

April 13, 2020

# CFTC Margin Requirements for Uncleared Swaps

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## CFTC Revises Final Deadline for Compliance With Rule on Margin Requirements for Uncleared Swaps

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### SUMMARY

On April 9, 2020, the Commodity Futures Trading Commission published revisions to its 2016 rules establishing the schedule for compliance with initial margin requirements applicable to swaps that are not cleared through regulated clearing houses.<sup>1</sup> Under the revised rule, swap dealers, major swap participants, and other covered counterparties with between \$8 billion and \$50 billion in average daily aggregate notional amounts of uncleared swaps will not be required to comply with the CFTC's previously issued initial margin requirements for uncleared swaps until September 1, 2021, instead of the previous deadline of September 1, 2020. The Basel Committee on Banking Supervision and the International Organization of Securities Commissions have extended the final recommended compliance deadline to September 1, 2022 in response to COVID-19. However, neither the CFTC nor the Prudential Regulators have indicated whether they will do the same.

### BACKGROUND

In November 2011, the Group of Twenty (the "G20"), which is comprised of the countries with the 20 largest economies, issued a communique calling on the Basel Committee on Banking Supervision ("BCBS") and the International Organization of Securities Commissions ("IOSCO"), in conjunction with other organizations, to develop margin requirements for swaps not cleared through a regulated clearing house ("Uncleared Swaps").<sup>2</sup> In January 2016, the Commodity Futures Trading Commission (the "CFTC") mandated that certain swap dealers ("SDs") and major swap participants ("MSPs", and together with SDs, "covered swap entities" or "CSEs")<sup>3</sup> collect and post initial and variation margin for Uncleared Swaps (the

“CFTC Margin Rule”).<sup>4</sup> The CFTC Margin Rule, which aligned with the standards set by the IOSCO and BCBS, established five phases of implementation.<sup>5</sup>

Under the CFTC Margin Rule, the first phase applied to CSEs and covered counterparties with the largest average daily aggregate notional amounts (“AANA”) of Uncleared Swaps and other financial products.<sup>6</sup> Each successive phase brought CSEs and covered counterparties with progressively lower AANA within the CFTC Margin Rule’s scope.<sup>7</sup>

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### RULE REVISION

On September 1, 2019, phase 4 brought CSEs and covered counterparties with over \$750 billion in AANA within the CFTC Margin Rule’s scope.<sup>8</sup> Phase 5, which would have applied to all CSEs and covered counterparties with over \$8 billion in AANA, was to begin on September 1, 2020.<sup>9</sup> When the rule was adopted, market participants raised concerns that the phase 5 deadline provided insufficient time for smaller CSEs and covered counterparties to comply fully with the CFTC Margin Rule.<sup>10</sup> A study conducted by the CFTC’s Office of the Chief Economist (the “OCE”) found that phase 5 would apply to a large number of companies, each with miniscule AANA compared to entities covered by phases 1 through 4. “The OCE has estimated that the average AANA per entity in phase 5, under the current schedule, would be \$54 billion compared to an average [of] \$12.71 trillion AANA for each entity in phases 1, 2, and 3 and \$1 trillion in phase 4.”<sup>11</sup> As a whole, “Phase 5 could bring 700 entities in scope, which together encompass only 11% of the AANA across all phases.”<sup>12</sup>

In July 2019, in response to compliance concerns, and considering the modest market share impacted by phase 5, BCBS and IOSCO modified their recommended compliance schedule. BCBS and IOSCO retained the original implementation deadline for the largest CSEs and covered counterparties subject to phase 5, but introduced a phase 6 deadline of September 1, 2021 for the smallest CSEs and covered counterparties that were originally subject to phase 5.<sup>13</sup> On April 9, 2020, the CFTC revised the timeline in the CFTC Margin Rule to reflect the changes made by BCBS and IOSCO (the “Revised CFTC Margin Rule”).<sup>14</sup> Under the Revised CFTC Margin Rule, CSEs and covered counterparties with AANA between \$50 billion and \$750 billion still must comply by the original phase 5 deadline of September 1, 2020,<sup>15</sup> but the Revised CFTC Margin Rule adds a phase 6, whereby all remaining CSEs and covered counterparties with AANA above \$8 billion are covered as of September 1, 2021.<sup>16</sup> The Revised CFTC Margin Rule becomes effective as of May 11, 2020.<sup>17</sup>

On April 3, 2020, in response to business challenges resulting from the spread of the coronavirus (“COVID-19”), BCBS and IOSCO delayed phases 5 and 6 by one year, with phase 5 starting on September 1, 2021 and phase 6 commencing on September 1, 2022.<sup>18</sup> The CFTC<sup>19</sup> has not issued any further statement about whether it will amend the Revised CFTC Margin Rule to reflect BCBS and IOSCO’s further revision.

