April 13, 2018

U.S. Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549
Attn: Mr. Eduardo Aleman, Assistant Secretary

RE: FILE NUMBER SR-FICC-2018-001

Dear Mr. Aleman:

Ronin Capital, LLC ("Ronin") appreciates the opportunity to respond to a comment letter submitted by the Fixed Income Clearing Corporation ("FICC") to the Securities and Exchange Commission (the "Commission") on March 19, 2018 (the "FICC Letter").[1] We intend to address several topics mentioned in the FICC's response to our original comment letter which was submitted to the Commission on February 22, 2018 (the "Ronin Letter").[2] Ronin continues to believe that the proposed rule change, which modifies the Required Fund Deposit ("RFD") Calculation in the Government Securities Division ("GSD") Rulebook, imposes an unnecessary competitive burden on smaller, non-bank GSD members. Ronin requests that the Commission rejects this proposed rule change in favor of directing the FICC to develop a risk-based margin system that more accurately and fairly reflects the particular risks present in the U.S. Treasury market.

Accuracy of FICC's Assumed Three-Day Liquidation Period

Rule 17Ad-22(e)(6)(vi)(B) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), requires the FICC to ensure that "back-testing practices are appropriate for determining the adequacy of the covered clearing agency's margin resources."[3] In the FICC Letter, the claim is made that the "three-day liquidation period is an accurate assumption of the length of time that it would take to liquidate or hedge a portfolio given the volume and types of securities that can be found in a Netting Member's portfolio at any given time."[4] Regardless of portfolio size, the FICC claims that hedging and/or liquidating the portfolio of a defaulting GSD Member would take three days. Clearly this assumption is overly simplistic. A portfolio worth several hundred billion USD would certainly take longer to liquidate or hedge than a small portfolio worth several hundred million USD. The statement that "idiosyncratic exposures"[5] somehow make it as difficult to liquidate a small portfolio of high-quality liquid assets ("HQLA") versus that of an extremely

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[1] See Letter from Timothy J. Cuddihy, Managing Director, The Depository Trust & Clearing Corporation ("DTCC") to Robert W. Errett, Deputy Secretary, Securities and Exchange Commission (March 19, 2018).
[2] See Letter from Robert Pooler, CFO, Ronin Capital, LLC to Robert W. Errett, Deputy Secretary, Securities and Exchange Commission (February 22, 2018).
[3] See 17 CFR 240.17Ad-22(e)(6)(vi)(B)
[4] FICC letter p. 3
[5] FICC letter p. 4

large portfolio of HQLA is not credible under any serious scrutiny.[6] And yet, some differentiation should be made with respect to portfolio size when undertaking "appropriate back-testing practices" as demanded by the Exchange Act. If the largest portfolios only require three days to liquidate, it is intuitive that smaller portfolios would require a shorter amount of time. This is a critical point, because back-testing violations during the U.S. presidential election of 2016 are being used as the rationale for changing the RFD Calculation for all GSD Netting Members, regardless of the sizes of their respective portfolios. When determining the adequacy of each Netting Member's RFD as required by the Exchange Act, it seems counterintuitive to assume that all portfolios have the same liquidity risks irrespective of size. The GSD only clears HQLA. If multiple days are needed to hedge and/or liquidate a portfolio of HQLA, certainly only the largest portfolios subject the FICC to idiosyncratic risk.

