

**MEMO# 26500**

September 13, 2012

# **ICI Comment Letter in Response to CFTC's Reopening of Comment Period on Proposed Margin Requirements for Uncleared Swaps**

[26500]

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TO: CLOSED-END INVESTMENT COMPANY COMMITTEE No. 30-12  
DERIVATIVES MARKETS ADVISORY COMMITTEE No. 49-12  
INTERNATIONAL COMMITTEE No. 34-12  
INVESTMENT ADVISER MEMBERS No. 29-12  
SEC RULES COMMITTEE No. 54-12 RE: ICI COMMENT LETTER IN RESPONSE TO CFTC'S  
REOPENING OF COMMENT PERIOD ON PROPOSED MARGIN REQUIREMENTS FOR  
UNCLEARED SWAPS

ICI has submitted a comment letter to the Commodity Futures Trading Commission ("CFTC" or "Commission") on its proposed margin rules for uncleared swaps. The CFTC re-opened the comment period in response to a consultation paper published by the Basel Committee on Banking Supervision ("BCBS") and the International Organization of Securities Commissions ("IOSCO") to establish international minimum standards for margin requirements for uncleared derivatives. [\[1\]](#) The comment letter is attached and summarized briefly below.

The letter is intended to supplement our prior submission to the Commission in view of the Consultation Paper. [\[2\]](#) The letter states that the international regulators' proposed requirements in several key areas are instructive and consistent with ICI's previous suggestions to the Commission. The letter urges the Commission to work closely with the BCBS and IOSCO as they finalize the global standards and to adapt its requirements to reflect the emerging global consensus on margin requirements for uncleared swaps to the extent possible.

## **I. Two-Way Margin**

To better protect counterparties and the swaps markets more generally, the letter strongly urges the Commission, as ICI did in the July 2011 ICI Letter, to adopt final rules to require

SDs and MSPs (“covered swap entities”) to post margin to their non-covered swap entity counterparties at the same level and in the same manner as required for the counterparty. This fundamental requirement is consistent with the proposed global standard as proposed by the BCBS and IOSCO under which entities that engage in non-centrally-cleared derivatives would be required to exchange, on a bilateral basis, initial and variation margin in mandatory minimum amounts. The letter recommends that the CFTC amend its proposal, which would not require covered swap entities to post margin to their counterparties in those instances when their counterparties were required to post margin.

## **II. Use of Thresholds**

The letter recommends that registered funds be permitted to use thresholds and not to post margin under certain thresholds. The letter argues that use of thresholds should not be limited to entities that are subject to capital requirements established by a prudential regulator or a state insurance regulator. The letter notes that the BCBS and IOSCO stated that it may be desirable to apply different thresholds for initial margin (the amount under which a firm would have the option of not collecting initial margin) to different types of derivatives market participants. As highly regulated, financially sound swap counterparties and in recognition of the stringent securities regulation to which they are subject, the letter states that the CFTC should permit regulated funds to use an initial margin threshold below which they are not required to post collateral.

## **III. Calculation of Margin**

The letter recommends (as in the July 2011 ICI Letter) that the CFTC adopt a system of calculating initial margin that would permit the counterparty to choose between a covered swap entity’s proprietary model and a standardized table that specifies minimum initial margin as a percentage of the notional amount of a swap or security-based swap (with percentage ranges assigned to broad asset classes). The suggested approach is consistent with the proposal by the BCBS and IOSCO, which would permit the required amount of initial margin to be calculated by reference either to a quantitative portfolio margin model (subject to certain conditions) or a standardized margin schedule based on a percentage of notional exposure by asset class. The letter argues that providing the counterparty with the option between a quantitative portfolio margin model or a standardized table or schedule would promote greater uniformity and transparency for market participants and be easier to administer operationally than the approach proposed by the Commission.

## **IV. Forms of Margin**

Consistent with recommendations of the international regulators and the recommendations made in the July 2011 ICI Letter, the letter takes the view that the CFTC should expand the proposed list of eligible collateral to allow counterparties to a swaps transaction the flexibility to agree upon the appropriate collateral that may be posted for a particular swap. The CFTC’s proposal would limit the categories of eligible collateral to cash, U.S. Treasuries and, for initial margin only, certain government securities.

In light of the proposal by the BCBS and IOSCO for a broader set of eligible collateral, the letter urges the CFTC to expand the list of eligible collateral. For registered funds, the letter states that restricting collateral to a narrow range of permitted assets may force funds to hold lower-yielding securities at an increased cost to fund shareholders and/or to hold assets that do not correspond to the fund’s investment objectives.

## V. Daily Valuation of Margin

Finally, the letter recommends that the Commission require at least daily valuation of margin as suggested by the BCBS and IOSCO. Daily valuation of margin will help ensure that accurate exposures are being covered. Without frequent valuation of margin, counterparties will not be able to calibrate the amount of margin to the value of the swap positions.

Jennifer S. Choi  
Senior Associate Counsel – Securities Regulation

[Attachment](#)

### endnotes

[1] Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, RIN 3038-AC97, 77 FR 41109 (July 12, 2012), available at <http://www.gpo.gov/fdsys/pkg/FR-2012-07-12/pdf/2012-16983.pdf>. See Margin Requirements for Non-Centrally-Cleared Derivatives, Basel Committee on Banking Supervision and Board of the International Organization of Securities Commissions, July 2012, available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD387.pdf> (“Consultation Paper”).

[2] See Letter from Karrie McMillan, General Counsel, ICI, to David A. Stawick, Secretary, CFTC, dated July 11, 2011 (“July 2011 ICI Letter”).