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By Electronic Mail (rule-comments@sec.gov)

Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: Response to Comment Letters Filed with the Commission Regarding File No. SR-FICC-2020-017 – Exchange Act Release No. 90568 (the "Rule Filing") and SR-FICC-2020-804 – Exchange Act Release No. 90834 ("Advance Notice" and collectively with the Rule Filing, the "Filings") by Fixed Income Clearing Corporation

Dear Ms. Countryman:

Fixed Income Clearing Corporation ("FICC")[1] appreciates the opportunity to respond to the comment letters submitted by the Independent Dealer and Trader Association ("IDTA") and the Mortgage Bankers Association ("MBA"),[2] American Securities Association ("ASA")[3] and SIFMA[4] (each, a "Commenter;" collectively, the "Commenters") to the Securities and Exchange Commission ("Commission")[5] relating to a proposal (the "Proposal") by FICC to amend the

[1] FICC is a clearing agency registered with the U.S. Securities and Exchange Commission ("Commission") pursuant to the Securities Exchange Act of 1934, as amended (the "Exchange Act"). FICC is comprised of two Divisions — the Government Securities Division ("GSD") and the Mortgage-Backed Securities Division ("MBSD"). GSD provides central counterparty services to its customers with respect to the U.S. government securities market, and MBSD provides such services to the U.S. mortgage-backed securities market. FICC has been designated as a systemically important financial market utility ("SIFMU") by the Financial Stability Oversight Counsel pursuant to Section 805 of Title VIII of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank") in recognition of FICC's critical role in the national financial infrastructure. FICC is a subsidiary of The Depository Trust & Clearing Corporation ("DTCC"), which is a user-owned, user-governed holding company for FICC, two other registered clearing agencies and SIFMUs regulated by the Commission, and a number of other companies that provide a variety of post-trade processing and information services. FICC and DTCC's other registered clearing agencies provide critical infrastructure for the clearance and settlement of securities transactions in the U.S.

[2] Letter from James Tabacchi, Chairman, IDTA and Mike Fratantoni, Chief Economist, Senior Vice President, MBA, dated January 26, 2021 ("IDTA/MBA Letter").

[3] Letter from Cristopher A. Iacovella, Chief Executive Officer, ASA, dated January 28, 2021 ("ASA Letter").

[4] Letter from Christopher Killian, Managing Director, Securitization, Corporation Credit and Libor, SIFMA, dated January 29, 2021 ("SIFMA Letter").

[5] Comment letters are available at https://www.sec.gov/comments/sr-ficc-2020-017/srficc2020017.htm.

FICC MBSD Clearing Rules ("MBSD Rules")[6] set forth in the Filings to modify the calculation of the MBSD VaR Floor to incorporate a Minimum Margin Amount ("MMA").[7] FICC's comments to issues raised by the Commenters with respect to the Proposal are set forth below.[8] Where Commenters raised similar issues, they are addressed collectively.

I. Background

The Clearing Fund is designed to maintain an appropriate amount of financial resources from each Clearing Member to support FICC in the event that it needs to step in and complete settlement on their behalf. The VaR Charge is calculated using a risk-based methodology that is intended to capture the market price risk associated with the securities in a Clearing Member's portfolio. The methodology uses historical market moves to project the potential gains or losses that could occur in connection with the liquidation of a defaulting Clearing Member's portfolio. FICC requires that the Clearing Fund is sized to cover observed TBA price changes with a 99% confidence level.

In March 2020, the Federal Reserve began a series of quantitative easing steps that included rate cuts and bond buying programs. These steps resulted in price appreciation and significantly shorter TBA durations. Amid the high uncertainty over monetary policy and the voluntary and involuntary prepayment trends, price volatility continued and TBA volumes began to migrate to lower coupons. TBA risk model assumptions were challenged by these evolving market events, new borrower relief programs, and increasing unemployment.

FICC's sensitivity value-at-risk ("VaR") model can be decomposed by risk factor to assess the contribution or explanation that each risk factor change has on observable TBA price moves. The unexplained mark-to-market ("MtM") is the difference between the actual MtM and sensitivity-based VaR projection. The unexplained MtM will be small when the underlying risk factors are highly correlated with the TBA price changes. The unexplained MtM will be higher when prices are influenced by risk factors that are not fully captured in the sensitivity-based approach. FICC backtests its sensitivity VaR model daily to assess its model performance and material unexplained daily MtM. Prior to the COVID-19 period, the MBSD backtest results for January 2020 were 99.3% indicating that the daily Required Fund Deposits covered the observed MtM moves to a high degree of confidence over the previous 12-months.

