

RECOMMENDATIONS TO IMPROVE SCOPING AND IMPLEMENTATION OF INITIAL MARGIN REQUIREMENTS FOR NON-CLEARED SWAPS

REPORT TO THE COMMODITY FUTURES TRADING COMMISSION'S
GLOBAL MARKETS ADVISORY COMMITTEE BY THE SUBCOMMITTEE
ON MARGIN REQUIREMENTS FOR NON-CLEARED SWAPS

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Adopted by the Global Markets Advisory Committee for CFTC consideration on May 19, 2020. The views, analyses, and conclusions expressed herein do not necessarily reflect the views of the Commission or its staff, or the United States government.

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Preface

Global Markets Advisory Committee – Subcommittee on Margin Requirements for Non-Cleared Swaps

As the Commodity Futures Trading Commission’s (CFTC or **Commission**) uncleared swap margin rules (the **Margin Rules**)¹ approach later phases of compliance, a broad and representative group of market participants—on behalf of retail and private funds, pensions, insurance companies, institutional investors, asset managers, and dealers—along with self-regulatory organizations, market utilities, and service providers have come together on the Subcommittee on Margin Requirements for Non-Cleared Swaps (the **Margin Subcommittee**) to review the application of initial margin (**IM**) requirements to a new wave of market participants in Phase 5 and Phase 6 and beyond.

The Margin Subcommittee was established by the Global Markets Advisory Committee (**GMAC**) “to examine the implementation of margin requirements for non-cleared swaps, to identify challenges associated with forthcoming implementation phases, and to recommend actions the Commission may take to mitigate the challenges identified” and consider “regulatory initiatives that may address such challenges faced by market participants in complying with margin requirements for non-cleared swaps.”²

As the Honorable Commissioner Dawn Stump, sponsor of the GMAC, has recognized, the remaining phases of the Margin Rules will bring in scope different types of market participants than did prior phases, with distinct challenges. While the remaining phases will dwarf prior phases in the sheer number and types of impacted market participants, the average amount of margin to be exchanged with these market participants is expected to be far less. Indeed, Phase 5’s approximately 200 entrants would cover only 8 percent of the total average aggregate notional

¹ CFTC Regulation §§ 23.150-23.161, 17 C.F.R. §§ 23.150-23.161; *see also* Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 81 Fed. Reg. 636 (Jan. 6, 2016).

² *See* Request for Nominations for the Subcommittee on Margin Requirements for Non-Cleared Swaps Under the Global Markets Advisory Committee, 84 Fed. Reg. 57,706 (Oct. 28, 2019).

amount (AANA) of swaps across all phases, and Phase 6's approximately 500 entrants would cover only 3 percent of the AANA across all phases.³

In light of the unique challenges faced by future phased-in market participants and the potential unintended consequences, the Margin Subcommittee delivers the following report for the GMAC's consideration. The report provides some background on these newly-impacted market participants, outlines the scoping and implementation challenges associated with the remaining phases of the Margin Rules, and provides recommendations for addressing such challenges. The Margin Subcommittee respectfully asks that the GMAC endorse our recommendations for actions to be taken by the Commission to make the Margin Rules more workable and efficient for entities in the remaining phases without compromising the Margin Rules' purpose of reducing systemic risk. Further, the Margin Subcommittee respectfully requests that the GMAC urge the Commission to work with other U.S. and global regulators to undertake actions consistent with those recommended in the report as necessary and appropriate in the interest of international harmonization.

The Margin Subcommittee acknowledges and appreciates the CFTC's recent action to codify the implementation schedule providing for the Phase 5 and Phase 6 framework referred to above,⁴ which is consistent with the recommendation issued by the Basel Committee on Banking Supervision (BCBS) and the International Organization of Securities Commissions (IOSCO) in July 2019.⁵ Additionally, in issuing statements on March 18, 2020 to support that codification, the Honorable CFTC Chairman Heath Tarbert and other CFTC Commissioners recognized that unique and extenuating circumstances have arisen as a result of the sudden COVID-19 global pandemic, causing market participants to experience tremendous market uncertainty and volatility and necessitating targeted relief to address impacts from the crisis.⁶ Given the heightened challenges arising in the current environment and

³ See Initial Margin Phase 5 Report of the CFTC's Office of the Chief Economist (Oct. 24, 2018), at 4-5, available at <https://www.cftc.gov/PressRoom/PressReleases/7834-18> (the CFTC Margin Study) (Appendix A).

⁴ See Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 85 Fed. Reg. 19,878 (April 9, 2020).

⁵ See "Basel Committee and IOSCO Agree to One-Year Extension of the Final Implementation Phase of the Margin Requirements for Non-Centrally Cleared Derivatives" (July 23, 2019), available at <https://www.bis.org/press/p190723.htm>.

⁶ See, e.g., Statement of the Honorable CFTC Chairman Heath P. Tarbert in Support of Extending Relief for Initial Margin Requirements for Uncleared Swaps (Mar. 18, 2020), available at

after submission of a request letter on March 25, 2020 by the International Swaps and Derivatives Association (**ISDA**) and 20 other industry associations,⁷ BCBS-IOSCO amended its recommended margin framework on April 3, 2020 to push out each of the Phase 5 and Phase 6 compliance dates by one year (along with the relevant calculation periods for those phases).⁸

The Margin Subcommittee applauds the timeliness of the April 2020 BCBS-IOSCO action, which serves as confirmation by the collective international standard-setting bodies that it is critical for the industry to be able to divert and dedicate scarce resources to respond to the COVID-19 crisis and related market volatility and liquidity issues without jeopardizing compliance with upcoming regulatory obligations under uncleared swap margin rules. Cognizant that BCBS-IOSCO do not have the legal power to enact regulations, the Margin Subcommittee strongly encourages the CFTC and other U.S. and global regulators to formally adopt BCBS-IOSCO's latest recommendation for a push-out of the Phase 5 and Phase 6 compliance dates⁹ in addition to the specific recommendations for addressing margin-related issues, as set forth in our report.

Even assuming that the CFTC (and other U.S. and global regulators) will act swiftly to provide relief in accordance with the April 2020 BCBS-IOSCO recommendation, market participants coming into scope for the newly scheduled Phases 5 and 6 and beyond will continue to face various challenges that are distinct and apart from the current COVID-19 crisis. Put differently, the COVID-related time extension is not

<https://www.cftc.gov/PressRoom/SpeechesTestimony/tarbertstatement031820> (pointing out that “now that many firms’ resources have been appropriately redirected to [COVID-19] response efforts,” it is “even more challenging” for market participants to “put required custodial arrangements and documentation in place” and otherwise get into compliance with IM requirements in the remaining phases of the Margin Rules).

⁷ See Letter Re: Margin Requirements for Non-Centrally Cleared Swaps Margin – Impact of COVID-19 on Initial Margin Phase-In (Mar. 25 2020), available at <https://www.isda.org/a/sM7TE/IMPhases5-6COVID-19Letter.pdf>.

⁸ See Basel Committee on Banking Supervision and Board of the International Organization of Securities Commissions, Margin Requirements for Non-Centrally Cleared Derivatives (Apr. 2020), available at <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD651.pdf>. This BCBS-IOSCO recommendation for a revised implementation timeline effectively supersedes the BCBS-IOSCO recommendation issued in July 2019.

⁹ Several jurisdictions, such as Canada, Switzerland, Japan, Singapore (MAS), Hong Kong (SFC) and Australia, have adopted, or announced an intention to adopt, the latest BCBS-IOSCO recommendation.

designed to address the margin scoping and implementation issues anticipated for Phases 5 and 6 and beyond. We expect the industry to use the COVID-related time extension as it is intended: to focus on continuing basic, critical operations during a historic period of market volatility and uncertainty and, to the extent possible as market conditions stabilize and resources become available, re-engage in workflows necessary to comply with uncleared swap margin rules. The Margin Subcommittee's recommendations outline more targeted relief designed to address specific margin-related challenges, and we urge the GMAC to support such recommendations for adoption by the CFTC.

The Margin Subcommittee commends the GMAC and the CFTC for their continued focus on issues relating to the Margin Rules and gives special thanks to the Honorable Commissioner Stump for creating the Margin Subcommittee. The Margin Subcommittee also thanks CFTC staff, particularly Warren Gorlick (Associate Director, Division of Swap Dealer and Intermediary Oversight (**DSIO**)) and Carmen Moncada-Terry (Special Counsel, DSIO), whose participation and contributions were invaluable to the Margin Subcommittee's work.

Executive Overview

The Margin Subcommittee has identified a variety of challenges associated with the scoping and implementation of regulatory IM requirements in Phases 5 and 6 and beyond; some challenges are a result of U.S. divergence from the *Margin Requirements for Non-Centrally Cleared Derivatives* issued by BCBS and IOSCO (the **BCBS-IOSCO framework**) while others will require international coordination to address.¹⁰ After consideration of potential mitigants and regulatory initiatives which might address such challenges, the Margin Subcommittee is making the following recommendations, described in more detail in this report, to the GMAC for further consideration and action by the CFTC for the immediate term and later term.

Immediate Term Recommendations

Immediate term recommendations are expected to have the most beneficial impact if adopted *prior to, or as of, the Phase 5 compliance date*. The descriptions below for each recommendation highlight the challenge that the recommendation would address and how the recommendation could be implemented.

❖ Confirm Interpretation that a CSE Can Continue to Trade with an SMA Client in the Case of an Inadvertent Breach of the \$50M IM Threshold

- **Challenge:** Unique compliance issues arise where a covered swap entity's (CSE) counterparty, such as a pension fund, hires multiple asset managers to diversify its investments and investment expertise (a **Separately Managed Account Client**, or an **SMA Client**). For these SMA Clients, each asset manager will establish on behalf of the SMA Client one or more separately managed accounts to execute different investment mandates for risk diversification and other purposes (each such account, an **SMA**). While the regulatory IM threshold amount (regulatory maximum of \$50M) (**IM Threshold**) will need to be calculated and monitored by the CSE for the SMA Client in the aggregate, each SMA asset manager will only know the regulatory IM associated with the transactions that it independently executes for the SMAs that it manages on behalf of the SMA Client. Should the activities of another asset manager or managers

¹⁰ See Basel Committee on Banking Supervision and Board of the International Organization of Securities Commissions, *Margin Requirements for Non-Centrally Cleared Derivatives* (Apr. 2020), available at <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD651.pdf>.

unexpectedly put the SMA Client's uncollateralized regulatory IM exposure in the aggregate over the regulatory IM Threshold with a given CSE, the CSE may feel it needs to cease trading activity with *all* of the SMA asset managers (even those acting under regulatory IM compliant documentation or within agreed allocations of the regulatory IM Threshold) unless it has a regulatory interpretation on how to apply IM requirements to SMAs. The halting of trading, in turn, could impair investment activities and harm the underlying SMA Client.

- **Recommendation:** So long as the CSE and SMA Client allocate no more than a total of \$50M regulatory IM Threshold across the SMAs, permit a CSE to treat each SMA separately for compliance purposes. As such, if the CSE were to inadvertently exceed \$50M in uncollateralized regulatory IM exposure with an SMA Client in the aggregate, an SMA could continue to trade with the CSE, if (i) the asset manager for the SMA is trading under regulatory compliant IM documentation; or (ii) the CSE and asset manager for the SMA have agreed a regulatory IM sub-Threshold and the asset manager for the SMA is trading at or below the agreed regulatory IM sub-Threshold, provided that the CSE and the asset managers of the other SMAs of the SMA Client are no longer continuing to trade (absent other relief) and are working to reduce the aggregate uncollateralized regulatory IM exposure of the SMA Client back to at or under \$50M.

❖ **Removal of Certain Collateral Eligibility Restrictions on Money Market Funds**

- **Challenge:** The ability to use redeemable securities in a pooled investment fund, more typically referred to as a money market fund (MMF), as eligible collateral in the U.S. has been severely restricted by the condition that assets of the MMF may not be transferred through securities lending, securities borrowing, repurchase agreements, and reverse repurchase agreements.
- **Recommendation:** Eliminate undue restrictions on the activity of eligible MMFs to transfer assets through securities lending, securities borrowing, repurchase agreements, and reverse repurchase agreements.

❖ **Removal of Consolidation Requirement for Seeded Funds**

- **Challenge:** Certain investment funds are temporarily seeded by a parent, sponsor or affiliate that does not guarantee the obligations of such fund or participate in or control the management of such fund; the fund is

launched and seeded in order to establish a performance record before external investors will invest in them. When these “seeded funds” are seeded by a parent with material swaps exposure (MSE), such seeded funds have to post IM while other seeded funds sponsored by entities without MSE or not otherwise affiliated with a group that has MSE do not have to post IM. This disparate treatment puts these seeded funds at a disadvantage domestically and globally as most of the U.S.’s global competitors have adopted the BCBS-IOSCO framework’s recommendation that all investment funds be exempt from consolidation with their parent, sponsor or affiliate, provided that the seeding entity does not guarantee such fund’s obligations.

- Recommendation: In accordance with the BCBS-IOSCO framework and other global jurisdictions, provide an exemption from the consolidation of seeded funds with their sponsors (provided such sponsors do not guarantee the seeded funds’ obligations) for purposes of calculating AANA and MSE during the limited seeding period in order to provide a level playing field domestically and globally for these seeded funds.

❖ **Relief Relating to IM Calculations for Small Covered Swap Entities**

- Challenge: The smaller CSEs coming into scope in Phases 5 and 6, may not be approved to calculate IM amounts using a quantitative IM model like ISDA SIMM™. As a result, they may be required to post and collect higher IM amounts under the regulatory schedule, and may more readily breach the IM Threshold, reducing their preparation time.
- Recommendation: Provide no-action relief to small CSEs allowing them to rely on the IM amounts calculated by their CSE counterparties for purposes of IM monitoring and IM exchange.

❖ **Provide a Grace Period to Reduce Congestion and Facilitate Compliance**

- Challenge: Even with the actions taken by the Commission to date and the recommended extension of the Phase 5 and Phase 6 compliance dates due to the COVID-19 crisis, many Phase 5 and Phase 6 firms’ relationships will not be ready to exchange regulatory IM as of the phase-in dates notwithstanding best efforts due to existing industry resource constraints.
- Recommendation: For at least Phases 5 and 6, grant a 6-month grace period commencing from the day the regulatory IM for a relationship

exceeds the IM Threshold during which the parties must complete the IM documentation and operational set-ups and begin exchanging IM.

Later Term Recommendations

Later term recommendations are anticipated to have substantial beneficial impact if adopted by the CFTC *prior to, or as of, the Phase 6 compliance date*. The descriptions below for each recommendation highlight the challenge that the recommendation would address and how the recommendation could be implemented.

❖ Application of Separate IM Threshold to Each Separately Managed Account of an SMA Client

- **Challenge:** As indicated above, given the unique and separate counterparty relationship between an SMA Client, acting through its SMA asset managers, and a CSE with whom it trades, each individual SMA asset manager does not have visibility to, nor control over, the total regulatory IM amount of the SMA Client in order to independently manage the timeline for IM preparation. The SMA Client establishes each SMA independently (e.g., limited recourse arrangements, separate documentation, margining and netting arrangements, etc.) in order to achieve diversification. Each SMA asset manager is thus forced to make a cost-benefit decision as to whether to put in place documentation and custodial arrangements based solely on the transactions that it independently executes for the SMA it manages. If the SMA Client facing a particular CSE were to suddenly and unexpectedly exceed the \$50M IM Threshold in the aggregate, then SMA asset managers would encounter various cliff-edge scenarios, including potentially being cut off from trading or having to terminate existing positions.
- **Recommendation:** Given the lack of transparency and control among SMA asset managers and the independent operation of their SMAs, allow each SMA to be treated as a distinct entity to which a separate regulatory IM Threshold will apply, thereby giving each manager much-needed certainty and control over when an SMA is at or near the IM Threshold. Although this recommendation is the simplest and most efficient solution, we acknowledge that, absent broader support for it by other U.S. and global regulators, an alternative recommendation would be to allow the option for each CSE and SMA asset manager to agree to apply a flat IM Threshold of \$10M per SMA in light of the operational and practical difficulties of sharing the \$50M IM Threshold at the SMA Client level.

Although this recommendation to allow a \$10M IM Threshold per SMA would not be subject to an overall cap of \$50M, there are safeguards to mitigate the risks of an uncapped option, as explained further in Part II.B.1.

❖ **Adjustments to the MSE Calculation’s Timing and Methodology and the Post Phase-In Compliance Periods**

- Challenge: The Commission’s Margin Rules (as well as the uncleared swap margin rules of the U.S. Prudential Regulators (**USPRs**)) for the timing and method of conducting MSE calculations and the compliance dates following September 1, 2021, diverge from the global BCBS-IOSCO framework. The differences create significant cross-border complexity which leads to additional operational burdens, costs and compliance challenges for market participants subject to margin requirements in multiple global jurisdictions.
- Recommendation: Align the timing and methodology for MSE calculations and the post phase-in compliance periods with the BCBS-IOSCO framework and other global regulations.

❖ **Codification of Relief Related to Minimum Transfer Amount**

- Challenge: The minimum transfer amount (**MTA**) requirements do not account for certain practical operational processes and circumstances which limit the ability of CSEs and their covered counterparties to use the MTA, including issues with the application of an MTA for each SMA Client and the ability to split the maximum allowable MTA between distinct IM and variation margin flows.
- Recommendation: These challenges were effectively addressed by CFTC staff letters 17-12 and 19-25. As staff letters may expire or be revoked, we recommend that the CFTC provide certainty to CSEs and their counterparties by amending the Margin Rules to codify the provisions of CFTC staff letters 17-12 and 19-25.

❖ **Removal of Deliverable FX from MSE Calculation**

- Challenge: Small financial end users (a group of market participants described in Part I) are unnecessarily burdened by monitoring and other requirements due to the inclusion of deliverable foreign exchange (**FX**) swaps and forwards (collectively, **Deliverable FX**) in the MSE calculation.

- Recommendation: While the Margin Subcommittee recognizes that inclusion of Deliverable FX has been considered previously by international regulatory bodies without changes recommended, we strongly request reassessment of the market impact, particularly upon small financial end users, and amendment of the Margin Rules to exclude Deliverable FX from the MSE calculation. Since Deliverable FX itself does not have IM requirements, its inclusion in MSE calculations and resulting burdens on small financial end users is not warranted.

The Margin Subcommittee appreciates the GMAC's consideration of the above recommendations. Further background, explanation, and rationale are provided in this report.

I. Remaining Phases of Initial Margin for Uncleared Swaps: Background on Impacted Entities

A. COMPLETED AND REMAINING MARGIN REQUIREMENTS

The Margin Rules require certain swap dealers (**SDs**) and major swap participants (**MSPs**) to post and collect variation margin (**VM**) and IM for uncleared swaps with financial end users and other swap entities. VM requirements, which are now implemented in 10 jurisdictions and apply to all in-scope transactions involving SDs and financial end users, account for more than \$944.7 billion in margin posted or received, significantly reducing counterparty and systemic risks.¹¹ IM pledged to and collected from the entities that were brought into compliance during Phases 1 through 4—i.e., approximately 40 entities with an AANA exceeding \$0.75 trillion¹²—is already significantly contributing to these risk-reducing measures. According to ISDA’s Year-End 2019 Margin Survey, the 20 largest market participants alone collected more than \$100 billion in mandatory IM required by the Margin Rules in addition to discretionary IM.¹³

In contrast to Phases 1 through 4, the remaining phases (Phase 5, Phase 6 and beyond) for the IM requirements of the Margin Rules will bring into scope a much larger and more diverse group of financial end users and swap entities.¹⁴ The CFTC Margin Study found that entities in what are now known as Phases 5 and 6 will span a variety of business sectors, including pension funds (54), insurance companies (48), managed investors (153) hedge funds (163), corporates (65), among others.¹⁵ The CFTC’s DSIO acknowledged that “[a]s a result of the large reduction in the compliance threshold”—which would be from \$750 billion to \$50 billion for Phase 5

¹¹ See ISDA Margin Survey Year-End 2019 (Apr. 2020) at 3, available at <https://www.isda.org/a/1F7TE/ISDA-Margin-Survey-Year-end-2019.pdf> (ISDA YE 2019 Margin Survey).

