



U.S. COMMODITY FUTURES TRADING COMMISSION

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**Re: Time Limited No-Action Position with Respect to Margin for
Uncleared Swaps and Swap Clearing Requirement related to the
Conclusion of the Brexit Transition Period**

I. Introduction

This letter is in response to a request for a no-action position received by the Market Participants Division (“**MPD**”) and the Division of Clearing and Risk (“**DCR**” and together with MPD, the “**Divisions**”) of the Commodity Futures Trading Commission (“**CFTC**” or “**Commission**”) from the International Swaps and Derivatives Association, Inc. (“**ISDA**”). ISDA’s members include swap dealers (“**SDs**”) that are registered with the Commission and subject to the Commission’s rules regarding margin requirements for uncleared swaps¹ and the Commission’s swap clearing requirement promulgated pursuant to section 2(h)(1)(A) of the Commodity Exchange Act (“**CEA**”)² and codified in Part 50 of the Commission’s regulations (the “**Clearing Requirement**”).³ Specifically, ISDA requests that the Divisions provide relief from the CFTC Margin Rule (as defined below) and the Clearing Requirement for certain legacy swaps assigned or novated to certain affiliates planning for, or in response to, the end of the transition period

¹ The Commission’s margin requirements for uncleared swaps apply only to SDs and major swap participants for which there is not a prudential regulator. *See* 7 U.S.C. 6s(e)(1)(B). SDs and major swap participants for which there is a prudential regulator must meet the margin requirements for uncleared swaps established by the applicable prudential regulator. 7 U.S.C. 6s(e)(1)(A). *See also* 7 U.S.C. 1a(39) (defining the term “**Prudential Regulator**” to include the Board of Governors of the Federal Reserve System; the Office of the Comptroller of the Currency; the Federal Deposit Insurance Corporation; the Farm Credit Administration; and the Federal Housing Finance Agency). The Prudential Regulators published final margin requirements in November 2015. *See* Margin and Capital Requirements for Covered Swap Entities, 80 FR 74840 (Nov. 30, 2015) (“**Prudential Margin Rule**”). The Prudential Margin Rule is similar to the CFTC Margin Rule, including with respect to the CFTC’s phasing-in of margin requirements, as discussed below.

² 7 U.S.C. § 2(h)(1)(A).

³ 17 CFR part 50.

following the withdrawal of the United Kingdom (“UK”) from the European Union (“EU”).⁴

This letter is also being provided consistent with the Joint Statement by UK and US Authorities on Continuity of Derivatives Trading and Clearing Post-Brexit of February 25, 2019.⁵

II. CFTC Regulatory Background

(1) Margin

Section 4s(e) of the CEA directs the Commission to adopt rules establishing minimum initial and variation margin requirements on all swaps⁶ that are (i) entered into by an SD for which there is no Prudential Regulator (collectively, “CSEs”) and (ii) not cleared by a registered derivatives clearing organization (“DCO”) (“**uncleared swaps**”).⁷ To this end, the Commission promulgated the CFTC Margin Rule in January 2016,⁸ establishing requirements for a CSE to collect and post initial margin and variation margin for uncleared swaps. These requirements vary based on the type of counterparty to such swaps and the location of the CSE and its counterparty.⁹ These requirements also generally apply only to uncleared swaps entered into on or after the compliance date applicable to a particular CSE and its counterparty (each a “**covered swap**”).¹⁰ An

⁴ See ISDA Letter, dated Oct. 28, 2020 (“**ISDA Letter**”).

⁵ Available at <https://www.cftc.gov/PressRoom/PressReleases/7876-19>. Pursuant to the Joint Statement, the Commission committed to extending existing regulatory relief granted by the CFTC to EU firms, including UK firms, to UK firms at the point of the UK’s withdrawal from the EU.

⁶ For the definition of swap, see section 1a(47) of the CEA and Commission regulation 1.3. 7 U.S.C. 1a(47) and 17 CFR 1.3. It includes, among other things, an interest rate swap, commodity swap, credit default swap, and currency swap.

⁷ See 7 U.S.C. 6s(e)(2)(B)(ii). In Commission regulation 23.151, the Commission further defined this statutory language to mean all swaps that are not cleared by a registered DCO or a DCO that the Commission has exempted from registration as provided under the CEA. 17 CFR 23.151.

