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EFAMA views and recommendations on EMIR RTS CCP APC margin tools

The European Fund and Asset Management Association (EFAMA) welcomes the opportunity to respond to this important review of RTS 153/2013 and accompanying guidelines, in light of the procyclicality witnessed during the peak volatility of the Covid crisis. European CCPs already have standard anti-procyclicality tools in their rulebooks and this did lead to less volatile moves in margin in Europe versus other jurisdictions. Nevertheless, there remain important differences observed on CCP margin calls across CCPs which we believe can be addressed by improving the implementation of APC tools.

While the focus of this consultation is on the so-called Article 28 APC tools defined under EMIR RTS, we would like to reiterate the important antiprocyclical impact of allowing certain high quality securities to be admitted as collateral for the payment of variation margin calls. Allowing securities to be used to cover VM calls reduces the 'dash for cash' effect and the related risk of pro-cyclicality which is the consequence of having to sell securities to get cash for VM call payment, as observed during the height of the Covid crisis.

We believe that there is scope for sizing CCP IM requirements more conservatively while still preserving a careful balance between increased IM and managing volatility. This can be done using appropriate model assumptions to mitigate the potential for future procyclical initial margin moves. Finally, we would like to stress the importance of aligning any reforms with ongoing work at IOSCO level on margining practices.

Question 1: Do you agree that CCPs should be able to explain and justify their APC tool choices?

It is important to require CCPs to explain and justify their APC tool choices. The choice of tool should demonstrate the most impact in terms of antiprocyclicality, and be risk based, i.e., dependent on the underlying risk of the contracts and markets cleared, and not be driven by considerations at individual CCP level of the least difficult tool to implement.

Question 2: Do you agree that CCPs should define their own APC thresholds for margin changes based on their risk appetite/tolerance? Should the RTS explicitly require that CCPs seek the advice of the risk committee, when setting or reviewing its APC policies, including defining the risk appetite?

Yes, we agree that CCPs should define their APC thresholds for margin changes based on their own risk appetite/tolerance, but also the risk tolerance of its users, including end investors, the risk of the products cleared, and its membership composition and the risk they bring. We agree with the requirement to seek

the advice of the risk committee as this reflects a solid governance process. And while clearing members and end-clients are already represented on Risk Committees, this process could be improved in two ways. The role of the Risk Committee could be strengthened. It is not clear today to the extent to which advice of the Risk Committee is taken on board when considering changes to risk models and default procedures. In addition, in order for the Risk Committee to extract the full benefit of its diverse composition, discussions should not be limited to those of a highly technical nature, but also broadened out to address concerns that clearing members and end-clients might raise. Where feedback from members is not taken on board, the Risk Committee should make this transparent and provide rationale to members in a timely manner.

The CCP should also justify its choice of APC tools **to other relevant stakeholders outside of the Risk Committee**, i.e. end clients without Risk Committee membership, and not just to regulators and the Risk Committee. Providing this transparency is important for all users because it will enable market participants, including end clients, to better predict CCP IM requirements which would inherently enhance liquidity preparedness.

Question 3: Do you agree with ESMA's proposal to draft a new Article 28a? What other requirements should ESMA consider introducing in relation to the CCP APC policies and procedures?

We agree in principle with the new Article 28a.

CCPs generally believe they provide tools to predict margin while intermediaries and clients often conclude that those tools are not sufficient for them to predict IM changes. CCPs are disclosing to the market what they believe is sufficient but the market requires more granular information.

It was evident from the recent IOSCO report on CCP margins that the degree and quality of CCP margin transparency is wide-ranging, and the level of detail or lack thereof varies by CCP.¹

We recommend that regulators share the margin model disclosures provided by individual CCPs, if allowable, or at the very least, comment on the level of detail provided by CCPs based on size or jurisdiction. This information would be useful for market participants in preparing for the next market stress.