¹² See CFTC Margin Study at 4.

¹³ ISDA YE 2019 Margin Survey at 3.

¹⁴ See Statement of the Honorable CFTC Chairman Heath P. Tarbert in Support of Extending Relief for Initial Margin Requirements for Uncleared Swaps (Mar. 18, 2020), available at <https://www.cftc.gov/PressRoom/SpeechesTestimony/tarbertstatement031820>.

¹⁵ See CFTC Margin Study at 4-5.

(and from \$50 billion to \$8 billion for Phase 6)—“a significant number of counterparties will come into scope of the IM requirements.”¹⁶ According to the CFTC Margin Study, “[w]hile Phases 1 through 4 capture just over 40 entities,” Phase 5 as originally adopted (now split into the recently finalized Phase 5 and Phase 6) “could bring 700 entities in scope,” which amount to approximately 7,000 IM relationships.¹⁷ Of those 700 entities, approximately 200 entities would be captured by what is now known as Phase 5 and would represent 8 percent of the AANA across all phases, and approximately 500 entities would be captured by what is now known as Phase 6 and would represent 3 percent of the AANA across all phases.¹⁸

Moreover, the Initial Margin Phase-in Analysis conducted by ISDA in 2018 (**ISDA’s 2018 Quantitative Analysis**) indicated that, after applying the MSE phase-in threshold of \$8 billion, a significant portion of the counterparties and relationships brought into scope are not likely to be required to exchange regulatory IM, and those that do will make up a small percentage of the amount of the total industry ISDA SIMM™ (**SIMM**) amounts.¹⁹ Specifically:

- “The vast majority of the more than 1,100 counterparties brought into scope in [what are now known as Phase 5 and Phase 6] will fall close to the lower bounds of the EUR/USD 8 billion threshold.”
- “An estimated 83% (992) of 1,190 counterparties [in what are now known as Phase 5 and Phase 6], and 75% (7,220) of 9,598 relationships [in what are now known as Phase 5 and Phase 6] fall below the USD 100 billion level.”
- “As most of these parties would not exceed a USD 50 million IM exchange threshold, these relationships would on average attract only USD 29.9 million of IM using a regulatory schedule (grid-based) calculation methodology, and USD 10.5 million under a SIMM calculation.”

In the simplest terms, as stated by former CFTC Chairman J. Christopher Giancarlo, “small entities contribute little to systemic risk, and would, in any case, exchange

¹⁶ See CFTC Letter No. 19-16 (July 9, 2019) at 3, available at <https://www.cftc.gov/csl/19-16/download>.

¹⁷ See CFTC Margin Study at 4, 7.

¹⁸ See CFTC Margin Study at 4, 5.

¹⁹ See Letter Re: Margin Requirements for Non-Centrally Cleared Derivatives – Final Stages of Initial Margin Phase-In (Sept. 12, 2018) at 6, available at <https://www.isda.org/a/5evEE/Initial-Margin-Phase-In-Implementation-Joint-Trade-Association-Comments.pdf>.

only small amounts of initial margin.”²⁰ The following sections provide a further description of the general categories (and sub-categories) of entities impacted by the remaining IM phases under the Margin Rules.²¹

B. SMALL FINANCIAL END USERS

1. Key Features

The Margin Rules will bring into scope an expansive list of financial end users and, as noted above, a potentially high volume (including retail and private funds, pooled

Figure 1. Example of small financial end user calculation of AANA (rounded/anonymized)

AANA calculation: 10 Billion AANA; 90% attributable to Deliverable FX; the remaining 10% (\$1B) is split between non-deliverable FX forwards and swaps/swaptions.

Result: Fund will need to engage dealers regarding the Margin Rules, monitoring whether it is below the IM Threshold and posting/collecting if above on the \$1B exposure. If Deliverable FX were removed from AANA calculation, the Fund would be out of scope for the Margin Rules given that it does not maintain MSE.

Note: This Fund engages in Deliverable FX because it is a global fixed income strategy that pursues being 100% hedged to USD, the portfolio’s base currency. The Fund’s manager philosophically believes that unhedged and unmanaged currency risk is unjustified in this strategy given it is traditionally used by investors as a risk reducer/diversifier.

investment vehicles, SMA Clients, seeded funds, etc.). For purposes of this report, “**Small Financial End User**” refers to a financial end user that did not exceed the AANA thresholds in the prior phases (Phases 1 through 4) and that may be subject to IM requirements in the remaining phases. A sizeable portion of the Small Financial End Users would exceed the AANA thresholds in Phase 5 and Phase 6 due to the inclusion of Deliverable FX in the AANA calculation, notwithstanding that Deliverable FX is not subject to the IM requirements. According to the CFTC’s Office of the Chief Economist, 200 of the 700 (30%) of financial end users in what are now known as Phase 5 and Phase 6 will have

MSE due to Deliverable FX.²² Industry data analyzed by ISDA estimates that 1,363 relationships of 227 global financial end users are scoped in for IM requirements due

²⁰ See Letter Re: Phase Five Implementation from J. Christopher Giancarlo to Federal Reserve Board Vice Chairman Randal K. Quarles (Apr. 29, 2019) at 2, available at <https://www.cftc.gov/PressRoom/PressReleases/7922-19>.

²¹ Although not discussed at length in this report, certain security-based swap dealers and major security-based swap participants could also be brought into scope in Phase 5 and beyond.

²² See CFTC Margin Study at 6-7.

to Deliverable FX. These relationships would post only 4.6% (SIMM) or 2.5% (GRID) of the total IM for Phases 5 and 6.²³

Overall, the data and information highlighted above demonstrates that Small Financial End Users individually and in the aggregate do not present the systemic risk that the IM requirements aim to address. Yet, by virtue of being scoped in, Small Financial End Users will face legal, operational, technological and other costs and burdens, as discussed further in Part II. More importantly, these Small Financial End Users may also face disruptions to their trading of derivatives to hedge other risks in their portfolios, access certain markets and meet performance targets.

2. *Separately Managed Account Clients – Pensions, Insurance Companies, Pooled Investment Vehicles and Funds*

An SMA Client is a Small Financial End User such as a pension fund, insurance company or retail fund that has multiple investment mandates executed through separate asset managers. Each separate asset manager has full investment discretion over a strategy with a specified allocation of assets under management (AUM) and executes that strategy through an SMA. The account parameters are set forth in a separate investment management agreement and any permitted guidelines attached thereto (the IMA) between the SMA Client and the asset manager, which, among other things, sets out the scope of the asset manager’s authority to trade derivatives relative to that asset manager’s specified AUM. Numerous SMA Clients use derivatives as part of an overall investment strategy, with FX as the most common underlier due to the typical need to hedge currency exposure.

SMA Clients typically invest in different investment strategies through a multitude of asset managers in order to achieve diversity of investment perspectives, expertise, and asset allocations and to mitigate concentration risks. While the number of strategies and external asset managers employed by every SMA Client or client type is not the same, large pension funds, endowments, corporations or other institutional investors may have multiple asset managers trading OTC derivatives

²³ See Letter Re: Margin Requirements for Non-Centrally Cleared Derivatives – Final Stages of Initial Margin Phase-In (Sept. 12, 2018) at 7, available at <https://www.isda.org/a/5evEE/Initial-Margin-Phase-In-Implementation-Joint-Trade-Association-Comments.pdf>. The concepts of “SIMM” and “GRID” are explained in Part I.C.1.

on their behalf and, as principal, will face the same SD and its consolidated affiliates through each asset manager.²⁴

While the legal entity that constitutes the SMA Client (e.g., “ABC pension fund” or “University XYZ Endowment”) will be the same across the ISDA master agreement(s) and credit support documents entered into with each SD, the SMAs managed by each asset manager on behalf of the same SMA Client will be contractually treated as distinct counterparties in uncleared swap transactions, typically with liability limited (a/k/a ring-fenced) to the AUM allocated to the investment mandate. Moreover, each SMA will typically have its own payment and margin netting set for uncleared swaps transactions corresponding to each ISDA entered into by the relevant asset manager.²⁵ As a result, collateral movements for IM or VM are not netted across the SMA Client’s SMAs, including investment mandates pursued by the same asset manager, but instead, are covered under a separate, eligible master netting agreement per each strategy per asset manager.

Each asset manager has no transparency to, nor control over, any assets or trading activity for an SMA Client beyond its own AUM. SMA Clients usually require each asset manager to treat their individual trading mandates with confidentiality and do not share information across managers so no single manager would have access to or control over, all of the SMA Client’s overall assets. SD counterparties to SMA Clients are also bound by a duty of confidentiality to not share information across the asset managers for SMA Clients. As such, asset managers for a common SMA Client neither act in concert nor have visibility to the SMA Client’s overall trading activity. Consequently, a single asset manager for an SMA Client is unable to independently calculate or monitor an SMA Client’s aggregate AANA amount, IM Threshold or MTA across the SMA Client and all of its asset managers (and any

²⁴ For example, the Los Angeles County Employees Retirement Association (LACERA) in its 2019 Annual Financial Report provides a list of its investment managers organized by strategy and asset class. See LACERA 2019 Annual Financial Report at 125, available at: https://www.lacera.com/investments/Annual_Report/cafr/cafr.pdf.

²⁵ For example, swap dealer A may face ABC pension fund as principal on an ISDA negotiated and signed on behalf of ABC pension fund by Asset Manager 1 (managing 1% of the assets of the pension), while facing ABC pension fund on other ISDAs that were separately negotiated and signed by each of ABC pension fund’s other asset managers. Alternatively, ABC pension fund may negotiate its own ISDA with swap dealer A and each asset manager may establish a CSA to manage each payment and margin netting set separately. As such, each ISDA or CSA will have its own payment netting set, with eligible collateral, collateral haircuts and other features negotiated by the relevant asset manager, with such asset manager responsible for its own collateral movements.

consolidated affiliates of the SMA Client).²⁶ The SMA Client also does not coordinate or orchestrate the trading activities across its managers as it typically grants full investment discretion to each manager and as such, does not separately employ derivatives experts in-house. The Commission has recognized this lack of transparency and control as the basis to grant disaggregation relief in relation to SMA Clients under other CFTC regulations.²⁷

3. *Seeded Funds*

A seeded investment fund is a fund which has received a portion or all of its start-up capital from a parent or affiliate (each, a **sponsor**). While the sponsor may retain a passive, equity interest in the seeded fund, neither it nor its commonly consolidated entities controls or has transparency into the management or trading of the seeded fund and does not guarantee the obligations of the seeded fund. The asset manager retains independent management and investment discretion and has independent fiduciary duties to the other investors in the fund (if any). Additionally, the sponsor's exposure to the seeded fund is capped at its investment, similar to any other passive investment in a third party instrument or vehicle.

Although seeded funds do not independently have uncleared swaps exposures that pose significant risks to swap counterparties or the financial system, requiring consolidation with their sponsors for AANA purposes and/or IM Threshold purposes may result in the appearance of larger exposures that exceed the lower AANA thresholds of the remaining IM phases and the IM Threshold.

²⁶ These issues were raised at multiple points by the Asset Management Group (**AMG**) of the Securities Industry and Financial Markets Association (**SIFMA**) on behalf of multi-managed clients. See, e.g., Letter from SIFMA AMG to BCBS-IOSCO Re: Comment Letter on the Second Consultative Document for the Margin Requirements for Non-Centrally-Cleared Derivatives (Mar. 15, 2013), at 5-6, available at <https://www.sifma.org/resources/submissions/sifma-amg-submits-comments-to-the-bcbc-and-iosco-on-margin-requirements-for-non-centrally-cleared-derivatives/> (“[A] single client may have a number of separate accounts with different managers entering into derivatives on its behalf. Unlike the situation of affiliates within a corporate group that can communicate with each other to ensure they remain below a consolidated group threshold, multiple asset managers of a separate account client will not know of each other's existence or have the ability to manage the derivatives positions, on a group basis, to remain below a common threshold. Any concerted effort or shared communications would likely violate the managers' contractual or fiduciary obligations. In addition, a single asset manager may manage multiple accounts for the same separate account client, with no recourse or risk transfer between the accounts.”). However, regulators decided not to make changes to AANA or IM threshold requirements notwithstanding this feedback.

²⁷ See CFTC Regulation § 150.4(b)(4), 17 C.F.R. § 150.4(b)(4) (“Exemption for accounts carried by an independent account controller”).

In the Volcker Rule, the USPRs recognized that it is common practice to seed funds (in particular, retail funds) in order to build a track record in performance and attract third party investors and distributors when they provided an exemption for seeded funds from having to comply with the requirements of the Volcker Rule during a three-year seeding period.²⁸ Similarly, when determining how to calculate MSE for purposes of defining which entities constitute MSPs, the Commission declined to attribute the positions of a subsidiary to its parent in the absence of recourse.²⁹

C. SWAP DEALERS

1. *Small Covered Swap Entities*

The term “CSE” in the Margin Rules includes CFTC-registered swap dealers that are not regulated by a USPR. For purposes of this report, “**Small Covered Swap Entity**” (or **Small CSE**) refers to a dealer entity that is a CSE and that did not exceed the AANA thresholds in the prior phases (Phases 1 through 4) and may be subject to IM requirements in the remaining phases. According to the CFTC Margin Study, 20 SDs will begin posting and collecting IM in the remaining phases.³⁰ Under the Margin Rules, CSEs have the option to calculate the amount of mandatory IM using either a risk-based model or the standardized IM table set forth in the Margin Rules (such method based on the standardized IM table, **GRID**). All CSEs already subject to the IM requirements under Phases 1 through 4 have adopted the ISDA SIMMTM risk-based model (**SIMM**) to calculate IM and received the required regulatory approval to do so. By contrast, many Small CSEs intend to choose GRID based on the type of activity they primarily engage in (e.g., physical commodities) and customer classification (e.g., end users). The different IM calculation methodology

²⁸ 12 C.F.R. §248.12(a)(1); see also <https://www.federalreserve.gov/supervisionreg/faq.htm#16>.

²⁹ See Further Definition of “Swap Dealer,” “Security-Based Swap Dealer,” “Major Swap Participant,” “Major Security- Based Swap Participant” and “Eligible Contract Participant”, 77 Fed. Reg. 30,689 (May 23, 2012). Specifically, the Commission noted:

“We no longer take the position that a subsidiary’s swap or security-based swap position as a matter of course should be attributed to the subsidiary’s majority-owner parent. Instead, ... an entity’s swap or security-based swap positions in general would be attributed to a parent, other affiliate or guarantor for the purposes of the major participant analysis to the extent the counterparties to those positions would have recourse to that other entity in connection with the position. Positions would not be attributed in the absence of recourse.”

³⁰ See CFTC Margin Study at 5.

used by the CSEs in Phases 1 through 4 (i.e., SIMM) compared to the methodology used by Small CSEs (i.e., GRID) could create discrepancies when they face each other as counterparties, with GRID potentially requiring a higher amount of IM than would be required by SIMM. As discussed in Part II, such discrepancies could cause transaction disruptions or other delays.

2. *Dealers with Limited Bandwidth*

Large CSEs are a concentrated segment of the market. In a recent statement, the Honorable CFTC Chairman Tarbert noted that the biggest 40 SDs are all currently subject to IM requirements under the Margin Rules.³¹ While some post-financial reforms have made transactions with large banks less attractive by reducing counterparty protections,³² market structure has not materially changed to offer a broader range of alternative counterparties. One reason for this result is that many financial end users must transact with entities meeting certain regulatory counterparty eligibility requirements while other do so due to risk management standards.³³ Some financial end users also take comfort that large CSEs are subject to heightened capital and regulatory standards and therefore only approve trading with large CSEs or a smaller subset thereof. The costs and complex regulatory

³¹ See Statement of the Honorable CFTC Chairman Heath P. Tarbert in Support of Extending Relief for Initial Margin Requirements for Uncleared Swaps (Mar. 18, 2020), available at: <https://www.cftc.gov/PressRoom/SpeechesTestimony/tarbertstatement031820>.

³² For example, under bank supervisory rules adopted in the U.S. in 2017, global systemically important banks (GSIBs) are prohibited from entering into bilateral swaps and other QFCs that provide certain cross default rights and transfer restrictions upon the GSIB's bankruptcy or resolution proceeding, among other things. See, e.g., Board of Governors of the Federal Reserve System (Board), Final Rule, Restrictions on Qualified Financial Contracts of Systemically Important U.S. Banking Organizations and the U.S. Operations of Systemically Important Foreign Banking Organizations; Revisions to the Definition of Qualifying Master Netting Agreement and Related Definitions, 82 Fed. Reg. 42,882 (Sept. 12, 2017).

³³ See, e.g., for Irish UCITS, Central Bank (Supervision and Enforcement) Act 2013 (Section 48(1)) (Undertakings for Collective Investment in Transferable Securities) Regulations 2015 (SI No 420 of 2015) ("A responsible person shall only invest assets of the UCITS in an OTC derivative if the derivative counterparty is within at least one of the following categories: (a) a credit institution that is within any of the categories set out in Regulation 7; (b) an investment firm authorised in accordance with MiFID; or (c) a group company of an entity approved as a bank holding company by the Federal Reserve of the United States of America where that group company is subject to bank holding company consolidated supervision by the Federal Reserve.").

requirements for registered SDs have also deterred many alternative market participants from competing in this space.

Given this market concentration and reliance on large CSE, thousands of IM relationships will have to pass through yet another pinch point in order to comply with the IM requirements.

D. CUSTODIANS

As the number of new market participants scoped into Phases 5 and 6 is expected to be exponentially greater than all prior Phases combined, the demands for third party custodians and tri-party collateral agents' segregation services for regulatory IM has grown quite dramatically.

The lead time, however, required to set up the requisite segregated IM accounts is far longer and more complex than prior Phases. This is partly attributable to the extensive due diligence and background, credit and operational checks that need to be completed on new clients with whom the custodians do not have a prior relationship and the sheer volume of these new requests.

Some custodians have indicated that it may take as long as eight to twelve months to complete the segregation documentation and operational set up for Phase 5, and have imposed deadlines for initiating the documentation process well before the commencement of the relevant AANA calculation period. For end users, especially SMA Clients who may need to aggregate their AANA exposures for different calculation periods under different jurisdictional requirements from different asset managers, this in turn, will further exacerbate the pipeline challenges they face as they may not determine that they are in scope until a few months prior to the relevant compliance date, well after the deadlines set by most custodians.

II. Remaining Phases of Initial Margin for Uncleared Swaps: Challenges and Recommendations

A. ISSUES THAT SHOULD BE ADDRESSED IN IMMEDIATE TERM (PHASE 5 COMPLIANCE)

1. *Separate Compliance for Separately Managed Accounts*

- a) **Challenge:** Because SMAs Are Managed Independently Without Transparency Across Asset Managers, a CSE's Relationship with an SMA Client May Inadvertently Breach the \$50M Regulatory IM Threshold

Unique compliance issues arise where a CSE trades with an in-scope SMA Client that is advised by multiple asset managers. A typical example of this is a pension fund that hires 10 asset managers in order to diversify strategies and expertise; each asset manager will establish one or more SMAs for the benefit of the SMA Client and, where authorized to trade swaps, establish trading relationships with CSEs for the SMA. Given the limited number of CSEs in the market, each CSE will likely handle multiple SMAs for the same SMA Client; however, the CSE cannot provide each asset manager with transparency into all of the SMA Client's trading as it must limit information access to the asset manager's own portion. As the regulatory IM Threshold will need to be calculated by the CSE for the SMA Client in the aggregate, each SMA trading uncleared swaps will contribute towards the regulatory IM Threshold, but each asset manager will only know the regulatory IM for SMAs it is managing.