Like many market participants, it became clear that the Required Fund Deposits required an additional component to deal with the uncertainties emanating from the COVID-19 period. Given that our VaR model is data dependent, it takes time to assess, calibrate, and test when changes are required. While FICC's risk factors are typical TBA attributes, the analytics

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[6] Capitalized terms not defined herein are defined in the MBSD Rules, available at https://dtcc.com/~/media/Files/Downloads/legal/rules/ficc_mbsd_rules.pdf.

[7] File No. SR-FICC-2020-017 and File No. SR-FICC-2020-804.

[8] FICC also reviewed the following additional comment letters from the Commenters relating to the Proposal – (i) Letter from Christopher Killian, Managing Director, Securitization, Corporation Credit and Libor, SIFMA, dated February 23, 2021; (ii) Letter from James Tabacchi, Chairman, IDTA and Mike Fratantoni, Chief Economist, Senior Vice President, MBA, dated February 23, 2021 and (iii) Letter from James Tabacchi, Chairman, IDTA, dated February 23, 2021. FICC does not believe that these letters raise any new substantive issues from the earlier comment letters which require a further response other than as included in this letter.

supporting them rely on interest rate assumptions, mortgage attributes, and macroeconomic variables. The 2020 events challenged relationships such as delinquencies that are historically strongly correlated with the U.S. unemployment rate. Proper analysis takes time and data to develop appropriate assumptions.

Market prices do not always wait for the analysis. Looking forward, the analysis will continue to be challenged as TBA supply remains strong, prepayment risk is elevated, and mortgage-backed security demand is uncertain. The Federal Reserve purchase program continues to support market prices. A change in the Federal Reserve purchase program could introduce TBA price volatility that is not typically accounted for in a sensitivity VaR model. Therefore, it is important to have a Clearing Fund component that supports the VaR calculation using a transparent calculation that measures the price volatility in each Clearing Member's clearing portfolio using observable TBA benchmark prices.

As described in the Proposal, FICC's MBSD VaR margin calculation methodology did not respond effectively to the recent levels of market volatility and economic uncertainty, and FICC's VaR model did not backtest above the target 99% confidence level for the period beginning in March 2020 through the beginning of April 2020. Pursuant to the Filings, FICC proposes to incorporate the MMA into the VaR Floor to enhance the MBSD VaR model performance and improve the backtesting coverage during periods of heightened market volatility and economic uncertainty. FICC believes that the Proposal will increase the margin back-testing performance during periods of heightened market volatility by maintaining a VaR Charge that is appropriately calibrated to the observable market price volatility.

II. Concerns Stated by Commenters and FICC Response

Burden on Competition/Disproportionate Effect on Certain Clearing Members and Impact on the Market

Commenters expressed concerns that the Proposal imposes an unnecessary burden on competition and may have a disproportionate effect on small to mid-sized broker dealers.[9]

In the Rule Filing, FICC addressed the concerns that Proposal would impose a burden on competition that is not necessary or appropriate. As noted in Item 4 of the Rule Filing (Clearing Agency's Statement on the Burden on Competition) impact studies have indicated that on average Clearing Members would have had an increase in their VaR Charge of approximately 42% during the impact study period referenced in the Rule Filing and that the Proposal could impose a burden on competition. In addition, the Rule Filing makes it clear that Clearing Members may be affected disproportionately by the Proposal because Clearing Members with higher percentages of higher coupon TBAs in their portfolios are more likely to be impacted. As discussed in the Rule Filing, FICC believes that any burden on competition is necessary and appropriate in compliance with 17A(b)(3)(I) of the Exchange Act.[10]

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9 IDTA/MBA Letter p. 2 - 4; SIFMA Letter p. 4; ASA Letter p. 2.

10 15.U.S.C. 78q-1(b)(3)(I).

The methodology for computing the MMA under the Proposal does not take into consideration the Clearing Member's size or overall mix of business relative to other Clearing Members, and, therefore, does not discriminate against Clearing Members or affect them differently on either of those bases. Any effect the Proposal would have on a particular Clearing Member's margin requirement is solely a function of the market price risk posed to FICC by the Clearing Member's activity at FICC – firm size or business model is not pertinent to the assessment of that risk.

FICC is required to manage clearance and settlement risk presented by each Clearing Member with respect to the particular securities products it transacts through the system by, among other things, collecting margin sufficient to cover the market price risk with respect to those unsettled TBA obligations with a high degree of confidence.

