



**U.S. COMMODITY FUTURES TRADING COMMISSION**

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Division of Swap Dealer and  
Intermediary Oversight

Joshua B. Sterling  
Director

December 6, 2019

Ms. Tara Kruse  
Global Head, Infrastructure, Data and Non-Cleared Margin  
International Swaps and Derivatives Association, Inc.  
10 East 53<sup>rd</sup> Street  
New York, NY 10022

**Re: Commission Regulations 23.151, 23.152, and 23.153 – Staff Time-Limited No-Action Position Regarding Application of Minimum Transfer Amount under the Uncleared Margin Rules**

Dear Ms. Kruse,

This is in response to your letter dated October 24, 2019, to the Division of Swap Dealer and Intermediary Oversight (the “Division”) of the Commodity Futures Trading Commission (the “Commission” or the “CFTC”). You submitted your letter on behalf of the International Swaps and Derivatives Association, Inc. (“ISDA”) and its member swap dealers (“SDs”). By your letter, you request that the Division confirm that it will not recommend an enforcement action to the Commission if an SD or major swap participant (“MSP”) applies separate minimum transfer amounts (“MTAs”) for its initial margin (“IM”) and variation margin (“VM”) obligations on uncleared swap transactions with each swap counterparty, provided that the combined IM MTA and VM MTA per swap counterparty does not exceed \$500,000. We understand that ISDA is requesting this relief because the use of separate MTAs, as described in your letter to us, has been questioned during recent examinations of SDs by the National Futures Association.

### **Regulatory Background**

Commission regulations 23.152 and 23.153<sup>1</sup> require an SD or an MSP that is subject to the Commission’s margin rules<sup>2</sup> to collect or post, each business day, VM for uncleared swap

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<sup>1</sup> Commission regulations are found at 17 CFR Part 1 *et. seq.* (2017), and may be accessed through the Commission’s web site, [www.cftc.gov](http://www.cftc.gov). The Commission published final margin rules for uncleared swaps in 2016.

transactions with each counterparty that is an SD, MSP, or financial end user, and IM for uncleared swap transactions for each counterparty that is an SD, MSP, or a financial end user that has material swaps exposure.<sup>3</sup> IM posted or collected by an SD or MSP must be held by one or more custodians that are not affiliated with the SD, MSP, or the counterparty.<sup>4</sup> VM posted or collected by an SD or MSP is not required to be maintained with a custodian.<sup>5</sup>

Commission regulations 23.152(b)(3) and 23.153(c) provide, however, that an SD or MSP is not required to collect or post IM or VM with a counterparty until the combined amount of such IM and VM, as computed under Commission regulations 23.154 and 23.155 respectively, exceeds the MTA of \$500,000.<sup>6</sup> Once the combined IM and VM amounts required to be posted or collected exceed the MTA of \$500,000, the SD or MSP must collect or post the full amount of both the IM and VM required to be exchanged with the counterparty.<sup>7</sup>

In adopting the final margin rules, the Commission was cognizant of the need to balance the protections provided by the daily exchange of IM and VM with the operational burdens and costs of transferring small dollar amounts between counterparties. In this connection, the Commission stated that the MTA of \$500,000 was appropriately sized to generally alleviate the operational burdens associated with making de minimis margin transfers.<sup>8</sup> The Commission

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*See* Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 81 FR 636 (Jan. 6, 2016) (“CFTC Margin Rules”).

<sup>2</sup> The Commission’s margin requirements for uncleared swap transactions apply only to SDs and MSPs for which there is not a prudential regulator. *See* 7 U.S.C. 6s(e)(1)(B). SDs and MSPs for which there is a prudential regulator must meet the minimum requirements for uncleared swaps established by the applicable prudential regulator. <sup>7</sup> U.S.C. 6s(e)(1)(A). *See also* 7 U.S.C. 1a(39) (defining the term “prudential regulator” to include the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Farm Credit Administration, and the Federal Housing Finance Agency). The prudential regulators published final margin requirements for uncleared swap transactions in 2015. *See* Margin and Capital Requirements for Covered Swap Entities, 80 FR 74840 (Nov. 30, 2015). Accordingly, the relief provided in this letter extends only to SDs and MSPs subject to the CFTC Margin Rules. In addition, certain entities are excluded from the Commission’s margin rules including commercial end users. *See* 17 CFR 23.150.