When an SMA Client comes into scope for the Margin Rules, it is unlikely that all of that SMA Client's SMAs will be papered under regulatory IM compliant documentation at the outset, and given the difficulties for CSEs in monitoring IM amounts on an intraday basis across multiple SMAs and multiple trading desks at the CSE, it is possible that the \$50M regulatory IM Threshold could be inadvertently breached. Once the CSE exceeds \$50M in uncollateralized regulatory IM exposure with an SMA Client across all of its asset managers, the CSE may feel it needs to interpret the Margin Rules as requiring it to cease trading activity with **all** asset managers for such SMA Client—even those acting under regulatory IM compliant documentation or within agreed regulatory IM sub-Threshold limits.

b) **Recommendation: Issue Interpretive Guidance to Confirm that a CSE Can Continue to Trade with an SMA Client in the Case of an Inadvertent Breach of the \$50M IM Threshold**

The Margin Subcommittee requests that the Commission confirm that the Margin Rules be interpreted to allow a CSE to continue to trade with certain SMAs of an SMA Client in the case of an inadvertent breach of the \$50M regulatory IM Threshold if (i) the asset manager for the SMA is trading under regulatory compliant IM documentation; or (ii) the CSE and asset manager for the SMA have agreed a regulatory IM sub-Threshold and the asset manager for the SMA is trading at or below the agreed regulatory IM sub-Threshold, provided that the CSE and the asset managers of the other SMAs of the SMA Client are no longer continuing to trade (absent other relief) and are working to reduce the aggregate uncollateralized regulatory IM exposure of the SMA Client back to at or under \$50M.

Therefore, on occasions where the SMA Client's uncollateralized regulatory IM exposure in the aggregate across all SMAs inadvertently exceeds the \$50M regulatory IM Threshold due to one or more SMAs exceeding a regulatory IM sub-Threshold without regulatory compliant documentation or trading without a regulatory IM sub-Threshold, this interpretation would provide certainty that the impact would be limited to only those SMAs. We have included as Appendix C, the application of this interpretive guidance in various scenarios. It is important to note that, pursuant to this interpretive guidance, the uncollateralized regulatory IM exposure for the SMA Client would promptly be reduced back to at or below \$50M due to the condition that SMAs breaching a regulatory IM sub-Threshold or trading without a regulatory IM sub-Threshold must cease trading until the breach at the CSE and SMA Client level is cured. Further, we do not believe this recommendation would require a rule change, but rather could be implemented as interpretive guidance from the Commission regarding the application of Margin Rules to multi-managed SMA Client relationships.

c) **Supporting Rationale for Recommendation**

Inadvertent Regulatory IM Threshold breaches may occur. None of the CSE, SMA Client or asset manager of an SMA will be able to determine *pre-trade* whether a transaction with an SMA will result in the SMA Client breaching its regulatory IM Threshold with the CSE. This outcome is due to a number of market realities, including:

- (i) Asset managers often place a trade order with a CSE for multiple accounts simultaneously (a **bunched order**). CSEs typically do not know at the

time of trade whether an SMA is part of the bunched order or how much of the bunched order will be allocated to the SMA post trade by the asset manager. Further, multiple trading desks at a CSE may trade with an SMA, and there may be legitimate business reasons to prevent different trading desks from coordinating their activities with a particular SMA (e.g., confidentiality requirements or information barriers within a CSE). While CSEs can and do calculate aggregate regulatory IM exposure at the SMA Client level, those calculations are typically end of day and cannot always be done on a real-time basis. These issues can prevent a CSE from knowing, pre-trade, if a transaction for an SMA will result in regulatory IM exposure above an agreed regulatory IM sub-Threshold of the SMA.

- (ii) The asset managers of SMAs operate independent of one another and typically do not have knowledge of the trading strategies or activities of the other asset managers engaged by the SMA Client.
- (iii) The SMA Client does not know real-time the trades that each asset manager is executing for its SMAs in order to determine whether its aggregate regulatory IM Threshold with a CSE will be breached. Even if the SMA Client had perfect transparency, SMA Clients typically do not have the ability to calculate regulatory IM amounts themselves.

CSEs will likely not repaper all SMA trading relationships quickly, or potentially at all. Entering into the necessary documentation and taking the operational steps required to enable regulatory IM compliant trading is a significant undertaking. Where an SMA historically has, or is expected to, engage in trading strategies that will result in large regulatory IM exposures (e.g., \$15M or more), a CSE will likely prioritize putting in place regulatory IM compliant documentation with that SMA.

However, not all SMAs will engage in strategies that are expected to produce meaningful regulatory IM exposure. For example, the only “swap” activity for some SMAs may be in Deliverable FX, which will not generate any regulatory IM exposure. Further, some SMA asset managers may only trade infrequently and/or in swaps with small notionals, and therefore only generate small (e.g., <\$1M) regulatory IM exposure.

For these SMAs, given the low expected regulatory IM usage, a CSE may decide to monitor and manage the relationship without repapering, with (or in some cases without) agreeing a regulatory IM sub-Threshold. A CSE may not want to allocate a regulatory IM sub-Threshold to SMAs with low expected IM usage as that would allow the CSE to dynamically manage IM exposure across those SMAs over time and

would enable the CSE and SMA Client to make better use of the aggregate regulatory IM Threshold of \$50M.

Even where a CSE decides to repaper SMA relationships, it may prioritize those SMAs which are heavier users of swaps—meaning some SMAs will take longer than others to complete documentation.

As a result, there will likely be at least some period of time where not all SMAs are repapered and SMAs may be competing for the same CSE and custodian resources.

Rationale for relief. If an SMA Client’s aggregate regulatory IM exposure exceeds the regulatory IM Threshold of \$50M, a CSE may interpret requirements conservatively in the absence of regulatory confirmation such that the CSA may feel that any additional transactions, even those with SMAs that have repapered their relationships or those with SMAs who are operating under their agreed regulatory IM sub-Threshold, cannot occur because those transactions could create additional uncollateralized regulatory IM exposure at the SMA Client level.

Without relief, SMAs trading with regulatory IM compliant documentation and/or SMAs acting within their regulatory IM sub-Threshold may unexpectedly have trading disruptions due to the activities of a different asset manager who exceeds its regulatory IM sub-Threshold or who has not completed the documentation requirements of the Margin Rules. Provided the CSE is promptly addressing the issue by working with the SMA Client and/or relevant SMA asset manager to remediate the problematic trades, it would be inconsistent with the purpose of the Margin Rules to interrupt trading for SMAs that are compliant with requirements.³⁴

2. ***Collateral Eligibility Requirements for Money Market Funds***

a) **Challenge: Restrictions on the Eligibility of Money Market Funds as IM Collateral Broadly Disqualify Most Money Market Funds**

The Margin Rules permit CSEs and covered counterparties to use MMFs as regulatory IM, provided that the MMF holds only U.S. Treasuries (or securities unconditionally guaranteed by the U.S. Treasury), and cash funds denominated in U.S. dollars or similar quality government securities.³⁵ However, the Margin Rules

³⁴ See Appendix C for examples.

³⁵ See CFTC Regulation § 23.156(a)(1)(ix)(B), 17 C.F.R. § 23.156(a)(1)(ix)(B) (“Securities denominated in a common currency and issued by, or fully guaranteed as to the payment of principal and interest

significantly restrict the use of MMFs as eligible collateral by requiring that “[a]ssets of the fund *may not be transferred through securities lending, securities borrowing, repurchase agreements, reverse repurchase agreements or other similar means . . .*”³⁶

Nearly all U.S. MMFs engage in some form of these activities, or are authorized to do so, and therefore these limitations would severely reduce the number of MMFs that would qualify as IM under the Margin Rules to less than a handful worldwide. One leading custodial bank researched all the U.S. MMFs currently available to its institutional clients in the U.S. and found only four that would meet these new requirements. Additionally, the industry is not aware of a single MMF that would qualify as eligible IM under the CFTC’s Margin Rules, the USPRs’ uncleared swap margin rules (the **USPR Margin Rules**),³⁷ and the European Union’s (EU) uncleared swap margin rules (the **EU Margin Rules**).³⁸ As a result, absent any action or relief by the Commission:

- this efficient form of IM widely used by financial end users may be severely undermined and unduly disrupted (especially for financial end users who combine voluntary IM on legacy transactions with mandatory IM on new in-scope trades);
- any MMF IM pledged to CSEs may be concentrated in only a few eligible MMFs (which presents other systemic risks);

by, the European Central Bank or a sovereign entity that is assigned no higher than a 20 percent risk weight under the capital rules applicable to swap dealers subject to regulation by a prudential regulator, and immediately-available cash funds denominated in the same currency...”); *see also* Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 81 Fed. Reg. 636, 701 (Jan. 6, 2016).

³⁶ *See* § 23.156(a)(1)(ix)(C), 17 C.F.R. § 23.156(a)(1)(ix)(C) (emphasis added); *see also* 12 C.F.R. 45.6 (Comptroller of Currency eligible collateral); 12 C.F.R. 45.7 (Comptroller of Currency segregation of collateral); 12 C.F.R. 237.6 (Federal Reserve eligible collateral); 12 C.F.R. 237.7 (Federal Reserve segregation of collateral); 12 CFR 349.6 (FDIC eligible collateral) 12 C.F.R. § 349.7 (FDIC segregation of collateral); 12 C.R.F. 624.6 (FCA eligible collateral); 12 C.F.R. 624.7 (FCA segregation of collateral); 12 C.F.R. 1221.6 (FHFA eligible collateral); 12 C.F.R. 1221.7 (FHFA segregation of collateral).

³⁷ *See* Margin and Capital Requirements for Covered Swap Entities, 80 Fed. Reg. 74,840 (Nov. 30, 2015).

³⁸ *See* Commission Delegated Regulation No. 2016/2251 of October 4, 2016 Supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council of July 4, 2012 on OTC Derivatives, Central Counterparties and Trade Repositories with Regard to Regulatory Technical Standards for Risk-Mitigation Techniques for OTC Derivative Contracts Not Cleared by a Central Counterparty (as corrected by Commission Delegated Regulation (EU) 2017/323 of January 20, 2017).

- financial end users may be forced to use other less efficient or ideal forms of non-cash IM collateral (thus, increasing costs, settlement delays, tracking errors and operational burdens); and
- absent the use of substituted compliance or any further actions by other regulators, financial end users may be forced to use different MMFs or other forms of eligible IM when trading with U.S. and EU CSEs and also potentially causing asset managers to be forced to break up block trades across U.S. and non-U.S. clients with similar strategies when trading with a single CSE (applying different margin calculations) due to pricing differentials as a result of the different form of IM being pledged.

b) Recommendation: Eliminate Undue Restrictions on Eligibility of Money Market Funds

For Phases 5 and 6 and beyond, the Margin Subcommittee recommends eliminating the undue restrictions on MMFs’ activities under subparagraph (C) of Section 23.156(a)(ix) of the Margin Rules. This would allow for a broader selection of MMFs that are eligible for regulatory IM and thereby, mitigate any concentration risks and permit the uninterrupted use of existing MMFs by financial end users for legacy and new in-scope transactions.

c) Supporting Rationale for Recommendation

Under the Margin Rules, the Commission highlighted that the restrictions on a MMF’s use of securities lending, securities borrowing, reverse repurchase agreements, or similar arrangements was to “ensure consistency with the prohibition under the final rule against custodian rehypothecation of initial margin collateral”.³⁹ However, in the MMF sweep arrangements, under no circumstances does the pledgor’s custodian have any right to rehypothecate, reuse the IM collateral or take any other independent actions with respect to the pledged MMF shares. Instead, the CSE and financial end user agree upfront in the collateral documentation to the list of eligible MMFs and any associated haircuts, as pledgor any cash sweep into a MMF is instructed by the financial end user or its manager and absent any default, any transfers into and out of the collateral account by the custodian is instructed by the financial end user and agreed to by the CSE (as secured party).

³⁹ See Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 81 Fed. Reg. 636, 666 (Jan. 6, 2016).

Since the financial crisis of 2008, buy-side market participants have steadily increased the use of third party custodians to segregate voluntary IM away from SD counterparties. Also, as margin transfer deadlines continue to contract from a regulatory perspective, there has been a growing use of MMFs as a secure and efficient alternative to cash margin. MMFs are highly regulated short-term investment vehicles that are subject to liquidity and diversification requirements under U.S. and European MMF regulations, such as SEC Rule 2a-7. Many custodians offer money market sweep programs that allow buy-side entities, asset managers and end-user clients the continued operational ease of pledging cash⁴⁰ into segregated collateral accounts and then instructing the custodian to sweep such cash into MMF shares that are pledged as collateral to SD counterparties. MMFs invest predominantly in treasuries and other high quality, short-term government securities. The Commission has recognized such MMFs as safe, high quality investments, such as under CFTC Regulation 1.25 which permits the investment of customer margin by futures commission merchants (FCMs) without similar restrictions.⁴¹

Figure 2. Key reasons for enabling use of MMFs as eligible collateral

1. Cash settlement process is efficient, fungible, and meets compressed margin transfer timeframes. Firms may not have ready access to eligible non-cash collateral.
2. Firms may not have the optimal infrastructure and/or capacity to efficiently buy and transfer other eligible non-cash collateral.
3. Transformation outside the custodian can be costly for firms with less scale.
4. Holding securities specifically in anticipation of collateral calls creates a drag on performance, decreasing investment performance for end investors and increasing tracking errors.
5. There are situations where collateral transformation is not possible or practical prior to posting without ready access to MMFs e.g., due to reinvestment/custodian cut-off times.

These sweep arrangements afford buy-side market participants with the ability to timely and efficiently meet margin calls in compressed timeframes first in cash, without settlement delays or having traders (outside of collateral management operations) constantly buying or selling treasuries or other non-cash assets or dealing with odd lot sizes, transaction costs and other settlement issues. Additionally, the sweep into MMFs also allows buy-side market participants to

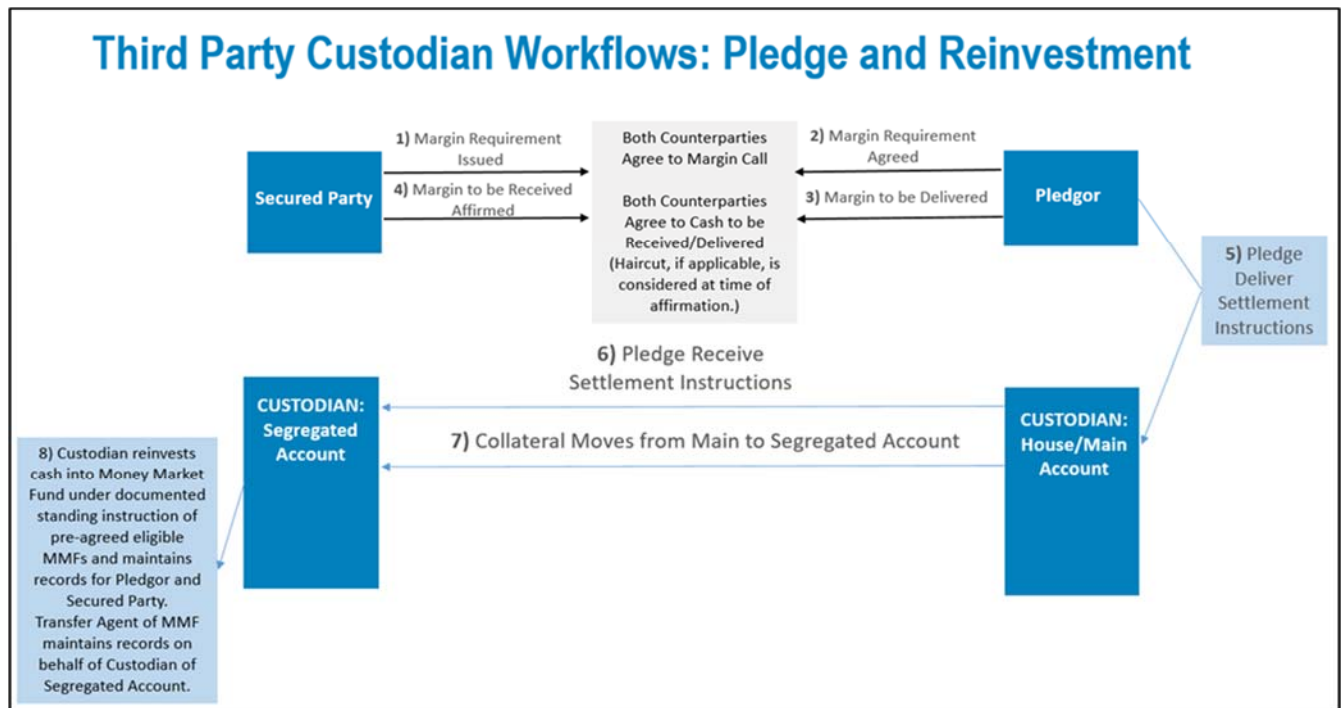
⁴⁰ According to the latest ISDA Margin Survey, 73% of derivatives collateral posted is cash. ISDA YE 2019 Margin Survey at 10.

⁴¹ Pursuant to CFTC Regulation 1.25(b)(3)(i)(E) and (c), an MMF is a permissible investment without limits for customer funds by an FCM so long as it meets certain requirements and does not voluntarily elect to be subject to liquidity fees or redemption restrictions. *See also* CFTC No-Action Letter No. 16-68 (Aug. 8, 2016). Additionally, CFTC Regulation 1.25 specifically permits, subject to certain conditions, FCMs to buy and sell otherwise permitted investments pursuant to repurchase and reverse repurchase agreements.

effectively mitigate insolvency risks to the custodians as non-cash collateral would not be consolidated with the custodian’s balance sheet or estate from a supplemental leverage ratio and bankruptcy perspective. Finally, the use of MMFs may avoid risk of potential negative interest rate charges that may be charged by custodian banks on cash collateral.

Most multi-billion dollar MMFs available to the institutional marketplace use securities lending, repurchase agreements, reverse repurchase agreements, and similar instruments in order to earn returns on cash and other high quality assets, avoid any cash drag on performance, diversify its investments and mitigate its potential exposure to its custodian’s insolvency and any consolidation issues with respect to any cash held at the custodian. The MMF’s asset manager, as its fiduciary, would determine the types of investments and transactions would be in the best interest of the MMF and its investors. Neither the buy-side market participant pledging MMF shares as eligible IM collateral nor its SD counterparty has any transparency or control as to the trading activities or investments of the MMF.

Figure 3



Additionally, over the past few years, there have been unusual strains in the Treasury repo market which has led the Federal Reserve to take additional measures “to

mitigate the risk of money market pressures”.⁴² The vast majority of U.S. government MMFS engage in prudent repo, reverse repo, and securities lending. If the Margin Rules require financial end users to move 10s of billions in collateral out of those existing MMFs and into cash or the few eligible MMFs, it could create new and continuing trading and liquidity disruptions and concentration risks in this critical market.⁴³

To the extent that the CFTC (and USPRs) were to adopt the Margin Subcommittee’s recommendation and eliminate the undue restrictions on the underlying activities of eligible MMFs, there are still further complications for financial end users that are pledging IM to both U.S. and EU CSEs under different margin regimes as well as for asset managers trading in blocks across U.S. and EU clients with a single CSE that may apply different margin rules.⁴⁴ Absent measures by the EU regulators to also eliminate undue restrictions and operationally challenging conditions on the use of MMFs, to our knowledge, there are no MMFs that are eligible under both the EU Margin Rules and either the CFTC’s Margin Rules or the USPR Margin Rules. As a result, these restrictions significantly decrease the viable options for eligible collateral and efficient collateral management considering settlement and transfer timing limitations and global fragmentation.

3. ***Seeded Funds – Scoping Issue***

a) **Challenge: Seeded Funds Unduly Come in Scope Due to Consolidation with Passive Sponsors**

Under the Margin Rules, seeded funds are required to consolidate their AANA exposures with their passive sponsors (and their consolidated affiliates) that may have MSE and therefore may have to post regulatory IM during the critical time in which they are trying to establish a performance track record. This puts these seeded funds at a disadvantage to their global and domestic competitors who are not similarly burdened under other margin regimes.

⁴² See Board of Governors of the Federal Reserve System, Statement Regarding Monetary Policy Implementation (Oct. 11, 2019), available at <https://www.federalreserve.gov/newsevents/pressreleases/monetary20191011a.htm>.