Any increase in the Required Fund Deposit as a result of the Proposal for a particular Clearing Member would be in direct relation to the specific risks presented by such Clearing Member's portfolio, and each Clearing Member's Required Fund Deposit would continue to be calculated with the same parameters and at the same confidence level. Therefore, Clearing Members with portfolios that present similar risks, regardless of the type of Clearing Member or business model, would have similar impacts on their Required Fund Deposit amounts.

The Proposal is designed to calculate the exposure in each portfolio using observable TBA indices to benchmark the FICC VaR estimate to confirm that the VaR estimate covers the portfolio risk level under the current market conditions. The Proposal is intended to ensure that each Clearing Member has an appropriate VaR Charge in the event that the VaR model yields too low a VaR Charge for such portfolios. By identifying and providing for appropriate VaR Charges, adding the MMA to the VaR Floor would help to ensure that margin levels are commensurate with the risk exposure of each portfolio during periods of heightened market volatility and economic uncertainty. This is consistent with Rule 17Ad-22(e)(6)(v) of the Exchange Act[11] which requires the use of an appropriate method for measuring credit exposure that accounts for relevant product risk factors and portfolio effects across products.

The Proposal is not intended to advantage or disadvantage capital formation in any particular market segment. The Proposal focuses entirely on managing the clearance and settlement risk associated with TBAs as required by Section 17A of the Exchange Act. Clearing Members with portfolios that present similar risks would be similarly impacted, regardless of other characteristics of the Clearing Member.

In addition, while the Required Fund Deposit requires that a certain amount of cash and securities be available to FICC for risk mitigation, it is not a fixed cost and is available to the Clearing Member upon settlement of the TBAs. FICC maintains the Required Fund Deposit to account for risk of particular securities in Clearing Members' portfolios, including mortgage pools, but FICC does not keep the cash or securities that make up the Required Fund Deposit unless there is a default by a Clearing Member. So while FICC understands that the Required Fund Deposit can lessen liquidity for a Clearing Member by requiring that a certain amount of cash and securities be available to FICC in the form of the Required Fund Deposit, the amount of the cash and

[11] 17 CFR 240.17Ad-22(e)(6)(v).

securities is not a direct cost relating to particular mortgages. Additionally, FICC requires that only a portion of the minimum Required Fund Deposit be made in cash.[12] A portion can be made by depositing Eligible Clearing Fund Securities.

Need for Enhancements to Existing VaR Model Instead of MMA

Commenters questioned whether enhancements to the sensitivity VaR model instead of introducing the MMA would be more appropriate because the MMA would implement a "blunt tool"[13] that may cause "sudden and persistent spikes in margin requirements"[14] and that a return to "purely priced-based margin models" is not appropriate.[15] As described in the Filings, the sensitivity VaR model did not respond effectively to the 2020 market volatility and economic uncertainty and impact studies have indicated that introducing the MMA will increase the margin back-testing performance during such periods by maintaining a VaR Charge that is appropriately calibrated to the current market price volatility.

The MMA with a shorter lookback period of one to three years is designed to provide a quicker response to cover FICC exposures during heightened market volatility. The backtesting performance during the 2020 market volatility and economic uncertainty indicated that the Required Fund Deposits were not sufficient to satisfy the 99% confidence level. However, as indicated by subsequent impact studies, the VaR model, with the longer lookback period of 10 years (plus, if applicable, a stressed period), recalibrated to include market volatility events as shown by the narrowing difference in impact between the VaR model and MMA following the events in 2020. In the Filings, FICC indicated that the average daily VaR increase during the impact study period (February 3, 2020 – June 30, 2020) if MMA had been implemented was approximately $2.2 billion or 42%. As FICC's VaR model recalibrated to the current market conditions, the average daily increase during Q4 of 2020 had MMA been implemented would have been approximately $838 million or 7%. The impact study for Q4 reflecting this analysis has been distributed to the Clearing Members.

SIFMA states that the lookback period that FICC will implement initially for the MMA is two years, but states that the period used to determine a deficit in the desired 99% coverage ratio is only one month.[16] The MMA lookback period is for the model calibration, would be between one to three years and would be analyzed to evaluate its sensitivity and impact to the model performance under four distinctive market regimes, epitomized by recent observations as explained in the Rule Filing : The backtesting coverage calculation is based on rolling 12 months. MBSD's coverage ratio fell below 99% due to the series of market moves occurred during the month of February, March and April 2020.

As explained in the Filings, the Proposal is designed to calculate the exposure in each portfolio using observable TBA indices to benchmark the FICC VaR estimate to confirm that the

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12 The MBSD Rules require that each Clearing Member maintain the lesser of $5,000,000 or 10% of the Required Fund Deposit, with a minimum of $100,000, must be maintained in cash. MBSD Rule 4, Section 3.

