

CFTC proposes amendments to margin segregation requirements for swap dealers and major swap participants

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Introduction

On 24 July 2018 the Commodity Futures Trading Commission (CFTC) proposed amendments to certain requirements for swap dealers and major swap participants to notify counterparties of their right to segregate initial margin for uncleared swaps.⁽¹⁾ The proposal addresses several concerns previously raised by market participants about the existing rules, including through the CFTC's Project KISS initiative,⁽²⁾ which was intended to lift unnecessary regulatory burdens and reduce costs for market participants (for further information please see "[US derivatives regulation: a pause in 2017, and a look ahead to 2018](#)").

CFTC Rules 23.700-704 mandate that a swap dealer or major swap participant must notify a counterparty that it has the right to segregate initial margin in an account held by a third-party custodian that is separate from the swap dealer's or major swap participant's assets, on specified terms set out in the rules (the terms of this right to segregate apply only to transactions that are not subject to mandatory initial margin under the CFTC's rules; where initial margin is required, separate CFTC rules specify the manner in which such margin is to be held and segregated).⁽³⁾ Many market participants have long claimed that, among other things, these requirements:

- are overly burdensome;
- do not accommodate bilateral negotiation over segregation arrangements; and
- have discouraged the use of this segregation option.

Proposal

To address these concerns, the proposal would amend the rules to require that a swap dealer or major swap participant notify a counterparty of its ability to segregate initial margin prior to the first uncleared swap transaction that calls for the exchange of margin, rather than prior to each transaction or annually, as currently mandated. The proposal also eliminates the requirement that swap dealers and major swap participants obtain a counterparty's confirmation of receipt of the segregation notice, as the lack of a response may inhibit trading in some circumstances. Further, the proposal eliminates requirements for swap dealers and major swap participants to identify one or more creditworthy, independent custodians when notifying counterparties of their ability to segregate margin and to provide the required notification to individuals at the counterparty with specific job titles.

The proposal also:

- provides greater flexibility in terms of the withdrawal and turnover of control of initial margin;

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- allows swap dealers and major swap participants to negotiate terms of investment for segregated initial margin with counterparties bilaterally; and
- provides flexibility in respect of reporting requirements for swap dealers and major swap participants to counterparties that do not elect to segregate initial margin.

Although the CFTC voted unanimously to issue the proposal, Commissioner Rostin Behnam outlined some of his concerns with the proposal in a concurring statement.⁽⁴⁾ Behnam said that he would have preferred the CFTC to have sought additional input on how the restrictions on investment of segregated margin have affected end users before proposing to roll them back. He also discussed whether it may be more appropriate for the CFTC to provide more or clearer notification of a counterparty's right to segregation of initial margin rather than reducing the frequency with which a swap dealer or major swap participant must notify its counterparty of this right, as proposed.

All comments on the proposal must be received on or before 28 September 2018.

Comment

The proposal reflects market participants' concerns about a requirement that has long been regarded by many as burdensome and that has generally not provided a workable path to segregation for market participants that want this option. It remains to be seen what effect Behnam's concerns, along with comments from market participants, will have on any final rule.

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Endnotes

(1) [Segregation of Assets Held as Collateral in Uncleared Swap Transactions](#), 83 Fed Reg 146 (30 July 2018).

(2) [Project KISS](#), 82 Fed Reg 99 (24 May 2017).

(3) 17 CFR 23.700-23.704.

(4) Rostin Behnam, Commissioner, CFTC, [Statement of Concurrence of CFTC Commissioner Rostin Behnam Regarding Segregation of Assets Held as Collateral in Uncleared Swap Transactions; Amendments](#) (24 July 2018).

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