⁴³ The shift in margin is expected for market participants who will not preserve legacy netting sets but instead combine existing trades with voluntary IM with new in-scope transactions.

⁴⁴ For example, an EU domiciled CSE may apply the EU Margin Rules when trading with EU domiciled clients, but may apply the CFTC’s Margin Rules when trading with U.S. Persons.

b) Recommendation: Provide Exemption from Consolidation of Seeded Funds with Sponsors for Purposes of AANA Calculation

For Phases 5 and 6 and beyond, the Margin Subcommittee recommends that the Commission publish a time-limited no-action letter to exempt seeded investment funds from having to post IM until the Commission can adopt the following language via rule making:

“Investment funds that are managed by an investment advisor are considered distinct entities that are treated separately when applying the AANA and IM Threshold as long as the funds are distinct legal entities that are not collateralized by or are otherwise guaranteed or supported by, investment funds and other sponsors or the investment advisor in the event of fund insolvency or bankruptcy and shall not be considered to be an "affiliate" or "margin affiliate" of any other entity for a period of three years after such investment fund commences trading.”

This language is a verbatim restatement of the BCBS-IOSCO final statement on margin requirements for non-centrally cleared derivatives (which specifically excluded all investment funds that are not collateralized or otherwise guaranteed or supported by an affiliate to be excluded from the definition of a group for purposes of calculating the group’s AANA) except for the addition of the time limited seeding period at the end of the BCBS-IOSCO language: “for a period of three years after such investment fund commences trading”.⁴⁵

c) Supporting Rationale for Recommendation

Global Harmonization. This relief would put U.S. seeded funds on a level playing field globally with non-U.S. seeded funds that are not subject to the same consolidation requirements under other margin regimes. Regulators in other jurisdictions, including the EU, Japan, Australia and Canada, have fully adopted the BCBS-IOSCO’s investment fund exception without similar limitations.⁴⁶ The

⁴⁵ See Footnote 10 to Requirement 2.2 of the BCBS-IOSCO framework, available at <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD651.pdf>.

⁴⁶ The EU adopted this approach via Paragraph 13 of Commission Delegated Regulation No. 2016/2251 of October 4, 2016 Supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council of July 4, 2012 on OTC Derivatives, Central Counterparties and Trade Repositories with Regard to Regulatory Technical Standards for Risk-Mitigation Techniques for OTC Derivative Contracts Not Cleared by a Central Counterparty, 2016 O.J. L340/11, available at <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32016R2251&from=EN>. Canada adopted this approach via *Margin Requirements for Non-Centrally Cleared Derivatives* by the Office of the Superintendent of Financial Institutions of Canada effective as of June 2017, available at

Margin Subcommittee is not asking for the Commission to adopt BCBS/IOSCO's investment fund exemption with no time limit. Instead, we are asking for a time-limited exemption for seeded funds during a three year seeding period, typically after which, seeded funds have established a sufficient performance track record to draw in distributors and third party investors and are no longer consolidated with their sponsor or affiliates for AANA purposes.

To the extent that the Commission does not address this issue, U.S. CSEs may also be exposed to a reduction in liquidity and trading disruptions as EU seeded funds may intentionally limit their trading activities to non-U.S. CSEs to take advantage of the EU consolidation exemption.

Consistency with Prior Relief on Seeded Funds. The requested relief is consistent with the treatment of seeded funds by the Federal Reserve and the Commission under the Volcker Rule. In answers to frequently asked questions published on July 16, 2015, the Federal Reserve elected to exclude seeded funds from the requirements of the Volcker Rule during a three year seeding period recognizing the importance of allowing seeded funds time for the "...testing the fund's investment strategy, establishing a track record of the fund's performance for marketing purposes, and attempting to distribute the fund's shares."⁴⁷

This relief would be also consistent with the Commission's approach to MSP calculations. When adopting the MSP calculations, the Commission declined to attribute the positions of a subsidiary to its parent in the absence of any contractual recourse. Specifically, the Commission noted:

"We no longer take the position that a subsidiary's swap or security-based swap position as a matter of course should be attributed to the subsidiary's majority-owner parent. Instead, ... an entity's swap or security-based swap positions in general would be attributed to a parent, other affiliate or guarantor for the purposes

<http://www.osfi-bsif.gc.ca/Eng/Docs/e22.pdf>. The JFSA published the final Japanese margin rules on March 31, 2016 by way of amendments to the Cabinet Office Ordinance concerning Financial Instruments Business, etc. as one of the subordinate regulations of the Financial Instruments and Exchange Act. The Australian Prudential Regulation Authority (APRA) adopted the BCBS-IOSCO framework through the Banking, Insurance, Life Insurance and Superannuation (prudential standard) determination No. 1 of 2017 Standard CPS 226 Margining and risk mitigation for non-centrally cleared derivatives.

⁴⁷ See Board of Governors of the Federal Reserve System, Volcker Rule FAQ, Foreign Public Fund Seeding Vehicles (June 10, 2014), available at <https://www.federalreserve.gov/supervisionreg/faq.htm#5>.

of the major participant analysis to the extent the counterparties to those positions would have recourse to that other entity in connection with the position. Positions would not be attributed in the absence of recourse.”⁴⁸

Seeded Funds Do Not Pose Systemic Risk. Seeded funds are typically capitalized with \$50-100M and have little notional exposure (and are, for the purposes of the relief being sought, not guaranteed by their sponsor/investment adviser). Additionally, swap dealer counterparties to seeded funds generally do not have any recourse to a seeded fund’s sponsor or investment adviser.

An informal sampling in 2018 of members of SIFMA AMG and the American Council of Life Insurers identified that respondents had a total of 33 seeded funds that will be in scope due to their derivatives notional exposures being consolidated with entities with MSE. Absent consolidation with their sponsors, these 33 seeded funds had derivatives with a combined gross notional amount of \$938M relative to \$2.7B of total net asset value, and the average gross notional exposure for each seeded fund was \$32M. Therefore, none of these seeded funds would be in scope under the Margin Rules absent the consolidation requirements. Even though these seeded funds do not pose the type of systemic risk that the Commission, BCBS-IOSCO and other global regulators are properly attempting to mitigate with the implementation of the IM regime, these seeded funds will have to pledge IM under the U.S. margin regime as if they did pose a systemic risk to the financial system.

As an odd result, the obligation to pledge regulatory IM will either negatively impact a seeded fund’s performance or inhibit its ability to trade (if CSEs decline to repaper and exchange IM with the seeded fund) which defeats the whole purpose of the original seed capital. In addition, once third party capital is invested in a seeded fund and it is no longer required to consolidate with its sponsor or its affiliates, such seeded fund will grow larger and have more of a market impact on an individual basis, but since it will no longer be affiliates of an entity that has MSE, it will no longer exceed the AANA thresholds or potentially have to pledge IM.

Existing Risk Mitigation Applicable to Seeded Funds. Seeded funds remain subject to the VM requirements of the Margin Rules and will still be required to post at a minimum the required regulatory VM collateral on a daily basis, thus mitigating any risk such funds might pose to the overall financial system.

⁴⁸ Further Definition of “Swap Dealer,” “Security-Based Swap Dealer,” “Major Swap Participant,” “Major Security- Based Swap Participant” and “Eligible Contract Participant”, 77 Fed. Reg. 30,689 (May 23, 2012).

Also, seeded funds that trade derivatives are commodity pools that will be subject to the Commission's jurisdiction. Most seeded funds will rely on the de minimis exemptions to registration as a commodity pool provided by Rules 4.13(a)(3) or 4.5. If a seeded fund were to breach the limits set forth in those exemptions, then such seeded fund would be required to register with the Commission and provide additional reporting and transparency to the Commission with respect to its derivative positions.

Additionally, retail funds such as U.S. registered investment companies and European funds known as Undertakings for the Collective Investment in Transferable Securities (UCITS) and sociétés d'investissement à capital variable (SICAVs) are highly regulated entities subject to other regulatory regimes that limit their use of leverage and derivative instruments, which further prevent these types of seeded funds from generating systemic risk.

Performance Drag and Operational Costs. While the amount of IM posted by any specific seeded fund is expected to be negligible as compared to the overall size of the market for uncleared OTC derivatives, such amounts may be material to a fund in its start-up phase and result in performance drag to investors.

Performance drag will be especially felt in seeded funds that will not otherwise hold assets that are eligible collateral—with one day posting requirements this will generally take the form of a larger cash reserve (which cannot be used in the fund's investment thesis), but could also involve transformation costs of changing assets held by the fund that are ineligible for IM to IM-eligible assets.

Equity-focused funds, emerging markets funds and others may be especially hard hit. Smaller funds that are less able to spread set-up and maintenance costs of required margin accounts will also be more impacted than larger seeded funds.

In addition to drag from holding additional cash or transforming assets to assets that are eligible for IM, the funds will incur costs of setting up and maintaining margin accounts, hiring a custodian to handle IM, and other costs as a result of being required to post IM to CSE counterparties.

Such funds will also need to negotiate and complete complex margin documentation and develop compliance infrastructure to handle the posting and receiving IM at a cost not commensurate with their risk to the financial system.

Because of their small size, seeded funds are likely to encounter documentation issues as counterparties and custodians address similar documentation across their

client base—faced with a bottleneck, counterparties and custodians are likely to prioritize larger AUM clients.

Unlike larger entities that are not consolidated, seeded funds may not be able to take advantage of the \$50M IM Threshold in the Margin Rules, or such relief may be limited, because of potential fiduciary conflicts or confidentiality wall issues as between the fund, the investment adviser, the ultimate sponsor/parent and other affiliates of the sponsor/parent. This may be particularly acute for life insurance companies with fiduciary duties to mutualized policyholders or shareholders.

Some companies that may be consolidated for financial purposes are entirely distinct legally and operationally. As a result, they may not have the ability to share the AANA exposure information required to manage the \$50M IM Threshold. For example: determining an equitable division of the IM Threshold relief between the ultimate parent's hedging activity and the seeded fund's derivatives activity (in a list of funds that will constantly change) may be difficult to determine (or monitor) as the parent owes fiduciary duties to one group, while the fund investment adviser may owe them to different groups of investors in its various seeded funds. Additionally, there could be regulatory wall issues that would not permit any trade level information to be shared between a seeded fund and its sponsor/parent and other affiliates. For example, an insurance company making a seed investment in a fund would not share the fund's trading activity with an affiliate trading swaps to hedge general insurance risk.

Funds that are variable interest entities may consolidate at a threshold of 10% ownership, which means fund managers need to look not just their own affiliated entity consolidation issues, but whether any investor can consolidate the fund on its financial statements, in case that entity has MSE.

Domestic Harmonization. If a fund sponsor/seeder does not have MSE, then any fund it sponsors/seeds will not have to post IM or bear the operational costs of establishing and maintaining the infrastructure necessary to post and collect IM provided that the seeded fund is not otherwise consolidated with affiliates that collectively have MSE. A seeded fund that does have to post IM and bear these operational cost will be significantly disadvantaged vis-à-vis its domestic competitors which creates an uneven playing field for seeded funds here in the United States.

4. ***Small Covered Swap Entities and IM Calculation***

a) **Challenge: Small CSEs Using GRID May Not Be Able to Reconcile IM Calculations with CSE Counterparties Using SIMM Model**

Under the Margin Rules, CSEs have the option to use either a quantitative IM model, like the SIMM, or GRID to calculate the initial margin amount for the purpose of collecting or posting IM and to determine whether the \$50M IM Threshold has been exceeded. Many Phases 5 and 6 Small CSEs coming into compliance with the IM requirements have elected or intend to elect to utilize GRID. Due to the differing nature of the risk calculations between the GRID and the SIMM approach widely used by the larger CSEs, this may create potential barriers to Phase 5 and 6 Small CSEs from being able to engage in swaps transactions.

b) **Recommendation: Remove Barriers for Small CSEs to Rely on Their CSE Counterparty's SIMM Calculations**

The Margin Subcommittee recommends amending the Margin Rules prior to the compliance date for Phase 5 by adding new subparagraph (iii) to CFTC Regulation 23.154(a)(1) as follows:

§ 23.154(a)(1)(iii) For those covered swaps transactions where a covered swap entity having elected the table-based method pursuant to § 23.154(c) is transacting with a covered counterparty which uses a risk model approved pursuant to § 23.154(b) or approved by a Prudential Regulator, the parties may agree to use the IM calculation generated by the risk model subject to the following requirements:

- A. The parties must agree in writing that such IM calculation will be used to determine the amount of IM to be collected from the covered counterparty, and to determine whether the \$50 million IM Threshold amount has been exceeded, requiring compliance with the documentation requirements pursuant to §§ 23.157 and 23.158; and
- B. The parties must agree in writing that the IM calculation will be provided to the covered swap entity in such a manner and timeframe that would allow the covered swap entity to comply with § 23.152.

To the extent that the Commission is unable to amend the Margin Rules prior to September 1, 2020, we respectfully request that prior to such date the Commission issue interpretative guidance or an extension of the relief provided to Cargill

Incorporated pursuant to the CFTC's No-Action Letter dated December 19, 2019 (**Cargill NAL**), to all CSEs, including all Small CSEs using GRID. Additionally, for the reasons specified below, we respectfully request that the relief should apply to all swaps transactions, not just those entered into for the purpose of hedging.

c) Supporting Rationale for Recommendation

As noted in Part I of this report, a number of Small CSEs will be phased into the Margin Rules during Phases 5 and 6. Under the Margin Rules, CSEs have the option to calculate IM by using either (1) an approved risk-based model like SIMM, or (2) GRID. The SIMM calculates IM as the potential future exposure of a swap or a netting set of swaps which allows for a more finely calibrated approach. The GRID specifies the minimum IM that must be posted and collected as a percentage of a swap's notional amount, which varies based on the asset class and currency of the swap. In most cases, the SIMM calculates a lower IM number than the GRID, which is based on a notional value calculation.

The GRID is simpler to administer and does not require implementing more complicated systems. As a result, Small CSEs in Phases 5 and 6 will be using a different methodology to calculate IM from the CSEs in Phases 1 through 4. A primary concern is that GRID may result in the calculation of a much larger IM amount. As a result, CSE counterparties may decline to trade with Small CSEs if they are required to post a higher amount of IM than would be required by SIMM. This may have the additional consequence of disproportionately impacting liquidity in certain markets where there are fewer swap providers. Further, even if the CSE counterparty is willing to post a higher IM amount in order to transact with the Small CSE, this will result in higher transaction costs.

To illustrate, Phase 5 and 6 CSEs are already seeing how the GRID calculation of IM has the potential to cause an acceleration of reaching the \$50M IM Threshold for compliance with the IM documentation requirements. If allowed to proceed, the limited bandwidth of custodians and larger CSEs (discussed above) would become further congested. These larger CSEs and custodians are dealing with setting up thousands of counterparties over the next 2 years during Phases 5 and 6. Each covered counterparty margin pair will require approximately 5-10 documents/agreements collectively. If an entity is not close to the \$50M IM Threshold using SIMM, given the number of covered counterparties coming into compliance in Phases 5 and 6, it is unlikely they will be prioritized by larger CSEs and custodians to begin exchanging documents for onboarding.

One example of the stark differential in the calculation of IM between GRID and SIMM is the “Municipal Prepayment Transactions.”⁴⁹ Using GRID to calculate IM means that the IM obligation will likely be based on a notional value totaling a twenty-to-thirty-year exposure, which would be much larger than the IM risk valuation of the same transaction using SIMM and arguably inconsistent with the purpose and intent of IM. If a Small CSE using GRID must calculate IM based on a twenty-year notional value calculation, CSE counterparties in Phases 1 through 4 will no longer participate in these types of transactions with the Small CSE or if they do, the transaction will result in significantly higher transaction costs.

Extending the requested relief to non-hedge transactions would not curtail the Small CSE’s obligation to operate with the parameters of its risk management program under 23.600. All CSEs will continue to be required to have in place robust risk management programs as outlined by the CFTC and reviewed regularly by the National Futures Association (NFA) that set forth Value-at-Risk (VaR) limits applicable to all transactions to control systemic risk, and all transactions between CSEs are already subject to VM requirements. Additionally, the requested relief will result in an exchange of an appropriate level of IM between CSEs, even if it is based on one of the covered counterparty’s ISDA SIMM calculation.

Operationally, for many CSEs it is extremely difficult to separate hedging from dealing on a transaction-by-transaction basis since CSEs often manage hedging on a portfolio basis and transact both hedging and dealing swaps under a single ISDA Master Agreement. Therefore, limiting the relief to hedge transactions may diminish its utility for Small CSEs. As a result, this restriction has the potential to remove liquidity from the market for the reasons stated above. The CFTC has recognized that liquidity in the commodities markets is essential to allow market participants to hedge their commercial risk, so any measure that inadvertently harms liquidity should be avoided, if possible.

⁴⁹ Municipal Prepayment Transactions involve matched commodity swaps used to hedge a municipality’s prepayment for the supply of long-term (*e.g.*, 20-30 year) natural gas or electricity requirements. The matched swaps allow the parties to hedge their respective exposures to the changing price of the natural gas or electricity underlying the transaction with a single CSE. They expressly contain no mark-to-market credit exposure to participants upon either early termination or replacement events. The matched swaps thus economically offset each other in every way. Under the structure of the Municipal Prepayment Transactions, neither swap will survive the termination of the prepayment transaction, and the prepayment transaction will not survive if both commodity swaps do not remain in place. Accordingly, there is no counterparty, safety and soundness, or systemic risk associated with the matched commodity swaps in Municipal Prepayment Transactions.

5. ***Documentation and Account Set-Up - Industry Implementation Issue***

a) **Challenge: Pipeline Congestion and Other Obstacles Pose Delays for Completion of IM Documentation and Account Set-Up and May Result in Trading Disruptions and Loss of Hedges**

Financial end users and Small CSEs that will be in scope for Phases 5 and 6 and beyond are facing various challenges to completing documentation and operational steps necessary to comply with the Margin Rules before the relevant compliance dates and therefore, may be shut out of trading of derivatives.

Even if the CFTC (and other global regulators) grant an extension of the Phase 5 and Phase 6 compliance dates in accordance with the BCBS-IOSCO recommendation for relief related to the COVID-19 pandemic, market participants coming into scope for any newly scheduled Phase 5 and Phase 6 (and beyond) will still face pipeline issues and other obstacles that may delay getting IM compliant documentation and accounts in place. This extension of the compliance dates would not resolve these pipeline issues as the primary purpose of the extension is to give market participants the necessary time to mitigate the effects of the COVID-19 crisis, which has caused extreme market volatility and uncertainty. During the pandemic, firms have had to redeploy depleting resources to deal with market closures, trading suspensions, thinning liquidity and wider bid-ask offers, among other issues. With such resources appropriately redirected towards risk management and business continuity as well as covering for colleagues who are sick or caring for family members who are ill, counterparties and custodians will likely not be able to make material progress on IM documentation and account set up, and the same congestion issues will likely remain once implementation is expected under the new compliance dates. The extensions also will not solve for the compressed timeframes between the end of the AANA calculation periods and the relevant compliance dates. In other words, the extension of Phase 5 and Phase 6 compliance dates—while extremely helpful and necessary in light of the havoc being wreaked by COVID-19 on the global financial landscape—will not afford additional time to resolve the various margin implementation issues faced by the industry even before the COVID-19 crisis, but instead will bring those issues to a head at a later date.

b) **Recommendation: Provide 6-Month Forbearance Period**

The Margin Subcommittee requests that the Commission grant each CSE (and its consolidated affiliates) to financial end user (and its consolidated affiliates)/Small

CSE relationship, a one-time, 6-month grace period for compliance with the Margin Rules, commencing from the day the regulatory IM amount for the relationship exceeds the \$50M IM Threshold. We would ask that such grace period:

- 1) Be applicable to all types of financial end users and Small CSEs, subject to certain potential modifications in the context of SMAs, as will be discussed further in Part II.B.2;
- 2) Is time limited to Phases 5 and 6, and to be revisited for future compliance dates based on the number of accounts likely to be in scope for such date and the experience of market participants in Phases 5 and 6;
- 3) Be conditioned on the parties coming into compliance with the Margin Rules as soon as they are able to do so within the 6-month grace period; and
- 4) Could be provided immediately in the form of no-action relief or a statement of forbearance from enforcement against the CSE.

c) Supporting Rationale for Recommendation

The grace period is critical for market participants in Phases 5 and 6 who are urgently trying to enter into regulatory IM compliant documentation and be operationally ready by the applicable compliance date given the various challenges they currently face, that include, but are not limited to:

1. Account opening, document negotiation and operational set up for an in-scope relationship is estimated to take as long as 12-18 months leading up to a compliance date due to the large number of relationships coming into scope for Phases 5 and 6 and potentially thereafter as well. This includes, but is not limited to:
 - a. Negotiating amendments or new ISDA Master Agreements and Credit Support Annexes (**CSAs**) and agreeing, as needed, to how regulatory IM will overlay with existing Independent Amount margin requirements and whether legacy transactions will be margined together or separately from new in-scope transactions;
 - b. Negotiating allocations of the IM Thresholds with each CSE for each SMA client;
 - c. Establishing electronic communications channels and procedures among the counterparties and custodians;
 - d. Agreeing to the relevant jurisdictional margin requirements and margin methodology that apply to the different counterparty combinations and asset classes; and
 - e. Completing the necessary IM testing, file exchanges and reconciliations and operational set-ups among counterparties, custodians and any vendor platforms.

