



U.S. COMMODITY FUTURES TRADING COMMISSION

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Division of Swap Dealer and
Intermediary Oversight

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Director

CFTC Letter No. 17-11
No-Action
February 13, 2017
Division of Swap Dealer and Intermediary Oversight

Re: Commission Regulation 23.153: Time Limited No-Action Position for Failure to Collect and/or Post Variation Margin

Ladies and Gentlemen:

This letter presents a no-action position from the Division of Swap Dealer and Intermediary Oversight (“**DSIO**”) of the Commodity Futures Trading Commission (“**Commission**”) for swap dealers (“**SDs**”) registered with the Commission and subject to the Commission’s rules regarding margin requirements for uncleared swaps¹ regarding compliance with such margin requirements.

Specifically, as detailed below, this letter provides relief until September 1, 2017, from compliance with the variation margin requirements under Commission Regulation 23.153² that are subject to a compliance date of March 1, 2017, pursuant to Commission Regulation 23.161(a)(2)³ (the “**March 1 VM Requirements**”).⁴

¹ The Commission’s margin requirements for uncleared swaps apply only to SDs and major swap participants for which there is not a prudential regulator. See 7 U.S.C. 6s(e)(1)(B). SDs and major swap participants for which there is a prudential regulator must meet the margin requirements for uncleared swaps established by the applicable prudential regulator. 7 U.S.C. 6s(e)(1)(A). See also 7 U.S.C. 1a(39) (defining the term “Prudential Regulator” to include the Board of Governors of the Federal Reserve System; the Office of the Comptroller of the Currency; the Federal Deposit Insurance Corporation; the Farm Credit Administration; and the Federal Housing Finance Agency). The Prudential Regulators published final margin requirements in November 2015. See Margin and Capital Requirements for Covered Swap Entities, 80 FR 74840 (Nov. 30, 2015).

² 17 CFR § 23.153.

³ 17 CFR § 23.161.

⁴ For the avoidance of doubt, this letter has no effect on the variation margin requirements of § 23.153 that were subject to a compliance date of September 1, 2016. As of September 1, 2016, an SD was required to comply with the variation margin requirements of § 23.153 with swap counterparties where the SD (combined with all of its affiliates) and its counterparty (combined with all of its affiliates) had an average

I. Regulatory Background

Pursuant to section 4s(e) of the Commodity Exchange Act (“CEA”)⁵, the Commission is required to promulgate margin requirements for uncleared swaps applicable to each SD for which there is no Prudential Regulator.⁶ The Commission published final margin requirements for such SDs in January 2016 (the “**Final Margin Rule**”).⁷

As part of the Final Margin Rule, the Commission promulgated Commission Regulation 23.153, which requires SDs to collect and post variation margin with each counterparty that is an SD, major swap participant, or financial end user.⁸

Pursuant to Commission Regulation 23.161, compliance dates for the Final Margin Rule are staggered such that SDs must come into compliance in a series of phases over four years. The first phase affected SDs with the largest outstanding notional amounts of uncleared swaps, which began complying with both the initial and variation margin requirements of the Final Margin Rule on September 1, 2016.⁹ The second phase is the March 1 VM Requirements, which require SDs to comply with the variation margin requirements of Commission Regulation 23.153 with all relevant counterparties not covered in the first phase.

daily notional amount of covered swaps for March, April, and May of 2016 that exceeds \$3 trillion. See Commission Regulation 23.161(a)(1)(ii), 17 CFR § 23.161(a)(1)(ii).

⁵ 7 U.S.C. § 1 et. seq.

⁶ See 7 U.S.C. 6s(e)(1)(B).

⁷ See Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 81 FR 636 (Jan. 6, 2016). The Final Margin Rule, which became effective April 1, 2016, is codified in part 23 of the Commission’s regulations. See §§ 23.150-159, 161. The Commission’s regulations are found in Chapter 17 of the Code of Federal Regulations, 17 CFR 1 et. seq.

⁸ See Commission Regulation 23.153(a) and (b), 17 CFR § 23.153(a) and (b), stating:

(a) *Initial obligation.* On or before the business day after the day of execution of an uncleared swap between a covered swap entity and a counterparty that is a swap entity or a financial end user, the covered swap entity shall collect the variation margin amount from the counterparty when the amount is positive, or post the variation margin amount with the counterparty when the amount is negative as calculated pursuant to § 23.155 and in a form that complies with § 23.156.

(b) *Continuing obligation.* The covered swap entity shall continue to collect the variation margin amount from, or to post the variation margin amount with, the counterparty as calculated each business day pursuant to § 23.155 and in a form that complies with § 23.156 each business day until such uncleared swap is terminated or expires.

⁹ See Commission Regulation 23.161(a)(1), 17 CFR § 23.161(a)(1).

