

MEMO# 32783

September 25, 2020

CFTC Issues Supplemental Proposal on Part 190 Bankruptcy Regulations - ICI Member Call October 9

[32783]

September 25, 2020 TO: Derivatives Markets Advisory Committee RE: CFTC Issues Supplemental Proposal on Part 190 Bankruptcy Regulations - ICI Member Call October 9

On September 17th, the Commodity Futures Trading Commission (CFTC or “Commission”) unanimously approved a supplemental notice of proposed rulemaking (“Supplemental Proposal”) that is intended to address a concern raised by commenters about whether one of the CFTC’s proposed rules would hinder the ability of a derivatives clearing organization (DCO) in resolution to apply its close-out netting rules.[\[1\]](#) Comments on the Supplemental Proposal, which is summarized below, are due to the CFTC by October 26th.

ICI will hold a member call on October 9th, from 1:00-2:00 pm ET, to discuss the Supplemental Proposal and potential ICI comments. We are pleased to be joined on the call by our outside counsel from Cleary Gottlieb. We will send you an Outlook invitation for the member call that will include dial-in information. We look forward to your questions and comments.

Background

In April, the CFTC issued proposed amendments to its Part 190 bankruptcy regulations that are intended to update Part 190 for the first time in 37 years to reflect current market practices and lessons learned from past commodity broker bankruptcies (“April Proposal”).[\[2\]](#) Many commenters, including ICI,[\[3\]](#) expressed overall support for the April Proposal, but conveyed concerns about certain aspects of the proposal and provided recommendations for improvement. Several DCOs, as well as other commenters,[\[4\]](#) expressed concern that operation of proposed regulation 190.14(b)(2) and (3) could undermine the enforceability of certain DCO closeout netting provisions and questioned whether, for bank-affiliated clearing members, the proposed regulation would cause these arrangements to no longer qualify as a “qualifying master netting agreement” (QMNA) for purposes of the bank capital requirements that have been established by the US prudential regulators.[\[5\]](#) Proposed regulation 190.14(b)(2) and (3) would have allowed a DCO to continue operating for six or fewer days after an order for relief was entered where, among other things, continued operation would facilitate resolution under Title II of the Dodd-Frank Act or transfer of clearing operations to another DCO.[\[6\]](#)

Currently, the definition of QMNA requires that “any exercise of rights under the agreement will not be stayed or avoided under applicable law in the relevant jurisdictions, other than . . . [i]n receivership, conservatorship, or resolution under the Federal Deposit Insurance Act, [Title II Resolution] or under any similar insolvency law applicable to GSEs, or laws of foreign jurisdictions that are substantially similar to” the foregoing.^[7] This definition does not, however, exclude a bankruptcy subject to Part 190. The CFTC explains that, as a result, “to the extent that proposed §190.14(b)(2) and (3) acts as a stay, it would undermine the QMNA status of DCO rules,” with detrimental implications for close-out netting by bank-affiliated clearing members.

Supplemental Proposal

The Supplemental Proposal is intended to address these concerns. It would withdraw proposed regulation 190.14(b)(2) and (3). The CFTC instead proposes a stay on the derivatives contracts of DCOs that are Systemically Important DCOs (SIDCOs) for a brief time after bankruptcy in order to foster the success of a Title II resolution, if the FDIC is appointed receiver in the resolution proceeding within that time.

The CFTC’s proposed stay is intended to be consistent with the QMNA status of SIDCO rules. The length of the stay would be the shorter of (i) the period of time beginning on the commencement of the proceeding and ending at the later of 5 pm ET on the business day following the date of the commencement of the proceeding and 48 hours after the commencement of the proceeding;^[8] or (ii) the shortest such period specified in an action by any of the prudential regulators with respect to their SIDCO rules.^[9] The proposed provision would explicitly prohibit continued collection or payments of initial or variation margin during the Part 190 stay. If adopted, the CFTC’s proposed stay provision would become effective only if the CFTC concludes that the prudential regulators have taken steps to make the proposed Part 190 stay consistent with the QMNA status of SIDCO rules.^[10]

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endnotes

^[1] Bankruptcy Regulations, 85 Fed. Reg. 60110 (Sept. 24, 2020), *available at* <https://www.govinfo.gov/content/pkg/FR-2020-09-24/pdf/2020-21005.pdf>.

^[2] For a summary of the April Proposal, *please see* ICI Memorandum No. 32481 (May 22, 2020), *available at* https://www.ici.org/my_ici/memorandum/memo32481.

^[3] ICI’s comment letter on the April Proposal is *available at* <https://www.ici.org/pdf/32595a.pdf>.

^[4] Comments on the April Proposal are *available at* <https://comments.cftc.gov/PublicComments/CommentList.aspx?id=3097>.

^[5] For these purposes, the US prudential regulators are the Federal Deposit Insurance Corporation (FDIC), the Board of Governors of the Federal Reserve System, and the office of the Comptroller of the Currency.

[6] Proposed section 190.14(b) explicitly would have permitted the DCO to make calls for variation and initial margin during this period of ongoing operation.

[7] See, e.g., 12 CFR 324.2 (FDIC definition of QMNA).

[8] This formulation of the stay period is consistent with the stay period the prudential regulators have adopted in the context of their regulations on stays in qualified contacts of certain banks subject to their supervision. See, e.g., 12 CFR 382.4 (FDIC rules).

[9] We understand there may be a question of whether the CFTC's proposed stay could be "tacked on" to the FDIC stay in a Title II resolution proceeding, potentially resulting in a stay of up to five calendar days.

[10] The CFTC does not include proposed rule text in the Supplemental Proposal and does not mention a further opportunity for public notice and comment once it drafts such text. Rather, it states that it will provide public notice and comment once the prudential regulators have taken actions sufficient to make the Part 190 stay provision consistent with the QMNA status of SIDCO rules. Public comment would be limited to whether the prudential regulators' actions are sufficient to achieve that objective.

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