2. The AANA measurement period for Phase 5 is March, April and May of 2020 (2021 under the BCBS/IOSCO recommendations), which means that a financial end user will not know with certainty that it is in scope for Phase 5 until the end of May. However, some custodians have established deadlines for document negotiations to be completed that are well in advance of the end of May if a relationship is to be operationally ready by September 1, 2020 (or a delayed September 1, 2021). This is particularly challenging for SMA clients who need to aggregate data for the AANA period (not only under the CFTC's rules, but across all relevant jurisdictions) from various managers in order to determine if they have exceeded the AANA thresholds and will be required to exchange mandatory IM.
3. Some market participants are experiencing difficulty getting engagement from counterparties and/or custodians to start the documentation process for a variety of reasons such as low estimated SIMM numbers, unknown AANA numbers, or the mix of instruments traded (i.e., predominantly FX forwards which are not collateralized) resulting in de-prioritization of a relationship for repapering.
4. The template account control agreements with custodians to segregate IM (**Account Control Agreements**) to be used from Phase 5 for various custodial platforms, were only recently finalized by custodians and some templates are still under review by industry working groups as of April 2020. While Account Control Agreements were used by market participants in the prior phases, new templates are being drafted specifically for use in Phases 5 and beyond to enable market participants to negotiate those agreements in an efficient manner with end users' custodians who may not have been active in prior Phases.
5. Some CSEs prefer to use certain custodial platforms for their posting leg, but those platforms have only been used by CSEs. Onboarding non-CSE accounts to those platforms as the receiver of collateral is burdensome as the documentation is written with banks or CSEs in mind or they are based on new legal structures and documentation that have not been vetted in the prior phases.
6. There are a number of tasks that must be completed by the custodians, including but not limited to:
 - a. Assessing the applicable jurisdictions and required legal agreements based on the types of IM segregation arrangements;

- b. Performing the necessary “Know Your Customer” (KYC) due diligence on new clients as well as responding to similar inquiries from clients regarding the custodians’ financial stability, risk management, disaster recovery, business continuity, cyber security and data protection policies;
 - c. Determining the post-KYC documentation required for a new custody account, including credit documentation, settlement instructions, fee schedules, contact lists, user access requests, signatory lists and tax documentation; and
 - d. Completing tri-party documentation and operational set-up for the IM segregation, including the list of eligible collateral and haircut schedules based on the jurisdiction(s) of the clients. Due to the gross-gross nature of IM segregation, there can be 2-4 triparty documents and two eligible collateral schedules required for each relationship, as well as any custody documentation. See Appendix B for an illustration of the typical documentation involved in setting up arrangements for regulatory IM exchange and segregation.
7. For SMA Clients, there is the additional issue of multiple asset managers managing derivatives for the SMA Client’s accounts and having to discuss and agree an allocation of the IM Threshold with the SMA Client (as beneficial owner) and/or CSEs. The industry is dealing with this issue for the first time in Phases 5 and 6 and it remains to be seen how CSEs and SMA asset managers will resolve this challenge. Additional considerations related to SMA Clients include, but are limited to:
- a. SMA Clients may also need to perform due diligence and KYC analysis on new custodians used by their CSE counterparties, where they are the secured party in a transaction. In the case of an SMA, the asset managers may need to perform this as well; and
 - b. SMA Clients and each of their asset managers will have to determine if the SMA client, its custodian or each manager will negotiate and set up the IM segregation arrangements (including any additional custodial fees), if additional custodial accounts need to be opened and whether the asset managers have the requisite authority to act on behalf of the SMA Client in connection with the custodial arrangements. SMA asset managers may also need to comply with custody rules, such as under the Securities and Exchange Commission (SEC) regime based on the scope of the asset manager’s authority in relation to the custodial accounts.

Regarding the length of the grace period, the Margin Subcommittee believes that a period of at least 6 months would provide a reasonable, meaningful amount of time for market participants to work towards completing the tasks needed for compliance with the Margin Rules. The Margin Subcommittee contends that a shorter grace period, such as the 2-month grace period adopted by the SEC, would be insufficient for market participants subject to IM requirements in the remaining phases of the Margin Rules. Although the SEC did not specifically explain why it chose 2 *months* for its grace period, it apparently viewed such time to be sufficient in light of the unique features of its margin regime, which appear to present less of a burden for market participants in at least a couple of key ways:

- First, the SEC’s documentation requirements do not expressly call for specific margin documentation. Rather, the SEC’s margin rules include collateral agreement and netting agreement requirements that are arguably more high-level (e.g., agreement must be “legally enforceable”)⁵⁰ than the margin documentation that is required under the CFTC’s Margin Rules (along with collateral agreements that are also required under the Margin Rules).⁵¹
- Second, because the SEC’s margin rules are scheduled to become effective at some point in 2021 (i.e., approximately five years after the initial compliance phases for the margin rules of the CFTC/U.S. Prudential Regulators), the SEC may have expected SBSDs (particularly dual-hatted ones) to have acquired

⁵⁰ Under the SEC’s “collateral agreement” requirement (SEC Rule 18a-3(c)(4)), one of the conditions for a nonbank security-based swap dealer (**SBSD**) to be able to take into account the fair market value of collateral delivered by a counterparty is that such collateral “is subject to an agreement between the [SBSD] and the counterparty that is legally enforceable by the [SBSD] against the counterparty and any other parties to the agreement.” Similarly, under the SEC’s “netting agreement” requirement (SEC Rule 18a-3(c)(5)), a SBSBD “may include the effect of a netting agreement that allows the [SBSD] to net gross receivables from and gross payables to a counterparty upon the default of the counterparty, for the purposes of the calculations required pursuant to [the margin rules], if: (i) The netting agreement is legally enforceable in each relevant jurisdiction, including in insolvency proceedings; (ii) The gross receivables and gross payables that are subject to the netting agreement with a counterparty can be determined at any time; and (iii) For internal risk management purposes, the [SBSD] monitors and controls its exposure to the counterparty on a net basis.”

⁵¹ Under the CFTC’s margin documentation requirements, such documentation must (i) provide the CSE with the contractual right and obligation to exchange IM and VM in such amounts, in such form, and under such circumstances as are required by margin rules; (ii) specify the methods, procedures, rules, inputs, and data sources to be used for determining the value of uncleared swaps for purposes of calculating VM; (iii) describe the methods, procedures, rules, inputs, and data sources to be used to calculate IM for uncleared swaps entered into between the CSE and the counterparty; and (iv) specify the procedures by which any disputes concerning the valuation of uncleared swaps, or the valuation of assets collected or posted as IM or VM may be resolved. See CFTC Regulation §23.158, 17 C.F.R. § 23.158.

sufficient experience/systems/documentation to be in a position to more expeditiously comply with the SEC's margin rules. Indeed, the SEC alluded to nonbank SBSBs being able to leverage existing documentation (e.g., collateral agreements and margin documentation compliant with CFTC requirements) to meet the SEC's collateral and netting agreement requirements.⁵²

Overall, with market participants facing potentially lower compliance hurdles under the SEC's margin rules, a 2-month grace period may be appropriate in that context; however, a longer period (such as the 6-month grace period recommended in this report) would be needed for markets participants subject to the greater burdens in achieving compliance with the Margin Rules.

The Margin Subcommittee also believes that the 6-month grace period recommendation offers a measured, calibrated approach by including a time limitation to Phases 5 and 6 (with a potential exception in the SMA context, as discussed in Part II.B.2) and an explicit condition that IM exchange begin as soon as the parties have finished their preparations and are operationally ready within the 6-month period. The time limitation to Phases 5 and 6 recognizes that the bottleneck issues are likely to be most prevalent during those phases due to the various challenges outlined above. However, it is possible that the pipeline problem will not significantly subside after Phase 6 and thus we are asking the Commission to revisit the 6-month grace period recommendation for potential application to future post phase-in compliance dates based on the number of accounts likely to be in scope for such dates and the experience of market participants in Phases 5 and 6.

⁵² See Capital, Margin, and Segregation Requirements for Security-Based Swap Dealers and Major Security-Based Swap Participants and Capital and Segregation Requirements for Broker-Dealers, 84 Fed. Reg. at 43,909 (Aug. 22, 2019) (“[An existing netting or collateral agreement with a counterparty that was entered into by the nonbank SBSB in order to comply with the margin documentation requirements of the CFTC or the prudential regulators will suffice for the purposes of Rule 18a-3, as adopted, if the agreement meets the requirements of paragraph (c)(4) or (5) [requirements relating to collateral agreements and netting agreements], as applicable.”); *Id.* at 44,015 (SEC notes that a nonbank SBSB may not need to use the whole deferral period if “the nonbank SBSB and its counterparty have an existing agreement and processes that can be readily modified to incorporate the \$50 million threshold”); *Id.* at 43,920 (“[B]y aligning with the requirements of the CFTC and prudential regulators [with respect to sets of eligible collateral and haircuts], the [SEC’s] final rule should reduce the likelihood that SBSBs will seek to amend existing collateral agreements that may specifically reference haircuts in the margin rules of the CFTC or prudential regulators.”).

With respect to the condition relating to the extent to which the 6-month grace period can be used, the Margin Subcommittee has sought to clarify that the grace period should be used only to the point that it is necessary and, as such, parties would need to begin exchanging IM as soon as they are ready to do so. This would mean, for instance, that if parties are ready to exchange IM after the second month within the grace period, they should proceed to do so, rather than putting off the exchange of IM until the conclusion of the 6-month period. By crafting the 6-month grace period recommendation with this condition and the above-noted time limitation, the Margin Subcommittee has intended to strike a balance between, on the one hand, providing a fail-safe for those market participants facing various hurdles as they make their best efforts to comply with the Margin Rules and, on the other, ensuring that the exchange of IM pursuant to those rules is not unduly deferred.

B. ISSUES THAT COULD BE ADDRESSED IN LATER TERM (PHASE 6 COMPLIANCE)

1. *Separately Managed Accounts – Scoping Issue*

a) Challenge: Application of IM Threshold to SMA Client in the Aggregate Creates Uncertainty for SMA Client’s Independently Operating Asset Managers and Leads to Potential Cliff-Edge Events

With many Small Financial End Users (including SMA Clients) likely to cross the \$8B AANA threshold for Phase 6, they will then need to determine whether they exceed the \$50M IM Threshold vis-à-vis a CSE and therefore be required to exchange IM and be subject to the full suite of IM requirements. For SMA Clients in particular, the obligation to manage the \$50M IM Threshold with each CSE on a real-time, aggregate basis is unduly challenging in light of the lack of transparency and control across the SMA Client’s asset managers and may result in trading disruptions and the inability to hedge portfolios.⁵³ The requirement to share the \$50M IM Threshold

⁵³ In Letter No. 17-12, CFTC staff recognized that the separation among an SMA Client’s SMAs (and SMA asset managers) “is needed to allow asset managers to execute effectively on the investment strategy and to track the profits and losses for each strategy (in turn allowing the owner the ability to measure the effectiveness of each strategy and asset manager).” See CFTC Letter No. 17-12 (Feb. 13, 2017), at 4, available at <https://www.cftc.gov/sites/default/files/idc/groups/public/@lrllettergeneral/documents/letter/17-12.pdf>.

across an SMA Client's various SMAs that are independently managed by asset managers presents similar concerns to those that arose in 2017 in the context of an SMA Client's SMAs sharing an aggregate \$500,000 MTA. Such concerns include, but are not limited to:

- Negotiations and delays associated with CSEs allocating the \$50M IM Threshold; and
- Potential renegotiations, repapering, amendments and system updates based on reallocations due to changes in the number of SMAs/asset managers, trading mandates, volumes, market conditions, etc.

Unlike with MTAs, a CSE may decide not to allocate the IM Threshold to all or any SMAs of an SMA Client until the SMA Client's aggregate regulatory IM amount is at or near \$50M or the CSE's internal threshold.

Given the lack of transparency, control, or coordination in SMA arrangements and the current requirement to aggregate regulatory IM on a real-time daily basis across the SMAs of an SMA Client (and potentially, the lack of IM Threshold allocations), it is nearly impossible to ensure that the SMA Client in the aggregate will not exceed the \$50M IM Threshold at any time.⁵⁴ An SMA Client's sudden and unexpected breach of the IM Threshold would lead to cliff-edge events, such as the following:

- Some or all asset managers may no longer be able to trade for the SMAs they are independently managing on behalf of the SMA Client until the necessary documentation and operations are set up—thus, resulting in potential negative performance, realized losses, inability to hedge or execute prudent portfolio and risk management;
- Some or all of the asset managers may be asked or required to novate or terminate existing positions of their SMAs—again, to the detriment of the performance of the SMA Client's portfolio or the ability to effectively hedge the SMA Client's exposures;
- With the reduction of eligible counterparties, some or all asset managers may not be able to achieve best execution or comply with regulatory requirements or client guidelines regarding concentration limits (e.g., 5% securities related

⁵⁴ See Part II.A.1. for a more extensive discussion of the market realities that can lead to inadvertent breaches of the IM Threshold in the SMA context.

issuer limits for '40 act funds, 5% counterparty exposure limits for UCITS funds, etc.); and

- There may be a race to repaper across the asset managers for the same SMA Client with the same CSE and the same third-party custodians and/or tri-party collateral agents potentially at the same time, with smaller asset managers or those with smaller trading volumes likely to be deprioritized.

b) Recommendation: Permit Application of Separate IM Threshold to Each SMA of an SMA Client

As highlighted in prior comments submitted to the Commission, the cleanest and most efficient approach would be to extend to each SMA its own \$50M IM Threshold on the basis that each SMA functions as a distinct entity (e.g., limited recourse arrangements, separate margining and netting, etc.).⁵⁵ However, the Margin Subcommittee acknowledges that it may be difficult for this approach to gain support across jurisdictions, and therefore are recommending an alternate approach that would allow for the application of a flat IM Threshold of \$10M for each SMA akin to the flat MTA amount per SMA that was permitted in CFTC Letter No. 17-12. This flat \$10M IM Threshold would be an option, not a requirement, for CSEs to use instead of negotiating allocations of the \$50M IM Threshold across the SMAs/SMA asset managers of an SMA Client. In addition, the ability to rely on a flat \$10M IM Threshold per SMA could be subject to conditions such as those set forth in Letter No. 17-12, including:

- (1) Any such swaps are entered into with the CSE by an asset manager on behalf of an SMA owned by the legal entity pursuant to authority granted under an IMA; and
- (2) The swaps of such SMA are subject to a master netting agreement that does not permit netting of IM or VM obligations across SMAs of the legal entity that have swaps outstanding with the CSE.

Similar to the application of Letter No. 17-12 to MTA, this recommendation would not cap IM at \$50 million. As discussed below, safeguards mitigate the risk of providing this uncapped option.

⁵⁵ See, e.g., SIFMA AMG Letter to the CFTC and USPRs on Proposed Uncleared Margin Rules (Nov. 24, 2014), at 9-10, available at <https://www.sifma.org/wp-content/uploads/2017/05/sifma-amg-submits-comment-letter-to-multiple-regulators-regarding-margin-and-capital-requirements-for-covered-swap-entities.pdf>.

c) **Supporting Rationale for Recommendation**

Allowing a flat \$10M IM Threshold per SMA would help tackle the challenges faced by SMA Clients and their individual asset managers without limiting flexibility for a CSE to address credit, risk, or operational concerns. In particular, the flat IM Threshold approach would:

- Address the lack of transparency each asset manager has to the aggregate \$50M IM Threshold and provide them with certainty and control as to how much they can trade with a specific CSE;
- Address CSEs' credit, operational and legal burdens with having to (i) allocate and negotiate IM Thresholds with some or all of an SMA Client's SMAs, and/or (ii) potentially re-negotiate and amend the allocations if one SMA is at or near its allocation of the IM Threshold;
- Prevent the likely cliff edge events and mitigate potential trading disruptions;
- Permit asset managers to monitor and control how much trading their SMAs are doing with a CSE and address any potential overage by either novating, terminating or entering into offsetting trades prior to exceeding the \$10M IM Threshold per SMA;
- Mitigate the time, costs, burdens of pre-emptively setting up the tri-party collateral agent or third party custodial arrangements and the unnecessary clogging of the custodial and CSE pipeline;
- Allow asset managers who cannot or choose not to trade within the flat IM Threshold to seek to pre-emptively repaper; and
- Avoid the worst-case scenario where, according to feedback from some pension trusts and other financial end-users, the undue burdens and complexity flowing from the need to continuously monitor the sharing of the \$50M IM Threshold would cause SMA Clients to assign a \$0 IM Threshold across all their SMAs and CSEs.⁵⁶

Moreover, as indicated above, Letter No. 17-12 offers a precedent for allowing the application of a flat threshold amount at the SMA level in order to address the

⁵⁶ A similar concern arose in the context of MTAs. See Letter No. 17-12 at 5 ("If SMAs are left with no choice but to set MTA to zero at the account level, this consequence negatively impacts SMA owners, imposing burdens that SIFMA AMG argues are not necessary to achieve the objectives of the uncleared swap margin requirements.").

significant practical challenges that would otherwise arise if an aggregate threshold had to be shared by the SMAs of an SMA client. We acknowledge that the “flat threshold amount” in Letter No. 17-12 relates to MTA (i.e., 50K MTA per SMA), which is a distinct regulatory concept from the IM Threshold. However, we believe that the application of similar conditions in Letter No. 17-12 to the flat IM Threshold approach could help guard against potential misuse by market participants. Further, while the flat IM Threshold approach could potentially result in undocumented, unmarginated exposures beyond \$50M (at the SMA Client level), there are certain safeguards to prevent significant exposures/systemic risk:

- CSEs will have their own internal credit/risk parameters in determining how much uncollateralized exposures they are willing to take and are not required to agree to use the Flat IM Threshold for the SMAs of each SMA Client or asset manager; and
- SMA Clients that have significant uncollateralized exposures would run the risk of potentially having to register as MSPs and would be directly subject to the Margin Rules.

2. *Separately Managed Accounts – Implementation Issue*

a) **Challenge: Implementation Complexities Arise in the SMA Context Once the Applicable IM Threshold Is Exceeded**

If a flat IM Threshold approach is not adopted (or if a flat IM Threshold approach is adopted by the CFTC but a CSE refuses to use it with respect to the SMAs of an SMA Client), then the \$50M IM Threshold would be applied to the SMA Client in the aggregate and implementation issues would arise for SMA asset managers, particularly those that do not have regulatory IM compliant documentation/allocations at the time that the SMA Client may unexpectedly exceed the \$50M IM Threshold. We acknowledge that the recommendation in Part II.A.1 would be relevant in this scenario in regards to those SMA asset managers that do have documentation/IM allocations in place.

b) **Recommendation: Expanded Forbearance for SMAs**

The Margin Subcommittee recommends that the 6-month grace period (described in Part II.A.5) be made available in the SMA context even beyond Phase 6 (i.e., the 6-month grace period should not be subject to the time-limitation identified in Part II.A.5).

