collections where appropriate, after carefully considering the trade-off between the following:*

    a. *the increased operational burden associated with making more scheduled ITD calls, as well as the positive impact of using ad hoc calls when it is prudent; and*

    b. *the corresponding decrease in the probability of ad hoc ITD calls, as well as the positive impact on clearing members' operational readiness and financial capacity to meet the scheduled calls.*

2. *Giving participants sufficient time to manage the liquidity impact of an ITD call, while also considering the need to collect VM on a timely basis in order to mitigate the build-up of current exposures.*

Cboe Response

Although the idea of scheduled versus unscheduled VM calls may be considered synonymous with predictable and unpredictable VM calls, the concepts are not equivalent. Both scheduled and unscheduled VM calls may be unpredictably larger than expected if market movements are larger than expected. Notably, unlike initial margin (IM) requirements which may be more difficult to predict for CMs, VM requirements are easier to calculate and predict on any given day given they are simply a function of the change in price of a position.

If the goal is to better equip market participants to meet unexpected VM calls on days with large market movements, it is crucial to recognize that scheduling more frequent VM calls will not accomplish the stated objective. More frequent VM calls will simply reset or reduce the counterparty risk at the CCP.

Moreover, increasing the frequency of scheduled ITD margin collections across the board would be ill advised. For one, cleared products have different lifecycles, risk profiles, and regulatory frameworks which means in some cases only limited margin calls may be required (e.g., if the product has a short lifecycle). Additionally, ITD VM calls require more than simply exchanging funds more frequently. Each VM cycle requires substantial reporting, reconciliation, and back-office processes to settle. The added operational complexity to existing systems and processes would impact both CCPs and market participants. Certain non-financial firms and end users would need to set up new arrangements with their CMs and potentially face higher costs as CMs must provide a higher level of service.

Rather than increasing the frequency of VM calls, IOSCO could consider other ways to ensure market participants are better prepared for unexpected large VM calls (either scheduled or unscheduled), which at times may be necessary, through other means. Ultimately, CCPs should retain the discretion and flexibility to issue both scheduled and unscheduled ITD VM calls as needed.

We are supportive of the idea that market participants ought to have sufficient time to manage the liquidity impact of ITD calls. However, we believe our current time allowance of 1 hour, which is consistent with the standard practice, remains appropriate. From a financial stability perspective, it is well understood that uncovered exposure in form of VM losses must not accumulate at CCPs.

Offsetting, pass-through of VM, and excess collateral

> *3. Where allowed, practical and efficient, offsetting VM calls against other payment obligations, such as initial margin calls and product payment flows (eg coupons), in order to reduce liquidity demands on participants.*
>
> *4. Reviewing its operational practices based on an evaluation of the feasibility and the pros and cons of passing through ITD VM to mitigate the liquidity impact of ITD calls on participants.*
>
> *5. Subject to agreement with the CM or client and where legally and operationally feasible, allowing the use of excess collateral to meet ITD VM obligations.*

Cboe Response

We agree that, where possible, offsetting is important to enhance capital efficiencies. Whether IM and VM can be offset depends not just on the rules and practices of the specific CCP, but more so on the products cleared and the legal framework in which the CCP operates. CCE, for example, allows for offsets and use of excess collateral to meet obligations (i.e., if a CM's total margin requirement increases for any number of reasons but it is also owed VM because of mark-to-market gain in its portfolio). Per CCE's rules, the total margin requirement includes IM and VM, which means, by implication, that excess collateral for IM is used to cover a VM requirement intra-day. What's more, in the case of equities, CCE also allows for offsets between IM and VM requirements at end-of-day.[3] However, in derivatives and options markets – whether at CCE or Cboe Clear Digital – VM for futures and premium margin for options, the offsetting of margin is not always operationally feasible where there are various forms of collateral accepted.