<sup>3</sup> The term “material swaps exposure” is defined in Commission regulation 23.151 to mean 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 previous calendar year that exceeds \$8 billion, calculated only for business days.

<sup>4</sup> *See* 17 CFR 23.157(a).

<sup>5</sup> Commission regulation 23.157 does not require VM to be maintained in a custodial account.

<sup>6</sup> *See, e.g.*, 17 CFR 23.153(c). Such regulation states:

(c) *Minimum transfer amount.* A covered swap entity is not required to collect or to post variation margin pursuant to §§ 23.150 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 through 23.161 to be collected or posted and that has not been collected or posted with respect to the counterparty is greater than \$500,000.

<sup>7</sup> For example, if on a given business day an SD is required to post \$400,000 and \$150,000 of IM and VM, respectively, to a counterparty, the SD must post the full \$550,000 with the counterparty.

<sup>8</sup> *See* CFTC Margin Rules, 81 FR at 652.

further noted that the MTA should “mitigate some of the administrative burdens and counter-cyclical effects associated with the daily exchange of variation margin, without resulting in an unacceptable level of uncollateralized credit risk.”<sup>9</sup>

### **Request for Regulatory Relief**

In your letter, you state that an MTA for VM and IM for each party to a swap transaction has routinely and historically been included in Credit Support Annexes (“CSAs”) executed between the counterparties for the sole and practical purpose of avoiding frequent exchanges of small amounts of collateral between the parties. You further state that the Commission recognized this practice by permitting SDs and MSPs, and their respective counterparties, to include a combined IM and VM MTA in their respective CSAs of up to \$500,000.<sup>10</sup> However, in order to better reflect the operational requirements and the legal structure of the Commission’s regulations, you request that SDs and MSPs be able to maintain separate MTAs for IM and VM, provided that on a combined basis, the IM MTA and the VM MTA do not exceed \$500,000.

In support of your request for regulatory relief, you state that the Commission requires the exchanged IM to be segregated with an unaffiliated third party, while VM is not required to be segregated. You further state that the Commission’s IM requirements have necessitated a new and distinct workflow for IM settlement through custodians and tri-party agents that is completely separate from the VM settlement payment process.

You further represent that in order to comply with the IM segregation requirements as set forth in Commission regulations, and as a practical implementation matter, SDs have agreed to separate MTAs in each of their IM and VM CSAs, which when combined do not exceed \$500,000. You also state that each MTA is applied to the applicable settlement flow with: (1) an exchange of the full amount of VM in the event the VM MTA is exceeded; and (2) an exchange of the full amount of IM, minus the agreed upon threshold (up to \$50,000,000),<sup>11</sup> in the event the IM MTA is exceeded.<sup>12</sup>

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<sup>9</sup> See *id.* at 680.

<sup>10</sup> See definition of “minimum transfer amount” in Commission regulation 23.151 (defining the MTA as the combined IM and VM amount under which no actual transfer of funds is required).

<sup>11</sup> The Commission regulations limit the amount of the applicable threshold. Commission regulation 23.151 defines the initial margin threshold amount as “an aggregate credit exposure of \$50 million resulting from all uncleared swaps between a covered swap entity and its margin affiliates on the one hand and a covered counterparty and its margin affiliates on the other. For purposes of this calculation, an entity shall not count a swap that is exempt pursuant to § 23.150(b).” 17 CFR 23.151.

<sup>12</sup> The following provides an example of your request. An SD and a counterparty agree to a \$300,000 IM MTA and a \$200,000 VM MTA. If the margin calculations set forth in Commission regulations 23.154 (for IM) and 23.155 (for VM) require the SD to post \$400,000 of IM with the counterparty and \$150,000 of VM with the counterparty, the SD will be required to post \$400,000 of IM with the counterparty (assuming that the \$50 million minimum IM threshold amount for this counterparty has been exceeded). The SD, however, will not be obligated to post any VM with the counterparty as the \$150,000 requirement is less than the \$200,000 MTA.