To be clear, if a flat IM Threshold approach for SMAs is adopted by the CFTC (and if a CSE agrees to use the flat IM Threshold approach for the SMAs of an SMA Client), SMA asset managers (along with the industry in general) would still be able to avail themselves of the grace period as described in Part II.A.5 (i.e., with the time limitation).

c) Supporting Rationale for Recommendation

Assuming that the \$50M IM Threshold applies to the SMA Client in the aggregate, SMA asset managers will face uncertainty regarding whether the SMA Client is at/near that IM Threshold and thus will be subject to potential cliff edge events (as described in Part II.B.1), in addition to the general industry concerns about pipeline problems and other obstacles that may delay documentation and account set-up (as discussed in Part II.A.5). This would necessitate allowing for the 6-month grace period to be made available in the SMA context even beyond Phase 6.

Notably, if a flat IM Threshold approach is adopted by the CFTC and if a CSE agrees to use the flat IM Threshold approach for the SMAs of an SMA Client (allowing each asset manager to have certainty over when the SMA it manages is at/near the relevant IM Threshold rather than being in the dark as to whether the SMA Client in the aggregate is at/near the IM Threshold), there would still be the pipeline challenges of getting documentation in place once the relevant IM Threshold (\$10M) is exceeded. Accordingly, the 6-month grace period should be made available (with the time limitation as set forth in Part II.A.5).

3. MSE Calculation Period and Methodology and Post Phase-In Compliance Periods

a) Challenge: The Margin Rules' MSE Calculation Period and Methodology Are Inconsistent with Global Standards and Create Undue Complexity, Monitoring Burdens and Confusion

Under the Margin Rules, a financial end user is required to calculate whether it, together with its affiliates, exceed the MSE of \$8 billion, and must therefore comply with the requirements to exchange regulatory IM. The MSE calculation is conducted based on the averaging of the *daily* aggregate notional amount of uncleared swaps, security-based swaps, and Deliverable FX with all counterparties during *June, July and August* of the calendar year preceding the corresponding compliance year. Following the final phase-in period for IM requirements beginning September 1, 2021, if the MSE calculation changes the status of a group of consolidated entities to either bring them into or take them out of scope of the IM

requirements, such change would apply as of the next calendar year (i.e., beginning January 1). (The USPR Margin Rules work in a similar way.)

These requirements diverge from the BCBS-IOSCO framework and the requirements of global regulators in the following ways:

- *MSE calculation*
 - The BCBS-IOSCO framework and all other non-U.S. jurisdictions require the AANA to be calculated during *March, April and May*.
 - The BCBS-IOSCO framework and all other non-U.S. jurisdictions, besides Brazil, base the calculation on the *month-end* average of derivatives notional exposure.

- *Post phase-in compliance dates*
 - US, EU, Switzerland: January 1 to December 31
 - BCBS-IOSCO framework and all other jurisdictions: September 1 to August 31

These differences in the U.S. regulations create complexity and confusion, and lead to additional effort, cost and compliance challenges for smaller market participants that are generally subject to margin requirements in multiple global jurisdictions.

For further information, see Appendix D for a comparison chart of global AANA calculation requirements and IM compliance dates.

b) Recommendation #1: Align the Margin Rules' Timing and Calculation Methodology for MSE and the Post Phase-In Compliance Periods with International Standards

The Margin Subcommittee recommends that the CFTC amend its uncleared margin requirements to align the following with global standards: (i) the timing and method for the MSE calculation; and (ii) the post phase-in compliance periods.

The recommended alignment could be accomplished via the following amendments to the definition of material swaps exposure in §23.151 and compliance dates in §23.161(c):

“Material swaps exposure for an entity means that, as of September 1 of any year, the entity and its margin affiliates have an average daily month-end aggregate notional amount of uncleared swaps, uncleared security-based swaps, foreign exchange forwards and foreign exchange swaps with all counterparties for June, July, and August ~~March, April and May~~ of that year of

~~the previous calendar year~~ that exceeds \$8 billion, ~~where such amount is calculated only for business days.~~”

§ 23.161 (c)(1) If a covered swap entity’s counterparty changes its status such that an uncleared swap with that counterparty becomes subject to a stricter margin requirement under §§ 23.150 through 23.161 (for example, if the counterparty’s status changes from a financial end user without material swaps exposure to a financial end user with material swaps exposure), then the covered swap entity shall comply with the stricter margin requirements for any uncleared swaps entered into with that counterparty after the counterparty changes its status. A counterparty’s material swaps exposure status is determined on September 1 each year.

§ 23.161 (c)(2) If a covered swap entity’s counterparty changes its status such that an uncleared swap with that counterparty becomes subject to less strict margin requirement under §§ 23.150 through 23.161 (for example, if the counterparty’s status changes from a financial end user with material swaps exposure to a financial end user without material swaps exposure), then the covered swap entity may comply with the less strict margin requirements for any uncleared swaps entered into with that counterparty after the counterparty changes its status as well as for any outstanding uncleared swap entered into after the applicable compliance date under paragraph (a) or (c)(1) of this section and before the counterparty changed its status. A counterparty’s material swaps exposure is determined on September 1 each year.

As currently required, the MSE calculation period for IM requirements for the compliance period beginning September 1, 2021 (commonly referred to as “Phase 6”) is June, July and August of 2020. As it may not be feasible to effect an amendment prior to this time, there would still be value in adopting the amendments that would create global consistency to the ongoing annual MSE calculations that will be conducted by smaller counterparties following Phase 6. In such case, the definition of material swaps exposure could be amended as follows:

“Material swaps exposure for an entity means that, as of September 1 of any year, the entity and its margin affiliates have an average month-end daily aggregate notional amount of uncleared swaps, uncleared security-based swaps, foreign exchange forwards and foreign exchange swaps with all counterparties for March, April and May of that year ~~June, July, and August of the preceding calendar year~~ that exceeds \$8 billion, provided that for

September 1, 2021, material swaps exposure for an entity means that the entity and its margin affiliates have an average daily aggregate notional amount of uncleared swaps, uncleared security-based swaps, foreign exchange forwards and foreign exchange swaps with all counterparties for June, July and August of the preceding calendar year that exceeds \$8 billion, where such amount is calculated only for business days.”

c) **Recommendation #2: As an Alternative to Globally Aligned Post Phase-in Compliance Dates, Confirm that the Initial Post Phase-in Compliance Date is January 1, 2023, Consistent with the EU and Switzerland**

Alignment of the compliance dates following the phase-in period would only be helpful to the industry if these changes were also made by the USPRs and, ideally, the EU and Switzerland. If global alignment cannot be achieved, then in the alternative, the Margin Subcommittee recommends that the CFTC provide guidance confirming that the initial compliance date following the phase-in period is January 1, 2023, rather than January 1, 2022, in accordance with the intentions of the EU and Switzerland. This step would prevent a U.S. only compliance date of January 1, 2022 only four months after the Phase 6 compliance date.

In connection with this, we recommend that section §23.161 explicitly specify the compliance year cycle which follows the phase-in periods, so these dates are more transparent to market participants. Without consideration of the relevant discussion in the preamble, it is not clear to many market participants that a change in status is currently meant to apply from January 1 of each year.

d) **Supporting Rationale for Recommendations**

Requirement 8.9 of the BCBS-IOSCO framework, revised as of April 2020, states that:

On a permanent basis (i.e., from 1 September 2022), any covered entity belonging to a group whose aggregate month-end average notional amount of non-centrally cleared derivatives for March, April, and May of the year exceeds €8 billion will be subject to the requirements described in this paper during the one-year period from

1 September of that year to 31 August of the following year when transacting with another covered entity (provided that it also meets that condition).⁵⁷

Thus, the Margin Rules contradict both the timing and methodology for the calculation of the average notional amount of derivatives for the purpose of determining the application of initial margin requirements, as well as the annual compliance periods following Phase 6.

Material Swaps Exposure

ISDA's 2018 Quantitative Analysis estimates that 850 counterparties may become subject to regulatory IM in Phase 6 with an AANA between \$8 billion and \$50 billion. Of those, 53% (or 631) will have an AANA of less than \$25 billion. These hundreds of counterparties, along with potentially hundreds of others that do not initially breach the \$8 billion threshold, will need to annually reassess their MSE calculations.

However, U.S. deviation on the approach to the MSE calculation means that these smaller market participants will need to run completely separate calculations from those which they have run for all other jurisdictions since neither the timing nor the method match.

Changing the timing of the MSE calculation alone would be helpful, but it would be most beneficial to change the calculation method from daily to month-end averaging as well. A daily calculation is substantially more work for smaller counterparties and is only used for the U.S. The MSE calculation period that was conducted in June, July and August of 2019 for Phase 5 in the U.S. required 64 observations to be calculated for averaging; whereas the global AANA calculation period for Phase 5 in March, April and May of 2020 will require three.

The Margin Rules state that use of daily averaging for the MSE calculation is believed to be preferable to an as-of date such as year-end, which might allow a market participant to adjust its exposures for such date to avoid the CFTC's margin requirements. Use of month-end dates over the course of the 3-month calculation period mitigates this risk by providing three periodic dates on which the aggregate notional is calculated prior to averaging. It would be neither practicable nor financially desirable for parties to tear-up their positions on a recurring basis prior to each month-end, interfering with their hedging strategies and causing them to

⁵⁷ See Basel Committee on Banking Supervision and Board of the International Organization of Securities Commissions, Margin Requirements for Non-Centrally Cleared Derivatives (Apr. 2020), available at <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD651.pdf>.

incur realized PnL changes. Global regulations following the BCBS-IOSCO framework have soundly employed the month-end averaging approach since 2016. The CFTC has issued equivalence determinations for the uncleared margin requirements of Australia, EU and Japan which employ the month-end averaging method.

Compliance Dates

If an annual MSE calculation results in a change in status, those parties will need to notify all their counterparties and both sides will need to implement the necessary adjustments in their systems which track and either apply or disapply IM requirements to existing or future netting sets effective as of the applicable compliance date.

As the U.S., EU and Switzerland have diverged from the annual compliance period in the BCBS-IOSCO framework, market participants will have to apply jurisdiction-specific effective dates to a subset of each netting set. For instance, if a party subject to both Japanese rules and U.S. rules determined via its annual AANA/MSE calculation that it had exceeded the JPY 1.1 trillion AANA and \$8 billion MSE thresholds, such change would apply as of September 1 in Japan and as of the following January 1 in the U.S. Thus, swaps entered into between September and December would be subject to IM requirements in Japan and not the U.S. If that same party's status should change the following year such that it now fell below the minimum thresholds in both regimes, such change would apply to its transactions as of September in Japan and the following January in the U.S.

In addition, the bifurcated timelines may interfere with a party's ability to use substituted compliance. Using the same example of a swap subject to U.S. and Japanese IM requirements, a party which is subject to Japanese IM requirements as of September could not meet those requirements using U.S. rules as it would not become subject to U.S. requirements until the following January 1.

These misaligned compliance periods will create significant effort and cost for smaller market participants and their counterparties to track the jurisdictional application of IM requirements to a set of swaps. The complexity will lead to errors in tagging and tracking of transactions, resulting in differences in IM calculations, increased reconciliation effort and disputed IM amounts.

The additional cost and complexity of differentiated compliance periods and the impact to substituted compliance will incentivize use of local trading relationships and inhibit cross-border transacting.

If globally aligned compliance dates cannot be achieved, then the alternative recommendation to confirm an initial post phase-in compliance date of January 1, 2023 (January 1, 2024 under revised BCBS-IOSCO timeline) would at least eliminate a compliance date only applicable in the U.S. and avoid the additional cost and effort for CSEs and a portion of their financial end user counterparties to adjust their netting sets after only four months. In addition, it prevents financial end users from having to run an additional MSE calculation and provide a separate notification in respect of a status change applicable as of January 1, 2022 (or January 1, 2023 under revised BCBS-IOSCO timeline) only in respect of U.S. regulations. This exceptional case in the U.S. is not transparent to market participants, and there is a risk of inconsistent application.

The delayed transition to the calendar year compliance period cycle means that the first post-Phase 6 reassessment of MSE would not apply until 16 months after the Phase 6 compliance date. While this means parties newly exceeding the \$8 billion MSE threshold following the phase-in period will have a longer period before they are required to begin calculating regulatory IM and potentially exchanging IM. It also means there is a longer period before Phase 6 firms (which have already exceeded the MSE threshold), might come out of scope of the IM requirements should their MSE fall below \$8 billion. As ISDA's 2018 Quantitative Analysis shows that 85% of Phase 6 firms would not exceed a \$50M IM Threshold two years into their regulatory IM requirements, there is a very limited amount of IM exchange that might be impacted during this period. Therefore, the complexity, effort and cost of a U.S. only regulatory IM compliance date cannot be substantiated.

4. *Minimum Transfer Amount (MTA)*

a) **Challenge: Operational and Documentation Issues with Using MTA**

In order to ease the transaction costs associated with the exchange of margin, the Margin Rules allow a CSE and its covered counterparty to agree to a MTA of up to \$500,000. The CSE is only required to collect or post collateral, as applicable, when the amount of both variation margin and initial margin exceeds the MTA. Although generally useful, the MTA requirements do not account for certain practicable operational processes and circumstances which limit the ability of CSEs and their covered counterparties to use the MTA. These impediments were recognized and addressed by DSIO staff through two staff letters, CFTC Letter No. 17-12 and CFTC Letter No. 19-25.

b) Recommendation: Codify Relief Provided in CFTC Letters No. 17-12 and 19-25 Which Address Practical Challenges of Applying MTA to Collateral Settlement

As the accommodations in CFTC Letter Nos. 17-12 and 19-25 are practical in nature and do not materially increase the amount of uncollateralized exposure at a given time, they should be permanently adopted.

CFTC Letter No. 17-12 (**17-12**)⁵⁸

- In response to a request from SIFMA AMG, DSIO issued 17-12 on February 13, 2017. It allows an SD to apply an MTA of up to \$50,000 (for VM and IM) when entering into swaps with an asset manager on behalf of an SMA owned by an SMA Client, regardless of the number of managers for the SMA Client.
- This relief helps to address the practical challenge for SDs to negotiate sub-allocations of the aggregate \$500,000 MTA per SMA Client across an SMA Client's multiple managers.
- Further, it prevents the parties from having to negotiate amendments to the sub-allocations in the collateral documents based on the changes in the number of asset managers or alternatively, to have to set the MTA at zero for all SMAs, resulting in frequent transfers of small amounts of collateral.

CFTC Letter No. 19-25 (**19-25**)⁵⁹

- In response to a request from ISDA, DSIO issued 19-25 on December 6, 2019 which allows an SD or MSP to maintain separate MTAs for VM and IM with each covered counterparty, provided the combined amount does not exceed the maximum allowable MTA of \$500,000.
- ISDA requested this relief because the Margin Rules are misaligned with market practice, requiring parties to combine their total IM and VM amount for comparison to the MTA and settle both in the event the combined amount exceeds a single MTA agreed between the parties.

⁵⁸ CFTC Letter No. 17-12 (Feb. 13, 2017), available at <https://www.cftc.gov/csl/17-12/download>.

⁵⁹ CFTC Letter No. 19-25 (Dec. 6, 2019), available at <https://www.cftc.gov/csl/19-25/download>.

- ISDA argued that such an approach was not feasible, since VM and IM follow separate settlement flows due to the regulatory requirement for IM segregation and therefore, there is not a juncture at which the combined margins can be compared to the MTA and a decision transmitted regarding whether the transfer is required for both VM and IM.
- DSIO granted the relief until December 31, 2021 based on an understanding of the operational impediments and the knowledge that any amounts of margin that might otherwise have been exchanged would not be material.

The rule amendments for the MTA requirements under the Margin Rules can primarily be proposed in accordance with the relief terms provided in each of 17-12 and 19-25. However, the interplay of the two necessitates an additional nuance to the recommended rule amendment by which the option to split the applicable maximum MTA between VM and IM should apply to either a covered counterparty or an asset manager on behalf of an SMA.

These amendments to the Margin Rules could be effected by adding definitions for “separately managed account” and “SMA owner” and amending §§ 23.151, 23.152(b)(3), 23.153(c) and 23.158(b) as follows:

§ 23.151 Definitions applicable to margin requirements.

Separately managed account means an account managed by an asset manager and governed by an investment management agreement that grants an asset manager authority to exercise investment discretion over a portion of an SMA owner’s assets for management in a separate account. The swaps of the separately managed account are subject to a separate master netting agreement established by an asset manager that does not permit netting of initial or variation margin obligations across separately managed accounts of the SMA owner established by other asset managers that have swaps outstanding with a covered swap entity.

SMA owner means a client on whose behalf one or more separately managed accounts are managed by an asset manager.

Minimum transfer amount means an amount agreed between a covered swap entity and a counterparty in respect of ~~combined~~ initial margin ~~and/or~~ variation margin under which no actual transfer of funds is required. The ~~combined~~ minimum transfer amounts agreed by a covered swap entity with a counterparty for ~~both initial and variation margin~~ shall not exceed \$500,000, ~~except in respect of a counterparty that is an SMA owner, for which the~~

combined minimum transfer amounts may exceed \$500,000, provided that for each separately managed account the combined minimum transfer amounts for both initial and variation margin do not exceed \$50,000.

§ 23.152 Collection and posting of initial margin.

(b)(3) *Minimum transfer amount.* A covered swap entity is not required to collect or to post initial margin pursuant to §§ 23.150 through 23.152, 23.154 and 23.156 through 23.161 with respect to a particular counterparty or a separately managed account unless and until the ~~combined~~ amount of initial margin ~~and variation margin~~ that is required pursuant to §§ 23.150 through 23.152, 23.154 and 23.156 through 23.161 to be collected or posted and that has not been collected or posted with respect to the counterparty is greater than the minimum transfer amount for initial margin \$500,000.

§ 23.153 Collection and posting of variation margin.

(c) *Minimum transfer amount.* A covered swap entity is not required to collect or to post variation margin pursuant to §§ 23.150, 23.151, 23.153, 23.155, 23.156, and 23.158 through 23.161 with respect to a particular counterparty unless and until the ~~combined~~ amount of ~~initial margin and~~ variation margin that is required pursuant to §§ 23.150, 23.151, 23.153, 23.155, 23.156, and 23.158 through 23.161 to be collected or posted and that has not been collected or posted with respect to the counterparty is greater than the minimum transfer amount for variation margin \$500,000.

§ 23.158 Margin documentation.

(b)(2) Describe the methods, procedures, rules, inputs, and data sources to be used to calculate initial margin for uncleared swaps entered into between the covered swap entity and the counterparty; ~~and~~

(3) The minimum transfer amounts applicable to initial margin and variation margin; and

(4) Specify the procedures by which any disputes concerning the valuation of uncleared swaps, or the valuation of assets collected or posted as initial margin or variation margin may be resolved.

c) **Supporting Rationale for Recommendation**

As no-action relief can be revoked by staff and/or may expire, codifying the changes provides certainty to market participants which informs the negotiation of the collateral support documentation and operational builds. Providing this certainty

would be helpful for IM Phases 5 and 6 and beyond; though the ongoing availability of the relief would provide a stop-gap measure in the event rule amendments are not promulgated prior to the Phase 5 compliance date. 17-12 is not time bound, while 19-25 expires on December 31, 2021, and would need to be codified or extended prior to that time.

The rule amendment in respect of 17-12 only applies to SMAs and their SD trading counterparties. The rule amendment for 19-25 has application to SDs and their covered counterparties indirectly subject to the rule.

In respect of 17-12, the rule modification for SMAs would be a beneficial global accommodation, including by the USPRs and SEC, but is being requested from the CFTC regardless since the existing relief letter provides a practical accommodation.

The rule amendment in line with 19-25 would allow for SDs and their counterparties to manage MTA in an operationally practicable way that aligns with the global market standard.