An Outdated Cross-Margin Agreement

Rule 17Ad-22(e)(6)(i) of the Exchange Act requires the FICC to establish a risk-based margin system that produces margin levels that are "commensurate with, the risks and particular attributes of each relevant product, portfolio, and market."[7] While it is true that centralized clearing in the U.S. Treasury market is fragmented, there is an existing cross-margin agreement between the FICC and the CME which allows risk-based offsets between the two clearing agencies. Thus, claims by the FICC that it "cannot benefit from offsets of such positions in the event that a Netting Member defaults"[8] should not apply with respect to assets covered under this cross-margin agreement (CME interest rate futures and options). Differentiating hedged risk from outright risk is exactly what this cross-margin agreement addresses - it enables the participating clearing agencies to differentiate hedged portfolios from those that are not hedged. The cross-margin agreement that the FICC has in place with the CME addresses issues with portfolio visibility via the sharing of information. Risk of loss is mutualized via a formalized cross-margin guaranty - the details of this guaranty are available in the GSD Rulebook.[9] Unfortunately, this cross-margin agreement with the CME has not been maintained and is woefully out of date. The existing cross-margin agreement merely needs an update to provide true cross-margin relief for all GSD Netting Members while enabling the FICC to differentiate real risk from merely the appearance of risk. Ronin believes it is discriminatory that this cross-margin agreement has been allowed to languish while at the same time the FICC is requiring more margin from all of its Netting Members to mitigate risks identified via a flawed back-testing process.[10] Because this cross-margin agreement has been allowed to languish, Ronin is forced to post more margin than is necessary and consequently has greater risk-of-loss if one of the largest Netting Members were to default and margin posted to the Clearing Fund were to prove inadequate.

[6] The FICC (and other clearing agencies) allow clearing members to post HQLA instead of cash in order to meet their margin requirements. If idiosyncratic risk associated with HQLA under a default scenario is truly concerning, clearing members should not be allowed to post HQLA as a means of meeting their margin requirements.
[7] See 17 CFR 240.17Ad-22(e)(6)(i)
[8] See FICC Letter p. 4
[9] http://www.dtcc.com/~/media/Files/Downloads/legal/rules/ficc_gov_rules.pdf
[10] The assumed three-day liquidation assumption is a critical flaw in the current back-testing practice employed by the FICC. However, a much-needed update to the cross-margin agreement might also diminish the perceived need to accumulate more assets in the Clearing Fund. This is particularly true because of a lack of cross-margin relief in the long end of the curve, which tends to be more volatile historically and consequentially requires more margin from Netting Members.

Impact of the Proposed VaR Methodology on the Required Fund Deposit

The FICC states that it has "invested a significant amount of time helping the membership understand the impact of the proposal on their Required Fund Deposit amounts."[11] The problem with the current approach is the heavy reliance on parallel and historical studies - GSD Members lack the necessary tools to conduct their own scenario analysis. When trading activity or market conditions deviate from assumptions made under the various studies conducted by the FICC, Netting Members are forced to react rather than proactively manage capital needs. It is significantly more difficult to manage the capital needs of a business when a clearing agency does not provide appropriate tools for calculating projected margin requirements in advance.

Ronin does credit the FICC with finally taking the initiative to develop an interactive Margin Calculator for GSD Members. Unfortunately, this calculator won't be ready until at least 2019. This delay results in a dependency on FICC-supplied impact studies and parallel comparisons, which only provide a limited and inadequate view of the impact of the proposed changes. A pertinent example of the inadequacy of this current approach is demonstrated by examining the studies conducted by the FICC prior to the implementation of the Margin Proxy in 2017. The first impact study that Ronin received from the FICC prior to the approval of the Margin Proxy showed an extremely benign impact (~1% increase) over the two-month duration of FICC's initial study. At our request, the FICC provided a longer study covering the entire prior year (2016) which showed a marked average increase of 21% to our RFD obligation. Yet, these studies greatly minimized the actual impact of the Margin Proxy on our business. During the first quarter of 2018, the Margin Proxy has required Ronin to post 57% more margin on average than would have been required prior to the implementation of the Margin Proxy. This includes a single day maximum increase of 158% during the quarter. During the 4th quarter of 2017, Ronin experienced a single day increase of 238% attributable to the Margin Proxy. Prior to its implementation, Ronin complained about a lack of transparency in a comment letter (the "Margin Proxy Letter").[12] Little has changed in the way the FICC communicates such impactful changes. We still believe the FICC does not provide Netting Members with the proper tools to proactively understand changes in RFD obligations - this proposed rule change is another example of a flawed disclosure process.