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ENDNOTES

- 1 The CFTC Margin Rule requires initial margin to be posted and collected only by “covered swap entities” (swaps dealers and major swap participants”) and other entities with “material swaps exposure,” which is defined as an average daily aggregate notional amount of uncleared swaps, uncleared security-based swaps, foreign exchange forwards and foreign exchange swaps with all counterparties above \$8 billion. Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 81 FR 636 (January 6, 2016), available at <https://www.govinfo.gov/content/pkg/FR-2016-01-06/pdf/2015-32320.pdf>.
- 2 See G20, *Cannes Summit Final Declaration – Building Our Common Future: Renewed Collective Action for the Benefit of All*, Nov. 4, 2011, available at <http://www.g20.utoronto.ca/2011/2011-cannes-declaration-111104-en.html>.
- 3 The CFTC Margin Rule applies to entities that are not subject to the margin rules established by the Prudential Regulators. See 7 U.S.C. 6s(e)(1)(A). See also 7 U.S.C. 1a(39) (defining the term “Prudential Regulator” to mean the Board of Governors of the Federal Reserve System; the Office of the Comptroller of the Currency; the Federal Deposit Insurance Corporation; the Farm Credit Administration; and the Federal Housing Finance Agency). Those swap dealers that are banks are subject to the margin rules of the Prudential Regulators and not the CFTC’s rules, although the rules of the CFTC and those of the Prudential Regulators have generally been consistent with each other, both on substantive requirements and compliance schedules. The Prudential Regulators also revised their margin requirement deadlines to align with the changes made by BCBC, IOSCO and CFTC, modifying phase 5 and adding a phase 6. See Margin and Capital Requirements for Covered Swap Entities, 84 FR 216 (November 7, 2019), available at <https://www.fdic.gov/news/board/2019/2019-09-17-notice-dis-b-fr.pdf>.
- 4 Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 81 FR 635 (January 6, 2016), available at <https://www.federalregister.gov/documents/2016/01/06/2015-32320/margin-requirements-for-uncleared-swaps-for-swap-dealers-and-major-swap-participants>.
- 5 Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 85 FR 19878 (April 9, 2020), available at <https://www.cftc.gov/sites/default/files/2020/04/2020-06625a.pdf>.
- 6 85 FR 19879.
- 7 *Id.*
- 8 *Id.*
- 9 *Id.*
- 10 See, e.g., Letter from the Securities Industry and Financial Markets Association, the American Bankers Association, the Global Foreign Exchange division of the Global Financial Markets Association, and the Institute of International Bankers (April 5, 2019); Letter from the Managed Funds Association (June 20, 2019).
- 11 See Richard Haynes, Madison Lau, & Bruce Tuckman, Initial Margin Phase 5 (Oct. 24, 2018), available at [https://www.cftc.gov/sites/default/files/About/Economic%20Analysis/Initial%20Margin%20Phase%205%20v5\\_ada.pdf](https://www.cftc.gov/sites/default/files/About/Economic%20Analysis/Initial%20Margin%20Phase%205%20v5_ada.pdf).
- 12 *Id.* at 1.
- 13 Basel Committee on Banking Supervision, *Margin Requirements for Non-Centrally Cleared Derivatives* (July 2019), available at <https://www.bis.org/bcbs/publ/d475.pdf>.
- 14 85 FR 19878.
- 15 85 FR 19880.

ENDNOTES (CONTINUED)

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- <sup>16</sup> *Id.*
- <sup>17</sup> 85 FR 19878.
- <sup>18</sup> Basel Committee on Bank Supervision, *Basel Committee and IOSCO Announce Deferral of Final Implementation Phases of The Margin Requirements for Non-Centrally Cleared Derivatives* (April 3, 2020), available at <https://www.bis.org/press/p200403a.htm>.
- <sup>19</sup> Prudential Regulators have not indicated whether they will extend the deadlines for compliance in accordance with BCBS or IOSCO.

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