Finally, you state that this separate IM and VM MTA approach has been agreed to globally by market participants and is employed consistently across foreign jurisdictions. You note that this uniform approach eliminates the need to create and implement IM and VM settlement flows tailored to each relevant margin jurisdiction, as well as the need to amend CSAs, which already provide for the allocation of separate MTAs for IM and VM.

### **No-Action Position**

The Division recognizes that separate IM and VM MTAs may result in the exchange of a lower amount of total margin between an SD or MSP and its counterparty than the amount that would be exchanged if the IM and VM MTA were computed on an aggregate basis. However, staff believes that such differences in total margin exchanged would not be material and would not result in an unacceptable level of credit risk as the total amount of combined IM and VM that is not exchanged at any point in time will never be more than the \$500,000 MTA. Accordingly, the Division has considered the request and believes that the approach is consistent with the Commission's objective of requiring swap counterparties to protect themselves from credit and market risks, while eliminating the costs and burdens associated with the transfer of small balances

Based on the foregoing, the Division is issuing this time-limited relief and will not recommend that the Commission initiate an enforcement action against an SD or MSP that fails to combine IM and VM amounts in accordance with Commission regulations 23.152(b)(3) and 23.153(c). The time-limited no-action relief will expire at the earlier of December 31, 2021 or the effective date of a final rule addressing the application of the MTA. The time-limited no-action relief is subject to the following conditions:

- (i) in determining the amounts of IM and VM required to be posted or collected under Commission regulations 23.152(b)(3) and 23.153(c), the SD or MSP applies separate MTAs for IM and VM with each counterparty;
- (ii) the separate amounts of MTA allocated for IM and VM are specified in the margin documentation required pursuant to Commission regulation 23.158 between the SD or MSP and the counterparty;
- (iii) when combined, the separate MTAs allocated for IM and VM do not exceed \$500,000; and
- (iv) the full amount of IM or VM required to be posted or collected as specified in the applicable margin documentation is posted or collected if the corresponding IM or VM MTA is exceeded.<sup>13</sup>

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<sup>13</sup> The following provides an example of the final condition. An SD and a counterparty agree to \$300,000 IM MTA, and \$200,000 VM MTA. If the margin calculations set forth in Commission regulations 23.154 (for IM), and 23.155 (for VM) require the SD to post \$200,000 of IM with the counterparty and \$250,000 of VM with the counterparty, the SD would not be required to post IM with the counterparty as the \$200,000 requirement is less than the \$300,000 MTA. However, the SD would be required to post \$250,000 in VM as the VM required exceeds the \$200,000 VM MTA, even though the total amount of margin owed is below the \$500,000 MTA set forth in Commission regulations 23.152(b)(3) and 23.153(c).

This letter, and the positions taken herein, are based upon the representations made to us and are subject to compliance with the conditions stated above. Any different, changed or omitted material facts or circumstances might require the Division to reach a different conclusion and render this letter void. You must notify the Division immediately in the event there is any change to the facts presented to the Division. This letter does not provide no-action relief from any provision of Commission regulations 23.151, 23.152(b)(3) and 23.153(c), except as specifically noted above, or from **any** other applicable requirements in the Commodity Exchange Act or in the Commission regulations issued thereunder. Further, this letter represents the position of the Division only and does not necessarily represent the views of the Commission or of any other division or office of the Commission. Finally, this letter does not create or confer any rights for or obligations on any person or persons subject to compliance with the Commodity Exchange Act that bind the Commission or any of its other offices or divisions.

If you have any questions regarding this letter, please feel free to contact me at 202-418-6056, Warren Gorlick, Associate Director at 202-418-5195, or Carmen Moncada-Terry, Special Counsel at 202-418-5795.

Sincerely,

Joshua Sterling  
Director

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