13 ASA Letter p. 2.

14 SIFMA Letter p. 3.

15 IDTA/MBA Letter p. 4

16 SIFMA Letter p. 3

VaR estimate covers the portfolio risk level under the current market conditions. The Proposal is intended to limit FICC's exposure to Clearing Members by ensuring that each Clearing Member has an appropriate minimum VaR Charge in the event that the VaR model yields too low a VaR Charge for such portfolios. By identifying and providing for appropriate VaR Charges, adding the MMA to the VaR Floor would help to ensure that margin levels are commensurate with the risk exposure of each portfolio during periods of heightened market volatility and economic uncertainty.

Impact Clarity/Adequacy of Record

Each of the Commenters argue that FICC has not provided Clearing Members with enough information to evaluate the impact of MMA. One Commenter suggested that because of the "opaque nature" of the FICC clearing fund calculations, the increase in clearing fund as a result of the Proposal will be unpredictable.[17] Another Commenter stated that the Proposal was largely void of any evidence or data regarding the economic and market impact of implementing the Proposal.[18] IDTA/MBA stated that while the Proposal explains that the VaR model did not achieve a 99% confidence level for the period beginning in March 2020 through the beginning of April 2020, it does not explain which institutions (or which types of institutions) contributed the most to that shortfall.[19] ASA and SIFMA each state that the Proposal does not include evidence or data relating to the market impact and that a study on the market impact needs to be explored. [20]

FICC has followed up with Clearing Members to explain the effects of the MMA and provides tools and resources for Clearing Members to assist Clearing Members to determine their Clearing Fund requirements and the impact of the proposal. The impact study for Q4 had been distributed to the Clearing Members. As indicated by impact studies, the March-April 2020 market volatility impacted all Clearing Member types in MBSD. By the end of April 2020, 54 out of 71 Clearing Members were under the 99% confidence level with the overall margin backtesting level coverage at 97.3%

In addition to the Filings and Clearing Member outreach, FICC provides other tools and resources to enable Clearing Members to determine their margin requirements and the impact of proposals. FICC maintains the Real Time Matching Report Center (RTTM), Clearing Fund Management (CFM) System, and FICC Customer Reporting (FIR) service which are client accessible websites for accessing risk reports and other risk disclosures. These websites enable a member to view and download Clearing Fund requirement information and component details. The reporting enables a member to view, for example, a portfolio breakdown by CUSIP, including the amounts attributable to the sensitivity-based VaR model. In addition, members are able to view and download spreadsheets that contain market amounts for current clearing positions, and the associated VaR charge.

FICC also maintains the FICC Risk Client Portal which is a member accessible website portal that provides members the ability, for information purposes, to view and analyze certain

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17 SIFMA Letter p. 4.

18 ASA Letter p. 2.

19 IDTA/MBA Letter p. 3.

20 ASA Letter p. 2; SIFMA Letter p. 4.

risks relating to their portfolio, including daily customer reports and calculators to assess the risk and Clearing Fund impact of certain activities. FICC maintains the FICC Client Calculator available on the FICC Risk Client Portal that provides functionality to Clearing Members to enter 'what-if' position data and recalculate their VaR charge to determine margin impact pre-trade execution. The FICC Client Calculator allows Clearing Members to see the impact to the VaR charge if specific transactions are executed, or to anticipate the impact of an increase or decrease to a current clearing position.

FICC believes that the MBSD Rules, together with the outreach by FICC, the Filings and the tools and resources available to Clearing Members provide sufficient information to enable participants to identify and evaluate the risks, fees, and other material costs they incur by participating in MBSD in accordance with Rule 17Ad-22(e)(23)(ii) of the Exchange Act.

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CCLF Charges

SIFMA stated that certain of its members have inquired about whether FICC intends to review and/or adjust CCLF[21] charges in light of the Proposal.[22] The Required Fund Deposits and CCLF are not directly related and are each designed to account for different risks. Required Fund Deposits are designed to address the market risk inherent in each Clearing Member's portfolio and to mitigate potential losses to FICC associated with liquidation of a Clearing Member's portfolio in the event of a default. The CCLF is a rules-based liquidity tool designed to ensure that MBSD has sufficient liquidity resources to complete settlement for its largest failure of a family of accounts. Introducing the MMA would adjust the VaR Floor to help ensure that FICC collects adequate Required Fund Deposits from its Clearing Members to cover the market price risk of each Clearing Member's unsettled TBA portfolio. These are different financial risks that FICC must address and require discrete but different financial resources. FICC does not believe CCLF procedures or Clearing Member obligations with respect to CCLF will need to be modified as a result of the Proposal.