II. Summary of Request for No-Action Position

DSIO has received requests for a transitional relief period for the March 1 VM Requirements from virtually all SDs and entities that use swaps to hedge commercial risk, as represented by, among others:

- (1) The Securities Industry and Financial Markets Association's Asset Management Group;
- (2) The Investment Adviser Association;
- (3) The American Council of Life Insurers;
- (4) The Investment Company Institute;
- (5) The Federal Home Loan Banks;
- (6) The Committee on Investment of Employee Benefit Assets;
- (7) The ERISA Industry Committee;
- (8) The International Swaps and Derivatives Association;
- (9) The Financial Services Roundtable;
- (10) The ABA Securities Association, an American Bankers Association subsidiary;
- (11) The Global Financial Markets Association, including its Global FX Division;
- (12) The Investment Association;
- (13) The Association for Financial Markets in Europe; and
- (14) The American Benefits Council.

As represented by the SDs and this swap end-user community, SDs must execute new or amended credit support documentation with virtually all swap end-users, as well as put in place new operational processes to settle variation margin in accordance with the March 1 VM Requirements. Although the end-user community has actively engaged with SDs to execute credit support documentation in compliance with the March 1 VM Requirements, many firms have numerous credit support documents to execute or amend. The end-user community recognizes the efforts of the SDs to develop new documentation and execution processes through the International Swaps and Derivatives Association to help with implementation of the March 1 VM Requirements, but such efforts have been only partially effective because there is not a one-size-fits all credit support agreement that works for all market participants.

For these and other reasons, many SDs will not be able to implement the March 1 VM Requirements by March 1, 2017, without causing substantial disruptions to the uncleared swap market. Specifically, SDs may be required to stop trading with a significant number of counterparties, which could reduce access to liquidity and the ability to hedge positions for other counterparties. An abrupt cutoff in substantial swap trading activity could have harmful effects on the global swaps market with both foreseeable and unforeseeable consequences to market health and safety.

III. DSIO No-Action Position

It is the understanding of DSIO that the Commission remains committed to implementing the March 1 VM Requirements in accordance with the March 1, 2017, compliance date for variation margin requirements that was agreed upon in 2013 by 26 regulatory authorities from around the world,¹⁰ and thus all swaps entered into from March 1, 2017 must be subject to such requirements.

Given the foregoing, DSIO believes that a specific and limited no-action position will serve to preserve the Commission's March 1 implementation commitment, while helping to avoid a disruption in the uncleared swap market. Accordingly, DSIO will not recommend an enforcement action against an SD that does not comply with the March 1 VM Requirements prior to September 1, 2017, subject to the following conditions:

- (1) The SD does not comply with the March 1 VM Requirements with respect to a particular counterparty solely because it has not, despite good faith efforts, completed necessary credit support documentation (including custodial segregation documentation, if any) with such counterparty or, acting in good faith, requires additional time to implement operational processes to settle variation margin in accordance with the March 1 VM Requirements with such counterparty;
- (2) The SD uses its best efforts to continue to implement compliance with the March 1 VM Requirements without delay with each counterparty following March 1, 2017;
- (3) To the extent the SD has existing variation margin arrangements with a counterparty, it must continue to post and collect variation margin with such counterparty in accordance with such arrangements until such time as the SD is able to comply with the March 1 VM Requirements with respect to that counterparty; and

¹⁰ See "Margin requirements for non-centrally cleared derivatives" (updated March 2015), available at <http://www.bis.org/bcbs/publ/d317.pdf>. Key principle 8 of such requirements set forth a timeline for implementation of margin rules, including a requirement that from March 1, 2017, all covered entities will be required to exchange variation margin.

- (4) No later than September 1, 2017, the SD complies with the March 1 VM Requirements with respect to all swaps to which the March 1 VM Requirements are applicable entered on or after March 1, 2017.

During the no-action period, DSIO intends to monitor the progress of SDs who rely on this letter. In order to rely on the protections of this letter, such SDs are expected to make continual, consistent, and quantifiable progress toward compliance with the March 1 VM Requirements with all counterparties on a rolling basis during the no-action period. DSIO expects that all SDs should be in compliance with the March 1 VM Requirements with all counterparties, as applicable, by September 1, 2017.

This letter, and the positions taken herein, represent the views of DSIO and do not necessarily represent the positions or views of the Commission or of any other office or division of the Commission. The relief issued by this letter does not excuse persons relying on it from compliance with any other applicable requirements contained in the CEA or in the Regulations issued thereunder. This letter does not create or confer any rights or obligations on any person or persons subject to compliance with the CEA that bind the Commission or any of its other offices or division. As with all no-action letters, DSIO retains the authority to condition further, modify, suspend, terminate, or otherwise restrict the terms of the no-action relief provided herein, at its discretion.

Should you have any questions, please contact me at (202) 418-5326 or Frank Fisanich, Chief Counsel, at (202) 418-5949.

Very truly yours,

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