

MEMO# 31492

November 20, 2018

ICI Files Comment Letter with SEC on Proposals Regarding Capital, Margin, and Segregation Requirements for Security-Based Swap Dealers and Major Security-Based Swap Participants

[31492]

November 20, 2018 TO: ICI Members

ICI Global Members

Derivatives Markets Advisory Committee

ICI Global Regulated Funds Committee

ICI Global Trading & Markets Committee SUBJECTS: Compliance

Derivatives

International/Global

Investment Advisers

Trading and Markets RE: ICI Files Comment Letter with SEC on Proposals Regarding Capital, Margin, and Segregation Requirements for Security-Based Swap Dealers and Major Security-Based Swap Participants

On November 19th, ICI filed the attached comment letter in response to the Securities and Exchange Commission's reopening of the comment period and request for additional comments on several proposals relating to capital, margin, and segregation requirements regarding uncleared, security-based swaps ("SB swaps") for security-based swap dealers (SBSDs) and major security-based swap participants (MSBSPs) that do not have a prudential regulator.[\[1\]](#) The Reopened Proposing Release relates to three different proposals the SEC issued in 2012, 2013, and 2014, respectively (together, "SB Swaps Proposals").

The letter expresses ICI's concerns that the Reopened Proposing Release proposes such a radically different framework for SBSBD capital and margin, as compared to that which is applicable to swap dealers and non-SEC-regulated SBSBDs, that the SEC's proposal, if adopted, is likely to lead to fragmentation of the SB swaps markets, a reduction in the ability of counterparties to net exposures, and substantial uncertainty regarding the treatment in bankruptcy of SB swaps. We are also troubled that the Reopened Proposing Release does not address the many substantive comments that ICI and others submitted on the SB Swaps Proposals.

The letter points out that Congress, in adopting the Dodd-Frank Act, expressly directed the SEC to seek consistency in its regulations, where practicable, with the Commodity Futures Trading Commission. The Reopened Proposing Release, however, does not appear to reflect any coordination by the SEC with any of its fellow regulators, nor does the release take account of the significant changes in the SB swaps markets in the six years since the SEC proposed its capital, margin, and segregation rules for SBSDs and MSBSPs. In that regard, we note that the SB swap markets have changed greatly since 2012, driven in large part by market participants' response to the CFTC's regulation of swaps and the European Union's regulation of swaps and SB swaps.

The letter explains that the Reopened Proposing Release also fails to provide the public with an adequate basis to comment. It does not provide sufficient notice regarding how the SEC is considering altering the SB Swaps Proposals. Instead, the Reopened Proposing Release leaves market participants guessing about the potential changes that the SEC is considering.

To address these serious substantive and procedural concerns, ICI urges the SEC to re-propose margin rules that are consistent in all material respects with both the 2013 international framework governing margin requirements for uncleared derivatives, including SB swaps ("International Framework"), and the final rules on margin for uncleared swaps that have already been adopted and implemented by the CFTC and the US prudential regulators (together, "Swap Margin Rules"). We also recommend that the SEC consider carefully and address the comments it receives in response to the Reopened Proposing Release and those comments it received in the past on the SB Swaps Proposals.

We assert that, at a minimum, it is critical that the SEC include the following revisions in any final rules, consistent with the Swap Margin Rules and the International Framework:

- Adopt a margin-based approach rather than a capital-based approach that allows counterparties to close out and net positions, using posted collateral, upon the insolvency of an SBSD;
- Require bilateral exchange of collateral by SBSDs and MSBSPs and their counterparties in connection with SB swaps;
- Facilitate payment netting and close-out netting of SB swaps;
- Require only those counterparties that have "material swaps exposure" to post initial margin;
- Permit SBSDs to set a standard threshold for exchange of initial margin and raise the minimum transfer amount cap;
- Do not impose capital charges on SBSDs and MSBSPs when their counterparties elect to have their collateral held at a third-party bank custodian;
- To the extent the SEC includes an exception to capital charges, revise the proposed exception to make it workable;
- Expand permitted collateral to allow funds to post shares of registered investment companies and ETFs issued by an affiliate of the fund; and
- Do not adopt rules on portfolio margining without first issuing a proposal that provides significantly more detail and analysis regarding the legal implications of these arrangements.

In addition, ICI urges the SEC to develop a uniform substituted compliance framework in coordination with other US and global regulators. The substituted compliance framework should, at a minimum, allow for consistent collateral posting and segregation requirements globally for swaps and SB swaps.

The letter also explains that the SEC should provide an adequate compliance period for SBSBs and MSBSBs and their counterparties to implement any final SEC SB swap rules, following a re-proposal.

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[Attachment](#)

endnotes

[1] *Capital, Margin, and Segregation Requirements for Security-Based Swap Dealers and Major Security-Based Swap Participants and Capital Requirements for Broker-Dealers*, Exchange Act Release No. 84409 (Oct. 11, 2018), 83 FR 53007 (Oct. 19, 2018) **available at** <https://www.gpo.gov/fdsys/pkg/FR-2018-10-19/pdf/2018-22531.pdf> (“Reopened Proposing Release”).

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