Regarding the suggested pass-through of ITD VM, there are notable differences across CCPs, products, and jurisdictions that may make this more or less feasible. For instance, in the case of CCPs operating in multiple

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3 See https://cdn.cboe.com/euroccp/resources/Regulation-Acceptable-Collateral-effective-6-November-2023.pdf

currencies, it may be more challenging to pass through ITD VM to CMs owed a credit in the same currency as the payment from the CMs who owed the funds to the CCP.

CCP-to-CM transparency and engagement with participants

6. Providing information regarding the CCP's processes and timing for ITD VM calls in order to facilitate its participants' ability to predict and manage liquidity requirements. This could be achieved by clearly defining and making available to participants (through the CCP's rulebook or other relevant documentation) the following:

- a. *the circumstances and any related thresholds according to which the CCP may make ITD VM calls;*
- b. *the timing and relevant notice periods for its ITD VM calls;*
- c. *the CCP's processes and rules concerning the netting of payments across margin accounts for each type of margin call, where excess collateral can be used to meet VM requirements, and any other provisions which have an impact on the amounts to be called from CMs;*
- d. *and granular information to help CMs understand the composition of VM calls, which may include items such as: a unique identifier to track the call across the CCP's systems, an indicator of whether the call relates to initial margin/variation margin/default fund/rights of assessment/other, a house/client account indicator, underlying unique portfolio/account identifiers, details of any offsets netted against other payments (such as other margin calls, securities deliveries and receipts or coupon payments), a breakdown of the calculation which sets out the individual elements comprising the total, the forms of eligible collateral or the quantity and forms of eligible excess collateral which may be used to satisfy the call, and details of the deadline(s) for meeting the call*

7. Seeking feedback on the CCP's VM practices from its participants and other relevant stakeholders (eg through risk committees or other established mechanisms) in order to aid the CCP's assessment of the trade-off between managing its own risks and the interests of its participants.

Cboe Response

CCPs generally provide detailed margin model descriptions to facilitate its participants' ability to predict and manage liquidity requirements. Moreover, with respect to seeking feedback, Cboe's CCPs provide a large amount of information and transparency to CMs through CCP rulebooks, PQD disclosures, and ongoing conversations. Moreover, Cboe regularly engages with its CMs to ensure they have the information they need to understand and meet their obligations. In the EU we have sought consultative feedback on our rulebooks and have a Risk Committee comprised of CMs and customers of CMs in accordance with EMIR. Similarly, in the U.S., the Commodities Futures Trading Commission approved a final rule effective this year requiring derivatives clearing organizations (DCOs) to establish one or more risk management committees comprised of CMs and customers of CMs to consult on issues that could materially affect the risk profile of the DCO.[4]

Generally, Cboe believes the additional granular information suggested will not meaningfully improve the ability of market participants to meet ad-hoc VM calls, which is the central issue. The fact that CMs rarely fail to meet VM calls, even during periods of stress, speaks to the effective processes currently in place.

CM-to-client transparency

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4 See "Clearing Rules - consultation of rule book changes June 2023," available at, https://clear.cboe.com/europe/; also see "Governance Requirements for Derivatives Clearing Organizations," 88 FR 44675 (July 13, 2023).

8. Providing transparency to clients regarding the CM's processes and timing of ITD VM calls, which may facilitate clients' ability to predict and manage liquidity requirements. This could be achieved by clearly defining and making available to clients details of the following aspects of the VM calls it issues:

a. its practices and procedures for the calculation and collection/payout of VM;
b. schedules for timely payment that its clients may be required to meet;
c. c. its rules and practices concerning:
   i. the usage and forms of excess collateral eligible for meeting VM calls;
   ii. acceptance and transformation of non-cash collateral for the purposes of meeting VM calls;
   iii. netting arrangements across client accounts

Cboe Response

We are generally supportive of efforts to increase the level of transparency between CMs and their clients but note that the PFMI is not applicable to CMs and their relationship with their clients. While CCPs may provide clearing CMs with information, it is not a given that this information is passed on to end users to help them manage their own liquidity requirements.