5. ***Removal of Deliverable FX from MSE Calculation***

a) **Challenge: Small Financial End Users Are Unnecessarily Scoped in for Phase 6 and Beyond Due to Inclusion of Deliverable FX in AANA Calculation**

As discussed in Part I, even though Small Financial End Users generally do not present the systemic risk that the IM requirements seek to address, at least 30 percent are scoped into the remaining IM phases, due in large part to the inclusion of Deliverable FX in their AANA calculations. Consequently, those Small Financial End Users would be subject to IM requirements if they exceed the \$50M IM Threshold (even intermittently). Small Financial End Users are thus unnecessarily burdened by having to: (1) monitor IM levels throughout the compliance period to determine if the \$50M IM Threshold is exceeded; (2) implement compliance measures *even in advance of exceeding the IM threshold* to address the potential risk of non-compliance; and (3) risk losing market access until IM-compliant agreements are in place if the IM Threshold is exceeded (even if temporarily or immaterially). These burdens come with a hefty price tag per legal entity and per CSE in annual vendor costs to monitor the SIMM on a daily basis to confirm if does not exceed the IM Threshold per CSE (and its consolidated affiliates), as well as approximately \$15,000-\$20,000 per Small Financial End-User to maintain segregated accounts (and such cost would be on a per manager basis if the Small Financial End User trades through asset managers).

Again, these impacts are exacerbated for Small Financial End Users that hedge FX risk with Deliverable FX and therefore, technically exceed the relevant AANA threshold as a result of the inclusion of Deliverable FX. Given the relatively low percentage of in-scope swaps that these Small Financial End Users may be trading as well as the limited CSE and custodian bandwidth to meet all repapering demands, these entities may be deprioritized and unable to implement their hedging strategies. In addition, the Small Financial End Users with the lowest exposures (including seeded funds which, absent the consolidation requirements under the Margin Rules, would not exceed the AANA threshold) have an increased risk of losing market access during the phase-in periods as CSEs and custodians will likely give higher priority to entities with relatively larger exposures.

b) Recommendation: Remove Deliverable FX from AANA Calculation

The Margin Subcommittee recommends assessment of market impact of including deliverable FX in the MSE calculation and amendment of the Margin Rules to exclude deliverable FX from the MSE calculation. The rule amendment would adjust the definition of “Material Swaps Exposure” to add “non-deliverable” prior to “foreign exchange forwards” and “foreign exchange swaps” as follows:

Material swaps exposure for an entity means that the entity and its margin affiliates have an average daily aggregate notional amount of uncleared swaps, uncleared security-based swaps, non-deliverable foreign exchange forwards, and non-deliverable foreign exchange swaps with all counterparties for June, July and August of the previous calendar year that exceeds \$8 billion,

c) Supporting Rationale for Recommendations

The Margin Subcommittee is proposing the above recommendation to mitigate burdens on Small Financial End Users that could be scoped into the remaining phases. Small Financial End Users do not present material, systemic risks that justify the burdens of monitoring initial margin, preemptive documentation and potentially losing market access due to immaterially or temporarily exceeding the initial margin threshold prior to complying with Margin Rules. These Small Financial End Users will also likely face challenges during the compliance period due to the need for CSEs and custodians to prioritize resources towards entities with higher regulatory IM amounts. Given that, as highlighted in Part I, one-third of the Small Financial End-Users captured by Phase 5 and 6 will have been unnecessarily brought in due to the inclusion of Deliverable FX in AANA calculations—even though Deliverable FX is not subject to IM requirements under the Margin Rules—we believe that Deliverable FX should be carved out from AANA calculations.

III. APPENDICES

- A. APPENDIX A – CFTC MARGIN STUDY
- B. APPENDIX B – ILLUSTRATION OF CUSTODIAL DOCUMENTATION ARCHITECTURE
- C. APPENDIX C – INTERPRETIVE GUIDANCE SCENARIOS
- D. APPENDIX D – COMPARISON CHART OF GLOBAL AANA CALCULATION REQUIREMENTS AND IM COMPLIANCE DATES

APPENDIX A

CFTC MARGIN STUDY

Initial Margin Phase 5

by

Richard Haynes, Madison Lau, and Bruce Tuckman¹

October 24, 2018

EXECUTIVE SUMMARY

The uncleared margin rules (UMR) mandate that registered swap dealers exchange initial margin (IM) on their trades with others swap dealers and financial end users. The covered entities first brought into scope were those, which—at the group level—had the largest average aggregate notional amount (AANA) of swaps. Compliance for those with smaller AANAs was required on later dates. The last such date, “Phase 5,” takes effect on September 1, 2020. As of then, all covered entities will be in scope so long as their AANAs exceed a material swaps exposure (MSE) of \$8 billion.

Market participants have argued that Phase 5 will bring into scope a large number of relatively small financial end users; that the costs of implementing these new IM arrangements will strain industry resources; that many newly in-scope entities will never actually have to post IM because their positions are in products exempt from IM or because their required IM falls below the existing \$50mm threshold; and, finally, that Phase 5 entities, because of their relatively small swaps positions, pose little systemic risk.

Following up on these concerns, industry representatives have begun to ask international regulators for various forms of relief, e.g., extending the phase-in schedule; permanently raising the MSE threshold; excluding physically-settled foreign exchange (FX) swaps—which are exempt from IM—from the calculation of AANA; and simplifying the compliance process.

The purpose of this paper is to guide regulators in their responses to these requests for relief by providing empirical estimates as to the coverage of Phase 5. Using regulatory data at the CFTC, this study complements the recent, related work of market participants and other regulators. Its main conclusions are as follows:

- While Phases 1 through 4 capture just over 40 entities, Phase 5 could bring 700 entities in scope, which together encompass only 11% of the AANA across all phases.
- Nearly 60% of entities coming into scope in Phase 5 have AANAs of less than \$25 billion, and over 75% have AANAs less than \$50 billion. These subsets of entities comprise about 15% and 30% of total Phase 5 AANA, respectively.
- Phase 5 entities will span a variety of business sectors. The average AANA of newly in-scope swap dealers, however, will be many times that of any other sector.
- Excluding physically-settled FX swaps from AANA could reduce the number of Phase 5 entities by nearly 30%.
- Phase 5 compliance could require implementing nearly 7,000 IM relationships. Excluding physically-settled FX swaps from AANA could reduce that number to under 5,000.

¹ Office of the Chief Economist, Commodity Futures Trading Commission. While this paper was produced in the authors' official capacity, the views expressed here are those of the authors and do not necessarily reflect the views of other Commission staff, the Office of the Chief Economist, or the Commission. The authors would like to thank Rafael Martinez and Jeffrey Hasterok for helpful comments and suggestions.

INTRODUCTION

Global uncleared margin rules (UMR) require that swap dealers exchange initial margin (IM) with financial entities and with other swap dealers against uncleared swap positions. Commercial end users and various government entities are exempt. All other entities covered by the UMR are subject to a gradual phase in of the requirements. The relevant schedule in the United States is shown in Figure 1.

The compliance phases are based on average aggregate notional amount (AANA) of swaps, which equals the daily average of notional amount of swaps over June, July, and August of the previous year. With the exception of swaps with commercial end users, all swaps must be counted toward the AANA, including swaps that are exempt from IM. AANA is calculated on a corporate group level, and swaps between affiliates are included, but counted only once.

Returning to the figure, Phases 1, 2, and 3, brought into scope entities with more than \$3 trillion, \$2.25 trillion, and \$1.5 trillion AANA, respectively. Phase 4 is scheduled to lower the threshold to \$750 billion AANA as of September 1, 2019, and Phase 5, as of September 1, 2020, to bring all remaining entities into scope.

As the figure shows, however, an entity remains out-of-scope if its AANA is below a material swaps exposure (MSE) of \$8 billion. One purpose of this MSE was to exempt entities that would probably never have to post IM because the margin requirement on their relatively small swaps positions would likely never exceed the \$50 million IM threshold. In any case, the combination of the UMR phase in and the MSE means that Phase 5 will capture entities with AANAs between \$8 and \$750 billion.²

As a result of global coordination, the UMR and its compliance schedule are similar in the United States and in other jurisdictions. For example, the only difference between the U.S. and European phase in is that the numerical thresholds in the latter are in Euros rather than U.S. dollars, that is, Phase 5 in Europe applies to entities with between €8 and €750 billion AANA.³

Several observers have noted that Phase 5 will bring a large number of relatively small entities into the scope of the UMR.⁴ Some have also surmised that the costs of implementing these new IM arrangements will strain industry resources; that many newly in-scope entities will never actually have to post IM because their positions are in products exempt from IM or because their required IM falls below \$50mm; and, finally, that Phase 5 entities, because of their relatively small swaps positions, pose little systemic risk.

Following up on these arguments, industry representatives have begun to ask international regulators for various forms of relief, e.g., extending the phase-in schedule; permanently raising the MSE

² The UMR in the United States is given by Commodity Futures Trading Commission (2016). Some details of AANA computation are on pages 703-4. The phase-in schedule is on pp. 675-676, and the MSE is on page 644. Note that, for the purposes of MSE, AANA is calculated as an average over March, April, and May.

³ BCBS-IOSCO (2015), pp. 24-25.

⁴ See Cloud Margin (2018), Condat, Puce, and Nommels (2018), ISDA (2018), and ISDA and SIFMA (2018). Please note that ISDA (2018) has been made available only to regulators.

threshold; excluding physically-settled foreign exchange (FX) swaps—which are exempt from IM—from the calculation of AANA; and simplifying the compliance process.⁵

The purpose of this paper is to guide regulators in their responses to these requests for relief by providing some empirical estimates of the coverage of Phase 5. Using regulatory data at the CFTC, this study complements the recent, related work of market participants and other regulators.

DATA AND METHODOLOGY

This study includes data on all U.S. reporting entities' interest rate swaps (IRS), index and single-name credit default swaps (CDS), FX swaps, and equity swaps. Data for all of these products except single-name CDS are available to the CFTC through reporting by Swap Data Repositories (SDRs). Data on single-name CDS are available to the CFTC through DTCC's Trade Information Warehouse.⁶ Data on IM currently exchanged on these positions was not available.

Due to current data limitations, commodity swaps are not included in this study. While regrettable, this omission should not be too consequential: commodity swaps constitute less than 0.35% of global swaps notional amounts.⁷

For compliance purposes, AANA is computed as a daily average over a three-month period. For simplicity, however, this study computes AANA from a single day's snapshot of positions on convenient dates around September, 2018.⁸ All notional amounts are converted to U.S. dollars at then prevailing exchange rates.

According to the UMR in the United States, swaps with commercial end users are not counted in the computation of AANA. The only available and relevant data, however, are that some swaps are tagged by commercial end users as hedges of commercial risk and, consequently, as exempt from clearing. This study, therefore, approximates the exclusion of swaps with commercial end users by excluding from AANA all swaps by entities that have tagged any of their swaps as hedges of commercial risk.

To make in-scope determinations, AANA is aggregated across all affiliated entities.⁹ This study accounts for the required aggregations by combining the legal entity identifiers (LEIs) that accompany each swap in the regulatory data with affiliate structure data from S&P's Cross Reference Services. Furthermore, as required by the UMR, inter-affiliate swaps are included only once in the calculation of AANA.

Some results in this paper rely on the categorization of entities by business sector. These sector classifications are a product of CFTC staff.

⁵ See, for example, ISDA *et al* (2018).

⁶ Single-name CDS are CDS on individual corporate or sovereign credits, as opposed to index CDS, which are CDS on baskets of credits or indexes. Index CDS are under the jurisdiction of the CFTC, which has established "Part 45" rules that govern reporting to SDRs. Single-name CDS are under the jurisdiction of the SEC, which has not yet implemented a corresponding reporting regime.

⁷ See BIS (2018).

⁸ The dates of these snapshots were August 31, 2018, for IRS, index CDS, and FX swaps; September 1, 2018, for single-name CDS; and September 21, 2018, for equity swaps.

⁹ See, for example, Commodity Futures Trading Commission (2016), pp. 703-704.

FINDINGS

While Phases 1 through 4 capture just over 40 entities, Phase 5 could bring 700 entities in scope, which together encompass only 11% of the AANA across all phases.

Table 1 shows the qualitative differences between Phases 1, 2, and 3, which have already taken effect, and Phases 4 and 5, which are to come. Phases 1, 2, and 3 combined captured 23 entities in this data set and encompassed \$292 trillion AANA, for an average of about \$13 trillion per entity. While Phase 4 would capture about the same number of entities, it would add only \$20 trillion AANA, for an average of \$1 trillion per entity. In sharp contrast, Phase 5 would capture over 700 additional entities, but, at an average of \$54 billion per entity, constitute only 11% of the total AANA across all phases.

Table 1: Number of Entities and AANA Covered by IM Phases

Phase(s)	Number of Entities	Total AANA (\$billions)	Average AANA per Entity (\$billions)
1, 2, and 3	23	292,338	12,710
4	20	20,049	1,002
5	704	38,275	54

The exact number of Phase 5 entities calculated here is less important than its order of magnitude. Because this study uses AANAs at particular dates in 2018, the actual number of entities that will be captured by Phase 5 in September, 2020, will certainly be different. There are, for example, 31 entities in the sample with AANAs between \$7.5 and \$8 billion that could grow into scope by September 1, 2020, and 34 entities between \$8 and \$8.5 billion that could fall out of scope by that time.

Although not shown in the table, there are tens of thousands of entities that have AANAs below the \$8 billion MSE and, therefore, will continue to remain out-of-scope after Phase 5.

Nearly 60% of entities coming into scope in Phase 5 have AANAs of less than \$25 billion, and over 75% have AANAs less than \$50 billion. These subsets of entities comprise about 15% and 30% of total Phase 5 AANA, respectively.

Figure 2 shows the distribution of Phase 5 entities across several AANA buckets. The choice of buckets is arbitrary, but the \$50 billion and \$100 billion thresholds have some significance, as market participants have called for raising the MSE threshold from \$8 billion to either \$50 billion or \$100 billion.¹⁰

The blue bars in Figure 2 give the number of entities (left axis) in each of the AANA buckets. The vast majority of the 704 Phase 5 entities are in the smallest two AANA buckets, with 403 entities, or 57%, in the \$8 to \$25 billion bucket and 139 entities, or another 20%, in the \$25 to \$50 billion bucket. There are 70 entities (10%) in the \$50 to \$100 billion range, and the remaining 92 entities (13%) fall in the over \$100 billion range.

The red line in Figure 2 (right axis) gives the cumulative AANA across buckets, starting from the rightmost bucket. For example, the cumulative amount of AANA covered by Phase 5 entities with AANAs in the five rightmost buckets, i.e., from \$50 to \$750 billion, is about \$28 trillion.

¹⁰ See, for example, Bartholomew (2018) and ISDA *et al.* (2018), p. 4.

Along this line, the following statistics may be computed. Entities in the \$8 to \$25 billion bucket encompass \$5.6 trillion AANA, or about 15% of the \$38.3 trillion Phase 5 total, while entities in the two leftmost buckets, with AANAs between \$8 and \$50 billion, encompass \$10.6 trillion AANA or 28% of the Phase 5 total.

Recalling from Table 1 that the entirety of Phase 5 AANA is 11% of the AANA of all phases combined, entities with AANAs below \$50 billion constitute 28% of 11%, or about 3% of AANA across all phases of the UMR.

Phase 5 entities will span a variety of business sectors. The average AANA of newly in-scope swap dealers, however, will be many times that of any other sector.

Table 2 analyzes the Phase 5 entities by sector. The first row gives the number of Phase 5 entities in each sector; the second row gives the total Phase 5 AANA in each sector; and the third row gives the average AANA of entities in that sector. It should be noted that the government sector used here matches the rules of the UMR, by, for example, including U.S. municipalities but excluding central banks.¹¹

By count, banks, hedge funds, and asset managers predominate. By total AANA, banks, hedge funds, and, to a lesser extent, asset managers, are the largest. By average AANA, however, swap dealers are many times as large as entities in other sectors.

Table 2. Phase 5 Entities and their AANAs by Sector

	Swap Dealers	Banks	Hedge Funds	Asset Managers	Insurance Companies	Pension Funds	Corporates	Gov't Sector	Unclassified
Number of Entities	20	158	163	153	48	54	65	14	29
Total ANA (\$billions)	4,045	9,180	10,412	6,598	3,985	1,445	1,226	840	544
Average ANA (\$billions)	202	58	64	43	83	27	19	60	19

Table 2 also reveals that 704 Phase 5 entities may be somewhat of an overestimate. As discussed in the section on data and methodology, this study excludes commercial end users that have claimed commercial hedging exemptions from clearing. It is possible, however, that some of the 65 corporates in Table 2, which did not claim such exemptions, may claim to be commercial end users that are exempt from the UMR. In that case, the true number of Phase 5 entities will fall from 704 by the number of these commercial end users.

¹¹ More specifically, central banks and entities guaranteed by a federal government are excluded from the UMR and from the entity count in Table 2, with the exception of FNMA and FHLMC, which are included. (The swaps of these excluded entities, however, are included in the calculation of AANA for covered entities.) Other government-related entities, like U.S. municipalities, Federal Home Loan Banks, and sovereign wealth funds are included in the UMR and in the entity count in Table 2.

Excluding physically-settled FX swaps from AANA could reduce the number of Phase 5 entities by nearly 30%.

Figure 3 shows how AANA breaks down by product across the IM phases. Entities in all phases have about the same percentage of IRS swaps, but, overall, Phase 4 and 5 entities have a much larger percentage of FX products and a much smaller percentage of equity products than entities in Phases 1, 2, and 3.

The data used for this study do not allow for the precise identification of physically- vs. cash-settled FX swaps. Consistent with market practice, however, a rough rule has been applied here: all FX options, NDFs (non-deliverable forwards), and exotic derivatives are considered cash settled, while all FX forwards and swaps are considered physically settled.¹² Using this approximation, Figure 3 reveals that Phase 4 and 5 entities have a significant fraction of their AANA in physically-settled FX swaps.

The extent of AANA in physically-settled FX swaps has a particular policy implication. Under current rules, all FX swaps have to be included in AANA even though physically-settled FX swaps are exempt from IM requirements. Therefore, an entity with more than \$8 billion of physically-settled FX swaps but little of any other product would be captured by one IM phase or another, and would have to prepare for the exchange of IM, but would never actually need to collect or post IM. For this reason, market participants have asked regulators to exclude physically-settled FX swaps from AANA.

Table 3 describes the impact of excluding physically-settled FX swaps from AANA. Of the 704 Phase 5 entities predicted to be in scope, 501 (71%) would remain in scope, while 203 (29%) would fall out of scope, i.e., would have their AANAs fall below \$8 billion.

Table 3 also shows that average AANA—computed with all swaps—is significantly higher for entities remaining in scope than for those falling out of scope. In other words, on average, excluding physically-settled swaps exempts the smallest swap counterparties from the IM regulatory regime. There are a small number of cases, however, in which entities with relatively large AANAs fall out of scope because their AANAs are concentrated in physically-settled FX swaps.

Table 3. Effects of Excluding Physically-Settled FX Swaps from AANA. (FX Forwards and FX Swaps are the products assumed to be Physically Settled.)

AANA Includes all Swaps	
Phase 5 in-scope entities (AANA between \$8 and \$750 billion)	704
Average AANA	\$54 billion
AANA Excludes Physically-Settled FX Swaps	
Phase 5 entities remaining in scope	501
Average AANA (all swaps)	\$69 billion
Phase 5 entities falling out of scope	203
Average AANA (all swaps)	\$19 billion

¹² Cross-currency swaps, which are explicitly included in IM requirements, are considered cash-settled FX swaps for the purposes of this study.

Phase 5 compliance could require implementing nearly 7,000 IM relationships. Excluding physically-settled FX swaps from AANA could reduce that number to under 5,000.

As mentioned in the introduction, market participants claim that the implementation of new IM agreements between Phase 5 entities and swap dealers from any phase will severely strain the resources of the financial industry. To quantify this concern, this paper estimates the number of IM relationships required by Phase 5 entities.