⁸ Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 81 FR 636 (Jan. 6, 2016) (“**CFTC Margin Rule**”). The CFTC Margin Rule, which became effective April 1, 2016, is codified in part 23 of the Commission’s regulations. 17 CFR 23.150 through 23.159, 23.161. In May 2016, the Commission amended the CFTC Margin Rule to add Commission regulation 23.160, providing rules on its cross-border application. Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants – Cross-Border Application of the Margin Requirements, 81 FR 34818 (May 31, 2016). 17 CFR 23.160.

⁹ See Commission regulations 23.152 and 23.153, 17 CFR 23.152 and 23.153. For example, the CFTC Margin Rule does not require a CSE to collect margin from, or post margin to, a counterparty that is neither a swap entity nor a financial end user (each as defined in 17 CFR 23.151). Pursuant to section 2(e) of the CEA, 7 U.S.C. 2(e), each counterparty to an uncleared swap must be an eligible contract participant, as defined in section 1a(18) of the CEA, 7 U.S.C. 1a(18). See Commission regulation 23.160 on the cross-border application of the CFTC Margin Rule. 17 CFR 23.160.

¹⁰ Pursuant to Commission regulation 23.161, compliance dates for the CFTC Margin Rule are staggered such that CSEs must come into compliance in a series of phases. The first phase affected CSEs and their counterparties, each with the largest aggregate outstanding notional amounts of uncleared swaps and

uncleared swap entered into prior to a CSE's applicable compliance date for a particular counterparty (each a "**Margin Legacy Swap**") is generally not subject to the margin requirements in the CFTC Margin Rule.¹¹

To the extent that more than one uncleared swap is executed between a CSE and its covered counterparty, the CFTC Margin Rule permits the netting of required margin amounts of each swap under certain circumstances.¹² In particular, the CFTC Margin Rule, subject to certain limitations, permits a CSE to calculate initial margin and variation margin, respectively, on an aggregate net basis across uncleared swaps that are executed under the same eligible master netting agreement ("**EMNA**"). Moreover, the CFTC Margin Rule permits swap counterparties to identify one or more separate netting portfolios (*i.e.*, a specified group of uncleared swaps the margin obligations of which will be netted only against each other) under the same EMNA, including having separate netting portfolios for covered swaps and Margin Legacy Swaps.¹³ A netting portfolio that contains only Margin Legacy Swaps is not subject to the initial and variation margin requirements set out in the CFTC Margin Rule.¹⁴ However, if a netting portfolio contains any covered swaps, the entire netting portfolio (including all Margin Legacy Swaps) is subject to such requirements.¹⁵

A Margin Legacy Swap may lose its legacy treatment under the CFTC Margin Rule, causing it to become a covered swap and causing any netting portfolio in which it is included to be subject to the requirements of the CFTC Margin Rule. For reasons discussed in the CFTC Margin Rule, the Commission elected not to extend the meaning of Margin Legacy Swaps to include (1) Margin Legacy Swaps that are amended in a material or nonmaterial manner; (2) novations of Margin Legacy Swaps; and (3) new swaps that result from portfolio compression of Margin Legacy Swaps.¹⁶ Therefore, and as relevant here, a Margin Legacy Swap that is amended after the applicable compliance

certain other financial products. These CSEs began complying with both the initial and variation margin requirements of the CFTC Margin Rule on September 1, 2016. The second phase began March 1, 2017, and required CSEs to comply with the variation margin requirements of Commission regulation 23.153 with all relevant counterparties not covered in the first phase. *See* 17 CFR 23.161. On each September 1 thereafter ending with September 1, 2022, CSEs must comply with the initial margin requirements with counterparties with successively lesser outstanding notional amounts.

¹¹ *See* CFTC Margin Rule, 81 FR at 651 and Commission regulation 23.161. 17 CFR 23.161.

¹² *See* CFTC Margin Rule, 81 FR at 651 and Commission regulations 23.152(c) and 23.153(d). 17 CFR 23.152(c) and 23.153(d).

¹³ *See* CFTC Margin Rule, 81 FR at 651 and Commission regulations 23.152(c)(2)(ii) and 23.153(d)(2)(ii). 17 CFR 23.152(c)(2)(ii) and 23.153(d)(2)(ii).

¹⁴ *Id.*

¹⁵ *Id.*

¹⁶ *See* CFTC Margin Rule, 81 FR at 675. Certain limited relief has been given from this standard. *See* Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 83 FR 60341 (Nov. 26, 2018) and CFTC Staff Letter No. 17-52 (Oct. 27, 2017), *available at* <http://www.cftc.gov/ucm/groups/public/@lrllettergeneral/documents/letter/17-52.pdf>.

date may become a covered swap subject to the initial and variation margin requirements in the CFTC Margin Rule. In that case, netting portfolios that were intended to contain only Margin Legacy Swaps and, thus, not be subject to the CFTC Margin Rule may become so subject.

