

GMAC TECHNICAL ISSUES SUBCOMMITTEE RECOMMENDATION

Money Market Funds as Eligible Collateral

Issue:	Harmonize Money Market Funds (MMFs) as eligible collateral for non-cleared margin with other regulatory regimes.
Recommendations:	<ol style="list-style-type: none">1) Finalize proposed rule amendment to remove asset transfer restriction from eligible collateral rules.2) Encourage the US Prudential Regulators to adopt a corresponding amendment to their non-cleared margin rules, including allowing third country funds.3) Encourage EU policy makers to remove the third country fund restriction for eligible collateral from their non-cleared margin rules.
Background, Supporting Arguments or Examples & Data (if any)	<p><u>CFTC’s MMF Rule Amendment</u></p> <p>The CFTC proposed rule amendmentⁱ to remove the asset transfer restriction from MMFs used as eligible collateral for non-cleared margin will harmonize the parameters for MMF use with the UK and resolve one of the impediments to the use of MMFs between the US and the EU.. Implementing the proposed rule will also allow the CFTC to self-align MMFs with its eligible collateral requirements for cleared margin, per CFTC Regulation 1.25 (which governs the investment of customer money by futures commission merchants (“FCMs”) without similar asset transfer restrictions).</p> <p>The proposed rule amends aspects of the Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants (“Margin Rules”) based on the Recommendations to Improve Scoping and Implementation of Initial Margin Requirements for Non-Cleared Swaps (“GMAC Report”) adopted by the CFTC’s Global Markets Advisory Committee (“GMAC”) on July 22, 2020. The efforts of the Commission to take further steps to adopt the recommendations in the report are greatly appreciated by the industry. The CFTC should finalize the proposed amendment, and the industry will then begin to implement such changes once they become effective.</p> <p><u>Rationale for finalizing rule amendment</u></p> <p>The use of MMFs as eligible collateral is not as a direct pledge (or asset transfer) to meet margin obligations. MMFs are traditionally</p>

used when a pledgor meets a margin requirement with cash and then the custodian transforms, or sweeps, the cash into a MMF.

Therefore, without the ability to use MMFs widely, cash is not able to be used for Initial Margin (IM).

In the ISDA Margin Survey Year-End 2022, it was reported by 32 firms that cash was used for 73.8% of Regulatory VM, 68.4% of Discretionary VM, 37% of Independent Amount, and 2% of Regulatory IM.

The inability to post cash as IM and then transform to MMFs is a significant challenge for legal entities and funds that do not have ready-access to other types of eligible collateral because of their investment strategies, and therefore trading, operational, and settlement costs impact end-user performance. This results in increased transactional risks if a legal entity or fund has to transform cash into another type of eligible collateral before the collateral settlement cut-off time or maintain excess collateral within an asset type that is not part of the fund's primary investment strategy.

Although MMFs are allowed as eligible collateral under CFTC and other regulatory regimes' uncleared margin rules, there are key differences that do not allow a US entity to post a MMF that would also meet the regulatory requirements for an EU or UK entity. These differences are with the use of funds (i) issued in another jurisdiction (referred to as "third country funds") and (ii) which allow asset transfers (e.g. use of repurchase agreements, reverse repurchase agreements and securities lending ("repo")).

CFTC Margin Rules currently allow for third country funds to be posted, but do not allow for asset transfers. Because EU UCITS, for example, are allowed to execute asset transfers, US entities that face EU counterparties cannot use EU UCITS as eligible collateral. Cross-border harmonization on MMF eligibility will enable greater use of MMFs, resulting in reduced operational risk and investment performance drag to end-users.

But this is not just a cross border issue; US entities facing US counterparties have limited availability of MMFs because most funds allow repo. In addition, funds that do not allow repo have stricter reinvestment cut-off times which can negatively impact operational workflows and settlement processing.

Due to advocacy efforts from the industry, the UK now allows for third country funds to be usedⁱⁱ. As the UK rules do not restrict MMFs that allow asset transfers to be used as eligible collateral, the

	<p>CFTC’s amendment will enable use of MMFs between non-prudentially regulated swap dealers (SDs) and UK entities. Because the SEC allows SDs to follow CFTC requirements for eligible collateral, the CFTC’s amendment also facilitates the use of MMFs for margining security-based swaps transacted between non-prudentially regulated SDs and UK counterparties.</p> <p><u>Next step: Domestic and EU harmonization</u></p> <p>The CFTC has taken the lead in the US to address the recommendations in the GMAC Report; these efforts now include eliminating the asset transfer restrictions on MMFs. However, without domestic alignment, the benefit will only be available to non-prudentially regulated SDs and their counterparties. CFTC can further assist by encouraging US Prudential Regulators to make corresponding amendments to their non-cleared margin rules, including allowing third country funds.</p> <p>Unlike the CFTC and the UK, the EU does not currently allow for third country funds to be used as eligible collateral. Despite the CFTC’s effort to remove the asset transfer restriction, unless substituted compliance is available to the parties, MMFs will still not be eligible collateral between its SDs and EU entities. Having taken important steps themselves to resolve half of the cross-border issue, we recommend that the CFTC encourage EU policymakers to remove the third country fund restriction as the UK has done.</p>
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ⁱ 88 FR 53409

ⁱⁱ [PS11/22 – Margin requirements for non-centrally cleared derivatives: Amendments to BTS 2016/2251 | Bank of England](#)