NOTICE TO MEMBERS

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Gross Client Margin (GCM) Model Update and Approach to Implementation - Consultation with Clearing Members

Canadian Derivatives Clearing Corporation ("CDCC") is resuming its work related to the development and implementation of the Gross Client Margin (GCM) model for futures markets, consistent with the Principle 14 (PFMI), *Segregation and portability of the Principles for Financial Market Infrastructures*[1]. This principle stipulates that a CCP should have rules and procedures that enable the segregation and portability of positions of a Clearing Member's (CM) customers and the collateral provided to the CCP with respect to those positions.

Following previous discussions with industry stakeholders, it was generally agreed that a GCM model provides enhanced customer protection, especially by strengthening the ability to port customer positions and collateral in the event of a clearing participant default, and is the most appropriate model for the Canadian marketplace.

CDCC considers that GCM will provide to industry stakeholders the following main benefits:

- Reduced client's credit risk exposure to their CM and to client fellow risk since more of their margin collateral will be held with the CDCC;
- Level playing field between CMs since clients become equally protected under the CDCC customer protection regime;
- Increased portability of the clients' positions & related margin in a timely manner, rather than closing-out their positions within the current standard default management process; closing-out and re-establishing positions is destabilizing and unnecessarily costly for all participants;
- New minimum level of protection is given for all types of collateral accounts since the CM collateral (Firm collateral account) will be physically segregated from those of its clients (Client collateral account); and

[1] https://www.bis.org/cpmi/publ/d101_fr.pdf

- Operationally and commercially viable solution for all participants since CDCC will be leveraging an already implemented model in the US (e.g CME Clearing) and in Canada ICE Clear Canada)[2].

CDCC customer protection regime will also have implications on rules and procedures serving the Exchange Traded Derivatives (ETD) market, particularly on the Investment Industry Regulatory Organization of Canada (IIROC) and the Canadian Investor Protection Fund (CIPF). In this regard, CDCC is currently working with IIROC & CIPF to clarify roles and responsibilities in a default scenario with the introduction of GCM.

Moreover, given the important impact of GCM model on the Canadian Marketplace, CDCC will be holding a **CM consultation in early Q1 2020**, leveraging existing CM committees. The main objectives of these meetings is to finalize CDCC's business operation model proposal for GCM and to ensure that all stakeholders plan for their internal development to support this significant change. CDCC will be contacting User Group committee members to obtain CM representation for consultation. Following the consultations, we will provide an update on project status and timing that takes into account the input we receive from our Clearing Members.

Additional details on the proposed CDCC business operating model for GCM is also provided in the following section of the notice.

Details on the CDCC Business Operating Model for GCM

GCM Model

GCM implies that CDCC will be collecting margin on a gross basis, rather than on a net basis for futures positions (and options on futures) held in the omnibus customer accounts where all individual client positions are commingled. This means that under GCM, the amount of margin that a CM must post to the CDCC on behalf of its customers is the sum of the amounts of margin required for each customer, rather than the net margin required for all customers.

More specifically, on an EOD basis, GCM margin will be calculated net for all disclosed client positions (GCM positions) and gross amongst clients using the SPAN methodology. On an intraday basis, since client positions are not disclosed, only additional risk (on a net omnibus basis) will be added to the previous EOD GCM margin; otherwise, the previous EOD GCM margin is maintained.

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[2] All open positions at ICE Futures Canada were transitioned to an affiliated company, ICE Clear US in July 2018

Client Positions Declaration and New GCM File

GCM will not require any changes in how CDCC handles omnibus physical accounts; real-time net positions (where clients' positions are commingled) will continue to be reported on the official CDCC books and records in a similar way as currently via the SOLA Clearing system. However, on an EOD basis, a new GCM file will need to be provided to declare customer-by-customer positions. In order not to be penalized with higher margin requirements, CMs must submit the GCM file on a daily basis before a specific EOD deadline. Intraday declaration of customer-by-customer positions will not be required.

CDCC will allow CMs to submit their GCM positions through a file upload (e.g. FIXML format or CSV format). The file would follow similar declaration fields as ICE Clear US and CME Clearing.

New Segregated Firm and Client Collateral Accounts

Regarding the collateral accounts management, Firm and Client collateral accounts will be segregated rather than being commingled as it is currently at the CM level. Hence, in order to meet CM's margin deficits (at the Firm or Client account level), only Firm account collateral excess could be used. Collateral of the clients under GCM will also be physically segregated from those not under GCM.

Client Excess Margin Treatment

Excess margin will not be permitted in any CM Client GCM collateral account on a day-to-day basis (following a daily close) and would not be under CDCC control for standard default management. It will however be permitted to maintain client excess on an intraday basis.

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