(2) Clearing Requirement

Section 2(h)(1)(A) of the CEA, states that “[i]t shall be unlawful for any person to engage in a swap unless that person submits such swap for clearing to a [DCO] that is registered under [the CEA] or a [DCO] that is exempt from registration under [the CEA] if the swap is required to be cleared.”¹⁷ In 2012, the Commission issued a Clearing Requirement Determination, which requires market participants to clear two classes of credit default swaps and four classes of interest rate swaps.¹⁸ In 2016, the Commission issued a second Clearing Requirement Determination, which expanded the Clearing Requirement to include additional interest rate swaps.¹⁹

Like the CFTC Margin Rule, the Commission’s Clearing Requirement Determinations established a series of compliance dates to phase-in compliance with the Clearing Requirement.²⁰ Commission regulation 50.5 provides that swaps entered into before July 21, 2010, or the application of the Clearing Requirement for a particular class of swaps are not subject to the Clearing Requirement so long as such swaps are reported to a swap data repository (“**Clearing Legacy Swap**”).²¹

The Commission clarified that the Clearing Requirement applies to all new swaps, as well as changes in the ownership of a swap, including assignment, novation, exchange, transfer, or conveyance.²² Notably, the Commission did not address amendments, material or otherwise, to existing swaps.²³

¹⁷ 7 U.S.C. § 2(h)(1)(A).

¹⁸ See Clearing Requirement Determination Under Section 2(h) of the CEA, 77 FR 74284, 74315-16, 74336-37 (Dec. 13, 2012) (establishing Commission regulation 50.4, which sets forth the classes of swaps that are required to be cleared).

¹⁹ See Clearing Requirement Determination Under Section 2(h) of the Commodity Exchange Act for Interest Rate Swaps, 81 FR 71202 (Oct. 14, 2016) (expanding the Clearing Requirement to include fixed-to-floating interest rate swaps in nine additional currencies and making certain other modifications to the scope of the 2012 Clearing Requirement).

²⁰ See 77 FR at 74319-20; 81 FR at 71226-30.

²¹ 17 CFR 50.5.

²² See 77 FR at 74316.

²³ The Commission discussed certain negotiated swap provisions that counterparties may undertake based on the goal of reducing counterparty credit risk and stated that these changes to a swap would be viewed as “legitimate business purpose considerations on a case-by-case basis in conjunction with all other relevant facts and circumstances” and would be an affirmative defense to any charges of evasion of the clearing requirement. See *id.* at 74319. DCR believes that this preamble discussion of public policy considerations by the Commission offers additional support for the no-action position taken by staff in this letter.

III. Brexit Background

In June 2016, the people of the UK voted by referendum to leave the EU (“**Brexit**”). On March 29, 2017, the UK submitted notification of its intention to withdraw from the EU at the conclusion of a two-year period pursuant to Article 50 of the Treaty on European Union.²⁴

As a result of Brexit, financial entities, including CSEs in the UK,²⁵ faced uncertainty about the applicable regulatory framework they will operate within after such withdrawal, especially a UK exit from the EU absent a negotiated agreement on the specific terms of the UK’s exit (i.e., a “**No-deal Brexit**”). In particular, concerns arose from the potential inability of the firms, if located in the UK, to continue providing investment services related to swaps in the EU under the current passporting regime. On April 1, 2019, in order to address these concerns and maintain the status quo for legacy swaps with respect to the CFTC Margin Rule, the Commission adopted an interim final rule (the “**IFR**”) allowing CSEs, solely in the event of a No-deal Brexit, to enter into certain amendments to effect legal transfers of Margin Legacy Swaps between their margin affiliates (as defined in Commission regulation 23.151) without bringing such swaps into scope for the CFTC Margin Rule, as explained above.²⁶ The IFR did not address the application of the Clearing Requirement.

On October 19, 2019, the UK and the EU entered into the Agreement on the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and the European Atomic Energy Community (the “**Withdrawal Agreement**”). Pursuant to the Withdrawal Agreement, the UK has ceased to be a member of the EU, and a transition period began.²⁷ During the transition period EU law and EU regulatory, budgetary, supervisory, judiciary, and enforcement instruments and structures have continued to apply in the UK as if it were a member of the EU. Further, because a No-deal Brexit has not occurred, the provisions of the IFR that provide for the transfer of certain Margin Legacy Swaps without bringing such swaps into scope for the CFTC Margin Rule are not applicable.

