



Swap Margin Rule Update: LIBOR, Brexit, and Other Current Matters

FCA Board Meeting

March 12, 2020

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Outline

- ❑ **Clarifying Scope and Terminology**
- ❑ **Current Proposed Rule - LIBOR and Legacy Swap Amendments, Inter-affiliate Initial Margin**
- ❑ **March 2019 Interim Final Rule – “Brexit” and Legacy Swap Amendments**



Clarifying Scope & Terminology

Rule Scope: Establishes margin requirements for the non-cleared swap and security-based swap activities of Covered Swap Entities.

Covered Swap Entity (CSE)

- **Swap Dealer / Security-Based Swap Dealer:** Generally, an entity that makes a market in swaps.
- **Major Swap Participant:** Generally, an entity that maintains a “substantial position” in any major swap category (i.e., interest rate swaps).

Excepted or Exempted Swaps: As outlined in FCA Regulation § 624.1(d).

- **Small Institution** - FCS Institutions with Total Assets < \$10 billion.
- **Cooperative** - FCS Institutions with Total Assets > \$10 billion (swaps entered into for the benefit of FCS institution members).
- **NOTE:** Farmer Mac *is not* exempted or excepted under either of these provisions.



Clarifying Scope & Terminology

Variation Margin: Covers day-to-day changes in market value.

Initial Margin: Covers costs to replace swap upon counterparty default.

Legacy Swap: Any non-cleared swap entered into before the relevant compliance date outlined in the swap margin rule.





Current Proposed Rule - Overview



- **Amendments to Preserve Legacy Status:**
 - Swaps Amended to Accommodate a Change in Referenced Benchmark Interest Rates (“LIBOR” Amendments).
 - Swaps Amended as Part of Standard “Lifecycle” Events.
- **Amendment to Extend the Initial Margin Compliance Phase-In.**
- **Amendment to Clarify Initial Margin Contract Requirements.**
- **Amendment to Exempt Inter-Affiliate Swaps from Margin Requirements.**



Current Proposed Rule – “IBOR” Amendments



- **Policy Objective:** Accommodate transition of legacy swaps away from Inter-Bank Offered Rates (IBORs) like LIBOR due to their potential discontinuation.
- **Amendment Detail:** Allow amendments, via various contractual means, to replace certain referenced rates in legacy swaps without triggering margin requirements.
- **Public Response:** Respondents generally support the Agencies’ proposal.



Current Proposed Rule – “Lifecycle” Amendments



- **Policy Objective:** Accommodate amendments to legacy swaps that reduce operational or counterparty risk.
- **Amendment Detail:** Permit amendments to legacy swaps arising from routine industry practices over the life-cycle of a non-cleared swap without triggering margin requirements:
 - Compression Exercises.
 - Notional Reductions.
 - Technical Amendments.
- **Public Response:** Limited, and generally supportive.



Current Proposed Rule – Initial Margin Contract Requirements



- **Policy Objective:** To address market concerns regarding when initial margin trading documentation must be in place for CSEs and their counterparties.
- **Amendment Detail:** Amend regulation text to expressly state when initial margin trading documentation must be executed; specifically at the time when initial margin must be collected or posted under the Swap Margin Rule.
- **Public Response:** Commenters supported the Agencies' proposal.



Current Proposed Rule – Initial Margin Phase-In Extension



- **Policy Objective:** Address industry concerns regarding the operational and other difficulties associated with beginning to exchange initial margin with a large number of relatively small counterparties.
- **Amendment Detail:** Extend the Initial Margin phase-in schedule to give CSEs an additional year to implement initial margin requirements with smaller counterparties.
- **Public Response:** Commenters supported the Agencies' proposal.



Current Proposed Rule – Inter-Affiliate Initial Margin Requirements



- **Policy Objective:** Encourage prudent risk management; harmonize U.S. requirements with other international jurisdictions.
- **Amendment Detail:** Exempt non-cleared swaps between CSEs and their affiliates from Initial Margin requirements [variation margin still required]; expand the definition of “affiliate.”
- **Public Response:** Mixed
 - In Favor: IAIM requirements are unnecessary, discourage sound risk management, put U.S. firms at a competitive disadvantage, and increase costs to end-users.
 - Opposed: Eliminating IAIM increases risk to U.S. depository institutions [and thus U.S. Taxpayers] and increases overall systemic risk.



“Brexit” Interim Final Rule



- **Policy Objective:** Address industry concerns regarding the legacy status of swaps transferred from swap counterparties in the U.K. to affiliates in the E.U. or U.S. in preparation for a non-negotiated U.K. exit from the E.U. (a “Hard Brexit”).
- **Amendment Detail:** Permit amendments to legacy swaps to effect a transfer from a U.K. entity to an affiliate located in the E.U. or the U.S. without triggering margin requirements.
- **Public Response:** None.



Questions?



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