To be clear, we do not suggest that CCP IM models need to be homogenous. The mechanism to facilitate such credible challenge to CCP IM models is through enhanced risk governance. CCPs' governance arrangements should require them to have a formal process to obtain, consider and address market participants feedback on any changes that materially affect the risk profile of the CCP particularly as it relates to risk methodologies and financial safeguards. Such feedback should take place prior to CCPs making any formal filing with the relevant regulators and must be disclosed to regulators. This would provide relevant authorities with important market views that could help improve overall resilience of CCPs. We also recommend regulatory monitoring of CCPs risk models to ensure margin is sufficient in a continuously evolving financial market.

We sometimes hear CCPs say that they are unwilling to fully disclose margin model details because they consider the models proprietary and protected by intellectual property rights. We do not believe margin models should be viewed in such a manner since margin is a cornerstone of risk management and could have implications for financial stability. We believe standard setters need to determine if global financial stability is better supported by compelling margin model mechanics to be more broadly available.

We appreciate governance, disclosure, and transparency are not explicitly addressed in this consultation as ESMA wants to wait for the broader international work. However, we believe that CCPs' governance arrangements should require them to have a formal process to obtain, consider and address market participants feedback on any changes that materially affect the risk profile of the CCP particularly as it relates to risk methodologies and financial safeguards, including the usage of APC tools. Such feedback should take place prior to CCPs making any formal filing with the relevant regulators and must be disclosed to regulators. This would provide relevant authorities with important market views that could help improve overall resilience of CCPs.

¹ See IOSCO October 2021 report on Review of Margining Practices [CR04/2021 Review of margining practices \(iosco.org\)](https://www.iosco.org/publications/working-papers/Pages/CR04/2021%20Review%20of%20margining%20practices.aspx)

Ideally, disclosures should be standardised, with a significant level of detail included. The disclosed information should further be audited. We also reiterate the importance of the role of the Risk Committee and its members in providing risk oversight, providing advice to the Board, and a formal mechanism through which all market participants can receive feedback on changes to CCP risk models.

We look forward to working with ESMA on this matter when the time comes and the international work is finalised.

Question 4: Do you agree with ESMA's proposed amendment to require CCPs to assess margins based on quantitative metrics in the context of procyclicality?

Yes, we agree with ESMA that any APC tools chosen should be backed up by quantitative metrics and disclosed in detail to all users. Here again we stress the importance of improved transparency and predictability on CCP margin models for market participants, to allow for better preparedness and responsiveness in times of market stress. These disclosures should be standardized to allow users to compare the performance of APC tools across jurisdictions and CCPs. Perhaps this could be an area where global standard setters can work together to establish regulation to ensure a globally coordinated approach. In this context, it is worth referencing a Bank of England study on the cost benefit analysis of APC tools.²

Question 5: Do you agree with ESMA's proposal to introduce these three dimensions? Should these be mandatory or optional? How do these compare to the quantitative metrics that CCPs currently consider in practice?

Of the three dimensions, we would especially draw attention to conservativeness and stability. Again here we reiterate the point that margins should not be used as competitive tool. Margin is a core component of risk management, as well as CCP resiliency, and increased transparency will benefit the market.

Considering the lessons learned from March 2020, we recommend policymakers ensure CCPs size IM requirements more conservatively using appropriate model assumptions to mitigate the potential for future procyclical IM moves. Specifically, IM models should have more conservative and sound margin periods of risk, look back periods and margin offsets, and margin add-ons should be more transparent and defensible.

Question 6: Do you agree with ESMA's proposal to include in the RTS a requirement for CCPs which clear products whose price/yield can vary significantly to perform the assessment of the procyclicality of its margin model across different price/yield levels?

Question 7: Do you agree with ESMA's proposal to introduce into the RTS the requirement on CCPs to calculate APC margin requirements at all material risk factors?

Question 8: Do you agree with ESMA's proposal to consider the impact that the risk factor change will have on the margin, including for products with non-linear dependence on risk factors?

Question 9: Do you agree with ESMA's proposal on how to apply the APC options for different risk factors?

Question 10: Do you agree with ESMA's proposal that CCPs using the APC tool under Article 28(1)(a) should develop policies and procedures detailing the use of the buffer and its replenishment as included in the draft RTS test? Are there other items that the procedures should consider in the RTS?