Strictly speaking, an IM agreement is required between every pair of LEIs. In practice, however, LEIs representing affiliates of larger groups tend to realize economies of scale in establishing these agreements. An individual portfolio manager, for example, might have its own IM arrangements in place with a particular swap dealer, but has probably shared legal and operational resources with other portfolio managers in the same asset management group. For this reason, this study defines a “relationship” as an entity and a swap dealer, where the entity is an aggregation of related affiliates. The aggregation logic is the same as used for computing AANA.

Table 4 shows the number of relationships of Phase 5 entities that include at least 1 swap dealer. Under the aggregation assumption of the previous paragraph, the number of these relationships correspond to the number of IM agreements that must be in place for Phase 5 entities to continue their swaps business with their existing counterparties.

Table 4. Number of Phase 5 Relationships that Include at Least 1 Swap Dealer from any Phase. LEIs are aggregated at the group level.

	Including Corporates	Excluding Corporates
All FX trades in AANA	6,957	6,333
Excluding physically-settled FX swaps from AANA	4,918	4,509

The first column of Table 4 assumes that all of the corporates discussed in Table 2 fall under the UMR. In that case, Phase 5 could require nearly 7,000 IM agreements, or about 10 relationships for each of the 704 Phase 5 entities. If physically-settled FX swaps were excluded from AANA, the number of in-scope entities would fall and the number of required agreements would fall to below 5,000.

The second column of Table 4 assumes that all of the corporates in Table 2 declare themselves to be commercial end users that are exempt from the UMR. In that case, the number of agreements falls to 6,333, or, if physically-settled FX swaps are excluded, to 4,509.

CONCLUSION

This study has described the characteristics of the entities that are likely to be included in Phase 5 of the IM regime. On the whole, the findings show that Phase 5 will capture a large number of entities with relatively low AANAs and with a relatively high proportion of physically-settled FX swaps. Broadly speaking, these results are consistent with recent comments and studies by market participants and other regulators.

Figure 1. Scheduled Phase In of Uncleared Margin Rules. Entities come into scope when their Average Aggregate Notional Amount (AANA) exceeds the given thresholds. An entity is never in scope if its AANA is less than a Material Swaps Exposure of \$8 billion.

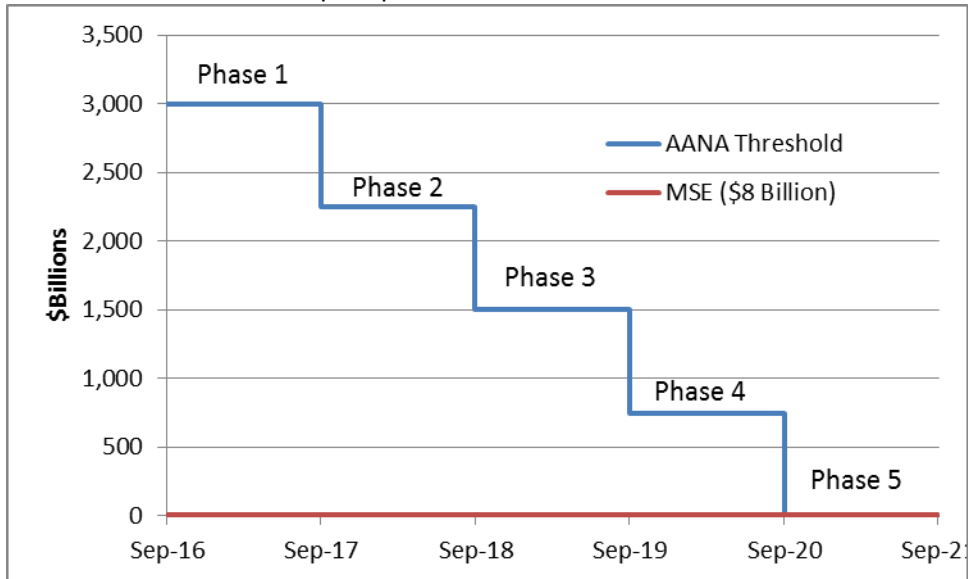


Figure 2. Phase 5 Entities by AANA Bucket. The blue bars (left axis) show the number of entities in each bucket. The solid red line (right axis) shows the cumulative AANA across buckets, starting from the rightmost bucket.

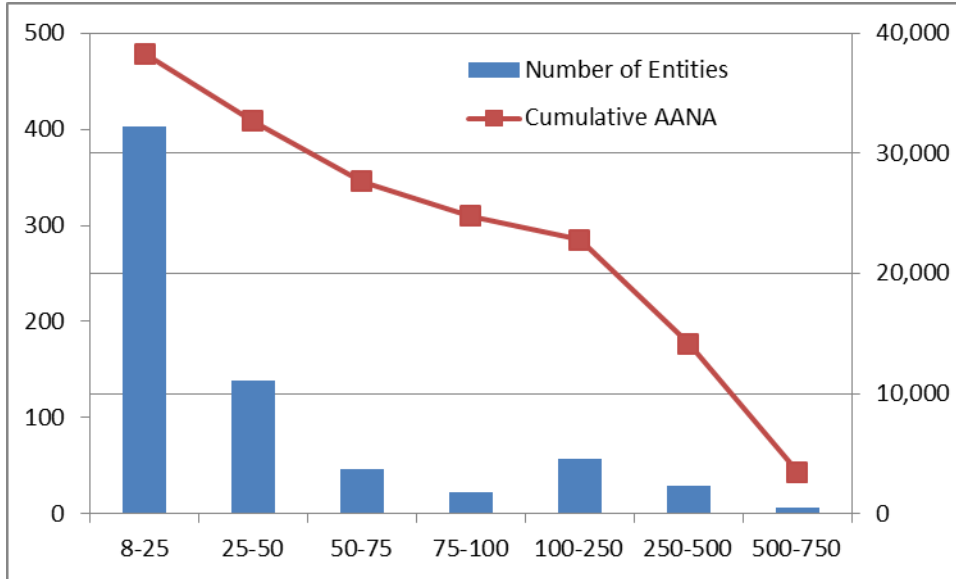
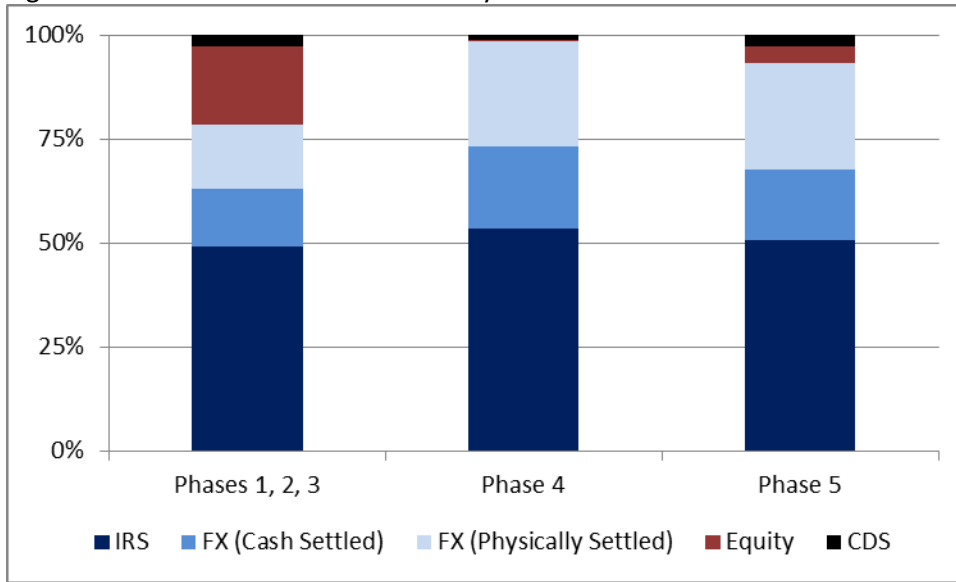


Figure 3. Product Breakdown of AANA by IM Phase



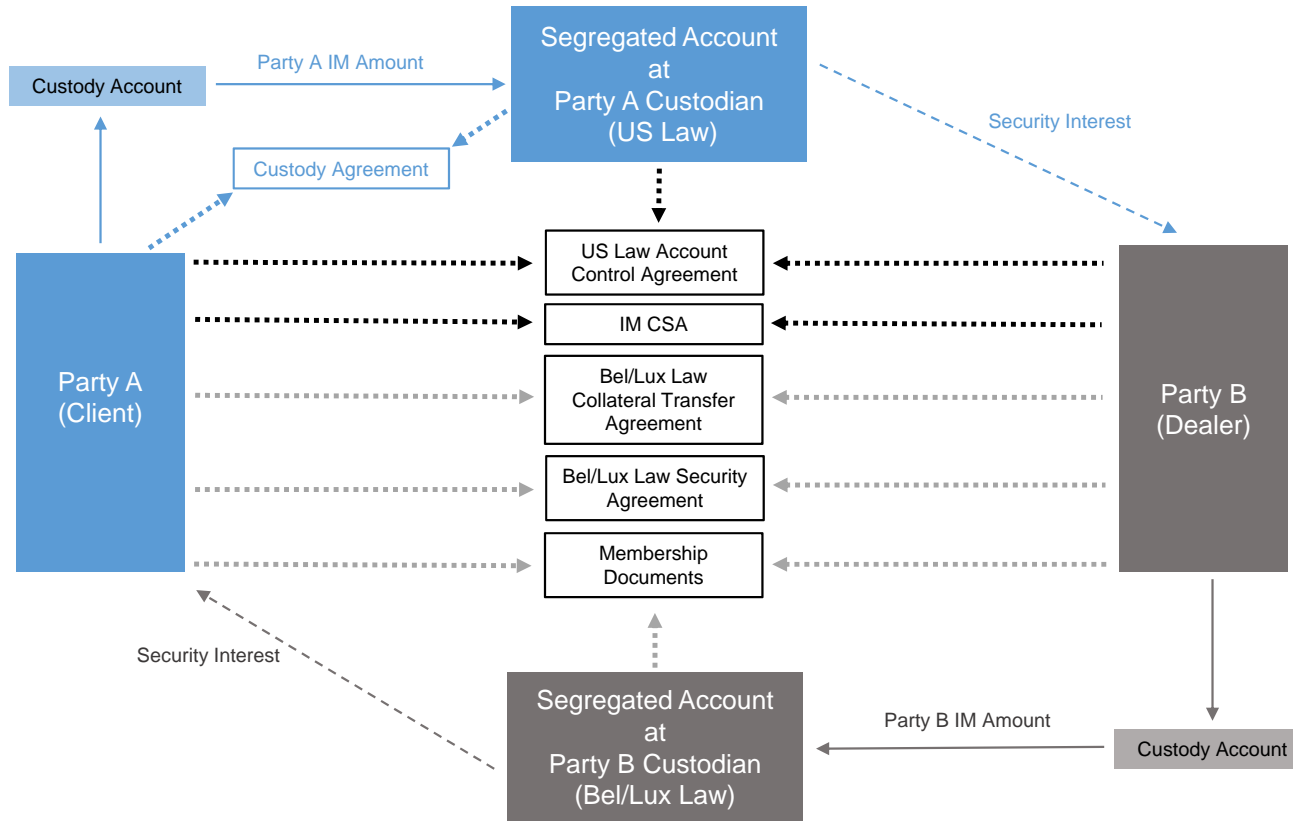
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APPENDIX B

ILLUSTRATION OF CUSTODIAL DOCUMENTATION ARCHITECTURE

Custodial Documentation Architecture: Illustration



APPENDIX C

INTERPRETIVE GUIDANCE SCENARIOS

Interpretive Guidance Scenarios

Scenario 1

Asset Manager	Reg IM Sub-Threshold	Reg IM Compliant ISDA/CSA	Reg IM Exposure	Reg IM Posted	Uncollected Reg IM
1	15	Yes	12	0	12
2	10	Yes	20	10	10
3	10	No	8	0	8
4	None	No	6	0	6
5	None	No	9	0	9
6	Zero	Yes	3	3	0
Total			58	13	45

Analysis: No regulatory IM compliance issues. Total uncollected regulatory IM for the SMA Client is less than \$50M. All Asset Managers may continue trading with Dealer.

Scenario 2

Asset Manager	Reg IM Sub-Threshold	Reg IM Compliant ISDA/CSA	Reg IM Exposure	Reg IM Posted	Uncollected Reg IM
1	15	Yes	12	0	12
2	10	Yes	20	10	10
3	10	No	8	0	8
4	None	No	10	0	10
5	None	No	12	0	12
6	Zero	Yes	3	3	0
Total			65	13	52

Analysis: Managers 4 and 5 execute new trades generating additional regulatory IM exposure, which results in a regulatory IM compliance issue, as total uncollected regulatory IM for the SMA Client is now \$52M. Under the proposed Interpretive Guidance, Managers 1, 2 and 6 could continue trading as each has regulatory IM compliant documentation in place. Manager 3 is also allowed to continue trading as it has an agreed regulatory IM sub-Threshold and is below that regulatory IM sub-Threshold. Dealer will need to work with Managers 4 and/or 5 to reduce aggregate uncollected regulatory IM to \$50M or below and Managers 4 and 5 cannot execute new trades (absent other relief).

Scenario 3

Asset Manager	Reg IM Sub-Threshold	Reg IM Compliant ISDA/CSA	Reg IM Exposure	Reg IM Posted	Uncollected Reg IM
1	15	Yes	12	0	12
2	10	Yes	20	10	10
3	10	No	15	0	15
4	None	No	6	0	6
5	None	No	9	0	9
6	Zero	Yes	3	3	0
Total			65	13	52

Analysis: Manager 3 executes new trades generating additional regulatory IM exposure, which exceeds its regulatory IM sub-Threshold and results in a regulatory IM compliance issue, as total uncollected regulatory IM for the SMA Client is now \$52M. Under the proposed Interpretive Guidance, Managers 1, 2 and 6 could continue trading as each has regulatory IM compliant documentation in place. Dealer will need to work with Manager 3 to reduce uncollected regulatory IM to Manager 3's regulatory IM sub-Threshold of \$10M or below, or to execute regulatory IM compliant documentation and collect \$5M in regulatory IM. Managers 4 and 5 do not have regulatory IM compliant documentation, nor a regulatory IM sub-Threshold, so they cannot execute new trades until the aggregate uncollected regulatory IM for the SMA Client is at or under \$50M (absent other relief). However, if Dealers were to agree a regulatory IM sub-Threshold of \$6M and \$9M, respectively, for example with Managers 4 and 5, they would be able to continue to trade up to their regulatory IM sub-Threshold.

Scenario 4

Asset Manager	Reg IM Sub-Threshold	Reg IM Compliant ISDA/CSA	Reg IM Exposure	Reg IM Posted	Uncollected Reg IM
1	15	Yes	22	0	22
2	10	Yes	20	10	10
3	10	No	8	0	8
4	None	No	6	0	6
5	None	No	9	0	9
6	Zero	Yes	3	3	0
Total			68	13	55

Analysis: Manager 1 has executed new trades and failed to post the required \$7M in regulatory IM. Manager 1 is in breach of its posting obligations to Dealer. Dealer will need to collect the required regulatory IM or close out Manager 1. Dealer can continue trading with Asset Managers 2 and 6 as each has regulatory IM compliant documentation in place. Manager 3 is also allowed to continue trading as it has an agreed regulatory IM sub-Threshold and is

below its regulatory IM sub-Threshold. Managers 4 and 5 do not have regulatory IM compliant documentation, nor a regulatory IM sub-Threshold, so they cannot execute new trades until the aggregate uncollected regulatory IM for the SMA Client is at or under \$50M (absent other relief). However, if Dealers were to agree a regulatory IM sub-Threshold of \$6M and \$9M, respectively, for example with Managers 4 and 5, they would be able to continue to trade up to their regulatory IM sub-Threshold.

APPENDIX D

COMPARISON CHART OF GLOBAL AANA CALCULATION REQUIREMENTS AND IM COMPLIANCE DATES

AANA Calculation Periods and Compliance Dates for Non-Cleared Margin Requirements

ISDA is providing the following information based on current understanding and is subject to change.

The information in yellow is subject to regulatory confirmation or rule amendments/finalization. The text in red denotes globally inconsistent dates or methods.

For ease of comparison, the below information does not reflect rule changes recently finalized or proposed to delay Phases 5 and 6 a year in accordance with the April 3rd Statement from BCBS and IOSCO.

		US		EU/UK		Japan		Canada		Switzerland		Australia		Hong Kong		Singapore		Korea		Brazil		South Africa	
AANA Calculation Method		Daily averaging		Month-end average		Month-end average		Month-end average		Month-end average		Month-end average		Month-end average		Month-end average		Month-end average		Daily averaging		Month-end average	
	Compliance Date	AANA/MSE	AANA Calc Period	AANA	AANA Calc Period	AANA	AANA Calc Period	AANA	AANA Calc Period	AANA	AANA Calc Period	AANA	AANA Calc Period	AANA	AANA Calc Period	AANA	AANA Calc Period	AANA	AANA Calc Period	AANA	AANA Calc Period	AANA	AANA Calc Period
Phase 5	1-Sep-20	USD 50 billion	March, April, May 2020	EUR 50 billion	March, April, May 2020	JPY 7 trillion	March, April, May 2020	CAD 75 billion	March, April, May 2020	CHF 50 billion	March, April, May 2020	AUD 75 billion	March, April, May 2020	HKD 375 billion	March, April, May 2020	SGD 80 billion	March, April, May 2020	KRW 70 trillion	March, April, May 2020	BRL 25 billion	March, April, May 2020	ZAR 30 trillion	March, April, May 2020
Phase 6	1-Sep-21	USD 8 billion	June, July, Aug 2020	EUR 8 billion	March, April, May 2021	JPY 1.1 trillion	March, April, May 2021	CAD 12 billion	March, April, May 2021	CHF 8 billion	March, April, May 2021	AUD 12 billion	March, April, May 2021	HKD 60 billion	March, April, May 2021	SGD 13 billion	March, April, May 2021	KRW 10 trillion	March, April, May 2021	BRL 25 billion	March, April, May 2021	ZAR 23 trillion	March, April, May 2021
Post phase-in period	1-Jan-22	USD 8 billion	June, July, Aug 2021	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Post phase-in period	1-Sep-22	n/a	n/a	n/a	n/a	JPY 1.1 trillion	March, April, May 2022	CAD 12 billion	March, April, May 2022	n/a	n/a	AUD 12 billion	March, April, May 2022	HKD 60 billion	March, April, May 2022	SGD 13 billion	March, April, May 2022	KRW 10 trillion	March, April, May 2022	BRL 25 billion	March, April, May 2022	ZAR 15 trillion	March, April, May 2022
Post phase-in period	1-Jan-23	USD 8 billion	June, July, Aug 2022	EUR 8 billion	March, April, May 2022	n/a	n/a	n/a	n/a	CHF 8 billion	March, April, May 2022	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Post phase-in period	1-Sep-23	n/a	n/a	n/a	n/a	JPY 1.1 trillion	March, April, May 2023	CAD 12 billion	March, April, May 2023	n/a	n/a	AUD 12 billion	March, April, May 2023	HKD 60 billion	March, April, May 2023	SGD 13 billion	March, April, May 2023	KRW 10 trillion	March, April, May 2023	BRL 25 billion	March, April, May 2023	ZAR 8 trillion	March, April, May 2023
Post phase-in period	1-Jan-24	USD 8 billion	June, July, Aug 2023	EUR 8 billion	March, April, May 2023	n/a	n/a	n/a	n/a	CHF 8 billion	March, April, May 2023	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Post phase-in period	1-Sep-24	n/a	n/a	n/a	n/a	JPY 1.1 trillion	March, April, May 2024	CAD 12 billion	March, April, May 2024	n/a	n/a	AUD 12 billion	March, April, May 2024	HKD 60 billion	March, April, May 2024	SGD 13 billion	March, April, May 2024	KRW 10 trillion	March, April, May 2024	BRL 25 billion	March, April, May 2024	ZAR 100 billion	March, April, May 2024

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