



Commodity Futures Trading Commission

Office of Public Affairs

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Q & A – Protection of Cleared Swaps Customer Contracts and Collateral

What is the goal of the proposed rulemaking?

The goal of the proposed rules is to implement Section 724 of the Dodd-Frank Act, which prescribes the manner that cleared swaps (and related collateral) must be treated prior to and after bankruptcy. Section 724(a) amends the CEA by inserting a new section 4d(f), which imposes the following requirements on FCMs and depositories (including DCOs):

1. FCMs must treat and deal with all cleared swaps customer collateral (including accruals thereon) deposited by a customer to margin its cleared swaps as belonging to such customer;
2. FCMs may not commingle cleared swaps customer collateral (including accruals thereon) with its own property and may not, with certain exceptions, use such collateral to margin the cleared swaps of any person other than the customer depositing such collateral; and
3. DCOs may not hold or dispose of customer collateral that an FCM deposits as belonging to the FCM or any person other than the customer.

Section 724(b) governs the bankruptcy treatment of cleared swaps (and associated collateral) by clarifying that cleared swaps are “commodity contracts” within the meaning of section 761(4)(F) of the Bankruptcy Code, and that associated collateral, when deposited by customers, would be subject to the protections of Subchapter IV of Chapter 7 of the Bankruptcy Code and Commission Regulation Part 190 (Bankruptcy Rules).

What stakeholders may be affected by the proposed regulations

Swaps customers, futures commission merchants, and derivatives clearing organizations are likely to be affected by these proposed rules.

By when must responses to the request for comments be submitted?

Comments on the proposed rules must be submitted within sixty (60) days of the publication of such rules in the Federal Register.

What model is the Commission proposing?

After considering comments that it received, the Commission is proposing a model entitled “Complete Legal Segregation” (referred to in the ANPR as the “Legal Segregation with Commingling” model). This model would allow the collateral of all of an FCM’s swaps customers to be kept together pre-bankruptcy in one account. But, in the event of a default by a clearing member of both an FCM and one or more of its cleared swaps customers, a DCO would not have recourse to the collateral posted by non-defaulting customers. The DCO would only have recourse against the collateral of the defaulting customers of that clearing member (as well as resources of the clearing member itself).

Under the Complete Legal Segregation Model must an FCM’s swaps customer accounts be segregated pre-bankruptcy?

The Complete Legal Segregation Model requires that swaps customer collateral be segregated from the FCM’s own property, but permits the cleared swaps collateral of all FCM customers to be kept together pre-bankruptcy in one

account. The proposed rules, to the extent applicable, parallel (in updated language) the regulations governing the segregated accounts in which FCMs currently hold futures customer collateral pre-bankruptcy.

Are any other models being considered?

Yes. Because the Commission is still evaluating the costs and benefits associated with the Complete Legal Segregation Model, the Commission is also considering a model entitled Legal Segregation with Recourse (referred to in the ANPR as the “Moving Customers to the Back of the Waterfall” model), in which the DCO would have recourse to collateral posted by non-defaulting customers of the defaulting FCM clearing member, but only after exhausting its own contribution to its default resources, as well as the guaranty fund contributions of non-defaulting clearing members. In addition, the Commission is seeking additional comment on the Futures Model (referred to in the ANPR as the “Baseline Model”) and a number of Optional Approaches (namely, permitting clearing organizations to choose between models).

Does this rulemaking affect futures?

None of the segregation provisions in Part 22 have any effect on segregation for exchange-traded futures. Some of the technical changes to Part 190, however, will affect both swaps and futures, but only with respect to an FCM in bankruptcy.

What types of investments does the Commission propose to permit for cleared swaps customer collateral?

The proposed rules provide that cleared swaps customer collateral may only be invested pursuant to Commission Regulation 1.25 (as it may be amended from time to time), which governs investment of customer property of futures customers. The proposed regulations do not, however, limit the types of collateral that a customer may post.

How did the Commission evaluate the costs and benefits of the proposal?

The proposed rule contains an analysis of the costs and benefits of each model described in the ANPR. This analysis incorporates estimates and observations regarding costs and benefits found in the comments that the Commission received to the ANPR. Because the Commission is still considering these costs and benefits, the proposal requests additional information on the costs and benefits of the Complete Legal Segregation Model, the Legal Segregation with Recourse Model, the Futures Model, and the Optional Approaches.

What other matters do the proposed rules address?

The Commission is proposing amendments to its Regulation Part 190 to implement changes wrought by the Dodd-Frank Act, including the inclusion of swaps cleared with a DCO as customer contracts for all commodity brokers, the inclusion of swaps execution facilities as a category of trading venue, and additional conforming changes to time periods. The proposed rules also include changes to conform Regulation Part 190 to current swaps market practices.

When will final rules implementing the requirements of the statute be published?

The Commission will consider the comments promptly after the deadline for responses closes, and will expeditiously move to publish final rules.