IV. Request for Relief

²⁴ See Article 50 of the Treaty on European Union, available at <https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:12012M050&from=EN>.

²⁵ In many instances, these firms made a strategic decision decades ago to use a UK establishment as their base of operations to provide financial services to customers across the EU, consistent with the EU’s system of cross-border authorizations to engage in regulated financial activities (known as “passporting”).

²⁶ See Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 84 FR 12065 (Apr. 1, 2019).

²⁷ As of the date of this letter, the Divisions anticipate the transition period will expire on December 31, 2020.

ISDA states that during the transition period, while the UK continues to be treated as if it were an EU Member State, the UK and EU have been negotiating the terms of a free trade agreement (“**UK-EU FTA**”) that will govern the relationship between the UK and EU following the end of the transition period. ISDA states that, as of the date of its request: (i) it is still unknown whether a UK-EU FTA will be in place when the transition period ends; (ii) that it is unlikely that the availability of a UK-EU FTA will be known until the final weeks, or even days, of the transition period; and (iii) that any UK-EU FTA that may be completed is unlikely to include continued rights for UK firms to carry on cross-border activities with EU counterparties (i.e., “passporting rights”).²⁸ Given the state of UK-EU negotiations and the likely loss of the ability of UK SDs to service their EU counterparties, ISDA states that the end of the transition period, similar to a No-deal Brexit, raises the need for SDs to be able to transfer uncleared swaps between affiliates as part of their strategic response to the impact of Brexit on their business.

Therefore, ISDA requests that the Commission provide relief in order to facilitate an orderly response to Brexit by SDs and avoid unintended impacts to the application of, and compliance with, the CFTC Margin Rule and the Clearing Requirement with respect to amendments to legacy swaps. Specifically, ISDA requests that the Commission extend relief to SDs to facilitate voluntary transfers of Margin Legacy Swaps and Clearing Legacy Swaps between affiliates solely in preparation for or response to the end of the Brexit transition period regardless of whether or not a UK-EU FTA is agreed prior to the end of the transition period, and that such relief be made available for a period of at least 12 months following the end of the transition period.²⁹

V. MPD Staff Position

After considering the request for relief and the related facts and circumstances, MPD believes that a no-action position is warranted. Specifically, MPD believes that, similar to what was provided by the IFR, certain relief is appropriate to maintain the status quo for Margin Legacy Swaps with respect to the CFTC Margin Rule to the extent any amendments thereto are made solely to transfer such swaps in response to the end of the Brexit transition period.

Accordingly, MPD will not recommend that the Commission take an enforcement action against a CSE registered with the Commission as an SD for failure to comply with the CFTC Margin Rule with respect to a Margin Legacy Swap solely to the extent that such compliance would be required as a result of an amendment to the swap entered into under the following conditions (each a “**Margin Covered Amendment**”):

²⁸ The Divisions note that whether a UK-EU FTA includes passporting rights will be a result of political decisions beyond the control of the parties to legacy swaps and not driven by U.S. regulatory policy.

²⁹ ISDA notes that it has requested similar relief from EU authorities. Further, ISDA states that, if any relief would fall away upon conclusion of a UK-EU FTA, there is insufficient incentive for SDs and (in particular) their clients to effect the transfer of uncleared swaps in anticipation of the impact of Brexit as such actions would require the application of the CFTC Margin Rule or the Clearing Requirement. See ISDA Letter at 2.

- (1) Solely in connection with a party to a Margin Legacy Swap's planning for or response to the expiration of the Brexit transition period specified in the Withdrawal Agreement (the "**Brexit Transition Period Expiration**," and the date of such expiration, as such may be extended or modified from time to time, the "**Brexit Transition Period Expiration Date**"), one or both parties to the swap transfers the swap to its margin affiliate³⁰, or a branch or other authorized form of establishment of the transferor, and the parties make no other transfers of the swap;
- (2)
 - (a) A CSE is a transferee from a party to the swap; or
 - (b) A CSE is a remaining party to the swap, and the transferor represents to the CSE that the transferee is a margin affiliate, or a branch or other authorized form of establishment of the transferor, and that the transfer was made solely in connection with the transferor's planning for or response to the Brexit Transition Period Expiration;³¹
- (3) The amendment does not modify any of the following: the payment amount calculation methods,³² the maturity date, or the notional amount of the swap;
- (4) The amendment takes effect no earlier than the date of this letter; and
- (5) The amendment is entered into and takes effect no later than the date that is one year after the Brexit Transition Period Expiration Date.