Supplying the Wrong Data

As detailed in our Margin Proxy Letter, Ronin claimed the implementation of the Margin Proxy would likely impart an unfair competitive burden on our firm.[13] The back-testing failure of the Clearing Fund as a whole (following the U.S. presidential election) was cited as the rationale for proposing and implementing the Margin Proxy over an accelerated time frame. Due to the abbreviated nature of the rule approval process, we don't believe the Commission had the time or ability to analyze the Margin Proxy for discriminatory impact. The Commission was not provided with data at the time of the Margin Proxy rule filing[14] and therefore was likely unable to determine whether the Margin Proxy was discriminatory in its application. The impact of the Margin Proxy on our business, as detailed above, is certainly not benign. This is

[11] See FICC Letter pp. 2-3
[12] See Letter from Robert Pooler, CFO, Ronin Capital to Eduardo A. Aleman, Assistant Secretary, Securities and Exchange Commission (February 24, 2017).
[13] See Margin Proxy Letter pp. 9-10
[14] No public mention was made of data being provided as part of the Margin Proxy rule proposal. This differs from the current proposal whereby data provided to the Commission was publicly disclosed as part of the rule filing.

particularly concerning, since we believe the rationale for the need to increase assets in the Clearing Fund was based on a flawed and discriminatory back-testing process.

In order to prove that the proposed rule (implementation of the sensitivity VaR model) is not discriminatory in its impact, the FICC publicly released a table in the FICC Letter detailing the impact of the proposed rule change on the RFD obligations of its Netting Members.[15] Ronin does not believe this data represents the true impact of the proposed changes. This is simply because the FICC is referencing data that already includes the Margin Proxy. Ronin believes it is important to remember that the Margin Proxy was instituted as a temporary and emergency change to the RFD calculation. The Margin Proxy is simply a backup VaR model - pressed into service because the sensitivity VaR model was not ready. When examining the proposed rule for discriminatory impact, it is important to compare the proposed sensitivity VaR model to the Current Volatility Calculation *without* the Margin Proxy. After all, the goal of the Margin Proxy was to immediately increase assets held in the Clearing Fund, so that the entire Clearing Fund met its historical back-testing requirements. The Margin Proxy was never examined for discriminatory impact. Using the Current Volatility Calculation with the Margin Proxy as the base case overlooks the discriminatory impact the Margin Proxy has already imposed on many Netting Members.

As required by the Exchange Act, the FICC must ensure that any rule changes do not "impose any burden on competition not necessary or appropriate." Ronin believes the FICC's proposed sensitivity VaR model, as applied, fails to meet these standards and imposes an unnecessary competitive burden on some of its Netting Members. Furthermore, we claim that the FICC does not provide the Commission with the proper data to ensure that this proposed rule change does not impart an unnecessary burden on competition. This is simply because the data provided by the FICC compares the impact of the proposed rule to RFD data that already includes the Margin Proxy. The following example shows a scaled version of both the Margin Proxy and the proposed rule change (Sensitivity VaR) on our RFD over a two-week span in January 2018:

	Current Vol Calculation	Margin Proxy	% Change	Sensitivity VaR	% Change
1/31/2018	75.23	124.69	65.74%	100.34	33.38%
1/30/2018	72.17	107.99	49.63%	90.09	24.82%
1/29/2018	75.44	116.57	54.53%	96.00	27.26%
1/26/2018	81.97	127.70	55.79%	105.27	28.43%
1/25/2018	78.84	123.45	56.58%	99.84	26.63%
1/24/2018	94.98	142.13	49.65%	128.57	35.37%
1/23/2018	95.85	144.49	50.74%	128.38	33.93%
1/22/2018	87.69	137.40	56.68%	113.06	28.93%
1/19/2018	87.30	137.38	57.37%	116.49	33.43%
1/18/2018	90.65	137.18	51.33%	116.71	28.75%
1/17/2018	92.43	135.58	46.69%	121.99	31.98%
1/16/2018	90.75	153.81	69.48%	133.39	46.98%
1/12/2018	100.00	170.19	70.19%	152.47	52.47%