Question 11: Do you agree that CCPs should set predefined thresholds but also be granted a degree of discretion when triggering the exhaustion of the margin buffer subject to appropriate governance arrangements?

² [A CBA of APC: analysing approaches to procyclicality reduction in CCP initial margin models | Bank of England](#)

Question 12: Do you agree with ESMA's proposal to set the minimum buffer to 25% while requiring CCPs to assess if a higher buffer would be needed and justify / regularly check the appropriateness of their choice?

Yes, we agree there should be a regulatory minimum for the buffer. Given the level of IM margin volatility experienced in March 2020, those CCPs using this particular APC tool should examine where a larger buffer, above the 25% regulatory minimum, is warranted based on its procyclicality target. We think such an approach is more supportive of long-term financial stability .

Question 13: Are there cases where ESMA's proposal to modify Article 28(1)(a) RTS would present difficulties for CCPs in practice?

Question 14: Do you agree that CCPs should consider the extreme market movements from the historical stress scenarios identified under Article 30 of the RTS?

Yes, the look back period determines how far back in history a margin model will look to inform predictions of future market moves. Current guidance suggests that the sample period be "appropriate" for each product, though there is no additional guidance on how to define "appropriate." As a result, we believe some margin models may not capture relevant market stresses. we see value in a longer look-back period, i.e., such as one that includes the Global Financial Crisis.

Question 15: Do you agree with ESMA's proposal that CCPs should also consider including the extreme market movements from the potential future stress scenarios identified under Article 30(2)(b)?

Question 16: Do you agree to require that CCPs ensure the set of extreme market movements includes an adequate number of extreme market movements for all margined products, including the ones that could expose it to the greatest financial risks?

Question 17: Do you agree with ESMA's proposal not to include a specific time restriction on when CCPs should add new stress observations in the set of extreme market movements used for the purpose of the APC tool, but instead add a provision to consider reviewing more frequently taking into account the procyclical effects from such revision?

Question 18: Do you agree with ESMA's proposal that CCPs should calculate the stress margin using the same model and parameters in compliance with Articles 24, 26 and 27, except for the time horizon under Article 25?

Question 19: Do you agree that for the purpose of calculating the stress margin to be used for the calibration of the APC tool, CCPs should recompute the stress margin at least daily and shall avoid using scaling techniques that can affect the severity of observations or calculated stressed margin?

Question 20: Do you agree with ESMA's proposal to include the provision to allow CCPs to temporarily increase the weight that is applied to the unadjusted margin and equally reduce the weight applied to the stress margin? Should there be a time limit on this provision?

Question 21: Are there cases where ESMA's proposal to modify Article 28(1)(b) RTS would present difficulties for CCPs in practice?

Question 22: Do you agree with ESMA's proposal that the margin floor should include stress market movements in addition to the 10-year lookback period? Do you agree with the methodology used to identify these extreme market movements?

Question 23: Do you agree that the margin floor should be calculated in compliance with Articles 24, 26 and 27 of the RTS?

Question 24: Do you agree that the margin floor should be recomputed at the same frequency than the baseline margin requirements?

Question 25: Do you agree that, when calculating the margin floor, CCPs shall avoid using scaling techniques that can affect the severity of observations, extreme market movements or calculated floor margin?

Question 26: Are there cases where ESMA's proposal to modify Article 28(1)(c) RTS would present difficulties for CCPs in practice?



ABOUT EFAMA

EFAMA, the voice of the European investment management industry, represents 28 member associations, 58 corporate members and 24 associate members. At end Q1 2021, total net assets of European investment funds reached EUR 19.6 trillion. These assets were managed by more than 34,600 UCITS (Undertakings for Collective Investments in Transferable Securities) and almost 29,600 AIFs (Alternative Investment Funds). At the end of 2020, assets managed by European asset managers as investment funds and discretionary mandates amounted to an estimated EUR 27 trillion.

More information is available at www.efama.org

Contact

Susan Yavari

Regulatory Policy Advisor

susan.yavari@efama.org | +32 2 513 39 69