VI. DCR Staff Position

³⁰ As defined in Commission regulation 23.151 (17 CFR 23.151), a company is a margin affiliate of another company if: (1) Either company consolidates the other on a financial statement prepared in accordance with U.S. Generally Accepted Accounting Principles, the International Financial Reporting Standards, or other similar standards, (2) Both companies are consolidated with a third company on a financial statement prepared in accordance with such principles or standards, or (3) For a company that is not subject to such principles or standards, if consolidation as described in paragraph (1) or (2) of this definition would have occurred if such principles or standards had applied.

Under Commission regulation 23.161, 17 CFR 23.161, a margin affiliate's relevant swaps are included in determining the applicable compliance date for the CSE and counterparty under Commission regulation 23.161, 17 CFR 23.161, and thus the compliance date of a CSE and its margin affiliates facing the same counterparty (or its margin affiliates) should generally be the same.

³¹ Each representation requested in this letter is a collection of information under OMB 3038-0049. No person is required to respond to this request for information unless a valid OMB number is displayed.

³² MPD does not believe the relief being provided should be expansively applied to encompass economic changes to a legacy swap. Accordingly, the relief is unavailable if the amendments to an uncleared swap modify the payment amount calculation methods, the maturity date, or the notional amount of the uncleared swap. Thus, for example, if the day count convention of an uncleared swap changes as a consequence of transferring the ownership of an uncleared interest rate swap several time zones away from the UK, the parties to the swap would not be changing the payment amount calculation methods. On the other hand, a change to one of the payment amount calculation economic factors (e.g., an interest rate margin or base rate) would be a change outside the scope of a Margin Covered Amendment.

After considering the request and the related facts and circumstances, DCR also believes that a no-action position is appropriate to maintain the status quo for Clearing Legacy Swaps with respect to the Clearing Requirement to the extent any amendments are made solely to transfer ownership of such swaps in response to the Brexit Transition Period Expiration.

Accordingly, DCR will not recommend that the Commission take an enforcement action against any person for failure to comply with the Clearing Requirement with respect to a Clearing Legacy Swap solely to the extent that such compliance would be required as a result of an amendment to the swap entered into under the following conditions (each a **“Clearing Covered Amendment”**):

- (1) Solely in connection with a party to a Clearing Legacy Swap’s planning for or response to the Brexit Transition Period Expiration, one or both parties to the swap transfers the swap to its affiliate, or a branch or other authorized form of establishment of the transferor, and the parties make no other transfers of the swap;
- (2) Each transferor represents to the transferee that the transfer was made solely in connection with the transferor’s planning for or response to the Brexit Transition Period Expiration;³³
- (3) The amendment does not modify any of the following: the payment amount calculation methods,³⁴ the maturity date, or the notional amount of the swap;
- (4) The amendment takes effect no earlier than the date of this letter; and
- (5) The amendment is entered into and takes effect no later than the date that is one year after the Brexit Transition Period Expiration Date.

The Divisions recognize that both a Margin Covered Amendment and Clearing Covered Amendment may be carried out using any of the methods typically employed for effecting uncleared swap transfers, including industry protocols, contractual amendments, or contractual tear-up and replacement. To the extent they would otherwise trigger margin or clearing requirements, judicially-supervised changes that result in an uncleared swap being booked at or held by a related establishment are similarly within the scope of a Margin Covered Amendment and Clearing Covered Amendment.

³³ Each representation requested in this letter is a collection of information under OMB 3038-0049. No person is required to respond to this request for information unless a valid OMB number is displayed.

³⁴ Like MPD, DCR does not believe the relief being provided should be expansively applied to encompass economic changes to a legacy swap. Accordingly, the relief is unavailable if the amendments to an uncleared swap modify the payment amount calculation methods, the maturity date, or the notional amount of the uncleared swap.

This letter, and the positions taken herein, represent the views of the Divisions only, and do not necessarily represent the position or view of the Commission or of any other office or division of the Commission. The relief provided in this letter does not excuse persons relying on it from compliance with any other applicable requirements contained in the CEA or in Commission regulations. Further, this letter, and the positions taken herein, are based upon the facts and circumstances presented to the Divisions. Any different, changed, or omitted material facts or circumstances might render the relief provided by this letter void.

As with all staff letters, the Divisions retain the authority to condition further, modify, suspend, terminate, or otherwise restrict the terms of relief provided herein, in their discretion.

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