While the Sensitivity VaR model shows a decrease in our RFD obligation when compared with the punitive impact of the Margin Proxy, the overall increase in our RFD obligation is non-trivial under both VaR model changes. By only providing data which already includes the Margin Proxy, we believe the FICC may

[15] FICC Letter p. 3

mislead the Commission into thinking the proposed rule change is benign simply because of the path dependency associated with first implementing the Margin Proxy as an emergency measure prior to replacing it with the sensitivity VaR model. Anecdotal evidence from informal discussions with other smaller non-bank Netting Members has given us the impression that smaller Netting Members have been disproportionately impacted by the various changes the FICC has made to its RFD calculations. We believe this imposes an unnecessary competitive burden on smaller Netting Members, particularly because these members maintain smaller portfolios which could more easily be liquidated or hedged in less than the arbitrarily defined three-day liquidation period. Ronin is concerned that smaller Netting Members are being forced to bear the brunt of proportional increases in their respective RFD obligations to correct back-testing violations for the Clearing Fund as a whole. And yet, the need for these changes is driven by back-testing practices that assume a uniform three-day liquidation period for all Netting Members. It seems intuitive that the largest portfolios impose the greatest idiosyncratic risk. It is not clear why smaller firms seem to be disproportionately bearing the cost of changes made to increase overall assets held in the Clearing Fund. As pointed out in our comment letter for the Margin Proxy, Ronin is already posting many multiples of our internal VaR to the FICC as margin.[16] Posting more margin only serves to expose us to idiosyncratic liquidity risk if one of the largest Netting Members defaults. Ronin claims this imposes a competitive burden and is discriminatory, given our higher cost of capital. We believe it is imperative that the Commission is provided with the proper data to determine whether the proposed rule change is indeed discriminatory.

Adding a Stressed Period

It is intuitive that fewer back-testing violations will occur when more margin is required from clearing members. However, a decline in back-testing violations does not prove that the back-testing process is fair or that margin levels are appropriate for the risks of the U.S. Treasury market. Requiring more margin than is necessary or required by the Exchange Act discriminates against firms with higher costs of capital. This is particularly true when the liquidity needs of the largest Netting Members determine the back-testing practices which are applied uniformly to all Netting Members. The FICC is only required to meet the 99% standard. Adding an additional stressed period employs statistical bias and unnecessarily raises the standard beyond that required by the Exchange Act.

Conclusion

Smaller Netting Members are disproportionately bearing the burden of increases to their RFD obligations even though idiosyncratic risk related to the liquidation of HQLA is correlated with portfolio size. The assumption of a three-day liquidation period for all Netting Members is clearly discriminatory. Increasing RFD obligations based on this assumption, which unfairly targets smaller firms, imparts an unnecessary competitive burden. Ronin contends the FICC should develop a new back-testing plan which fairly attributes a longer period of time for hedging or liquidating portfolios that are larger. By doing so, the FICC could then develop a VaR model which fairly imparts RFD obligations on Netting Members that pose greater risks to the FICC, rather than targeting smaller Netting Members with disproportionate increases in their RFD obligations to make up for a Clearing Fund shortfall. In addition, modernizing the cross-margin agreement with the CME might also enable the FICC to differentiate outright risk from hedged risk and

[16] See Margin Proxy Letter p. 10

thus reduce the number of perceived back-testing violations. In this manner, the FICC might be able to fairly burden the Netting Members imparting true risk to the FICC with increases to their RFD. This would avoid exposing Netting Members with hedged portfolios to greater potential risk of loss if assets held in the Clearing Fund were proven to be inadequate under a Netting Member default scenario.

In conclusion, we request that the Commission reject FICC's proposed rule change in favor of developing a risk-based margin system that more accurately and fairly reflects the particular risks present in the U.S. Treasury market. We thank the Commission for considering our comments. If you should have any questions, please contact me by email at [redacted] or by telephone at [redacted].

Very truly yours,

Robert E. Pooler, Jr.
Chief Financial Officer
Ronin Capital, LLC