Concentration Charges

IDTA and MBA questioned whether FICC should consider implementing concentration charges which they state are employed by other central clearers.[23] On October 14, 2020, FICC received approval from the SEC to introduce the Margin Liquidity Adjustment Charge ("MLA Charge") as an additional margin component.[24] The MLA Charge is calculated to address the risk presented to FICC when a Clearing Member's portfolio contains large Net Unsettled Positions in the particular group of securities with a similar risk profile or in a particular asset type. The MLA Charge is designed to mitigate the risk of incurring additional market impact cost from the

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[21] The Capped Contingency Liquidity Facility ("CCLF") is set forth in MBSD Rule 17, Section 2a.

[22] SIFMA Letter p. 4.

[23] IDTA/MBA Letter p. 5

[24] See Notice of Filing of Amendment No. 2 and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment Nos. 1 and 2, To Introduce the Margin Liquidity Adjustment Charge and Include a Bid-Ask Charge in the VaR Charges, Release No. 34-90182, 85 Fed. Reg. 66630 (October 20, 2020).

directionally concentrated portfolio, not price volatility, which the MMA is designed to cover. FICC does not believe that further concentration charges are necessary or appropriate.

Proposal Inconsistent with the Exchange Act/Historical Price Movements and Future Market Volatility

Some Commenters stated that the MMA is unreasonably designed to mitigate future risk and that reliance on historical price movements does not generate margin requirements that equate to future protections against market volatility and that, as a result, the proposal is inconsistent with the Section 17A(b)(3)(F) of the Exchange Act[25] and Rules 17Ad-22(e)(4)(i)[26] and (e)(6)(i)[27] of the Exchange Act.[28]

As explained in the Filings, the Proposal is designed to calculate the exposure in each portfolio using observable TBA indices to benchmark the FICC VaR estimate to confirm that the VaR estimate covers the portfolio risk level under the current market conditions. Backtesting results shows that the MMA's reliance on observed price volatility with a shorter lookback period will provide margin that responds quicker during market volatility to limit FICC's exposures. FICC believes that the Proposal will increase the margin back-testing performance during periods of heightened market volatility by maintaining a VaR Charge that is appropriately calibrated to the observable market price volatility

The General Instructions to Form 19b-4 (the "Form") prescribe the information to be included in the completed Form. With respect to the amount of information to be included, the self-regulatory organization is enjoined to "provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the [Exchange] Act and the applicable rules and regulations under the [Exchange] Act."[29] FICC believes that the documents submitted in connection with this Rule Filing are sufficiently clear and comprehensible for the Commission to order the approval of the Rule Filing. The documents submitted include the Rule Filing itself, the Advance Notice, the narratives included with the Rule Filing and the Advance Notice, this letter and the letters submitted by the Commenters. This letter addresses a number of concerns raised by the Commenters; however, to the degree Commenters' concerns are not addressed above, FICC believes that the record contains adequate responses with regards to such concerns.

In addition, FICC believes that the Proposal is consistent with 17A(b)(3)(F) of the Exchange Act,[30] Section 17A(b)(3)(I) of the Exchange Act,[31] Rule 17Ad-22(e)(4)(i) under the Exchange Act[32] and Rule 17Ad-22(e)(6)(i) under the Exchange Act[33] as described in the Rule Filing and as further described herein. FICC also believes that the Proposal is consistent with Rule 17Ad-

25 15 U.S.C. 78q-1(b)(3)(F).
26 17 CFR 240.17Ad-22(e)(4)(i).
27 17 CFR 240.17Ad-22(e)(6)(i).
28 IDTA/MBA Letter p. 4
29 Form 19b-4.
30 15 U.S.C. 78q-1(b)(3)(F).
31 15 U.S.C. 78q-1(b)(3)(I).
32 17 CFR 240.17Ad-22(e)(4)(i).
33 17 CFR 240.17Ad-22(e)(6)(i).

22(e)(6)(v) of the Exchange Act[34] and Rule 17Ad-22(e)(23)(ii) of the Exchange Act[35] as described herein. While some of the Commenters may disagree with the Proposal, FICC believes that the Rule Filing is consistent with the Exchange Act and provides a basis for the Commission to make a determination on the merits.

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FICC appreciates the opportunity to respond to the comment letters.

Sincerely,

Timothy J. Cuddihy

Managing Director
DTCC Financial Risk Management

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34 17 CFR 240.17Ad-22(e)(6)(v).
35 17 CFR 240.17Ad-22(e)(23)(ii).