

# Prudential Regulators and CFTC: Final Margin Rules for Uncleared Swaps

March 2016

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The Prudential Regulators and the CFTC release final initial and variation margin rules for uncleared swaps and security-based swaps.

On October 22, 2015, the Prudential Regulators<sup>1</sup> released final rules and accompanying interpretive guidance setting out the Prudential Regulators' initial and variation margin requirements applicable to uncleared swaps and security-based swaps (the "**PR Final Margin Rules**").<sup>2</sup>

On December 16, 2015, the Commodity Futures Trading Commission (the "**CFTC**") released final rules and accompanying interpretive guidance setting out the CFTC's initial and variation margin requirements applicable to uncleared swaps ("**CFTC Final Margin Rules**").<sup>3</sup>

Due to the significant harmonization undertaken by the Prudential Regulators and the CFTC, this Client Alert outlines the important concepts and consequences of both the CFTC Final Margin Rules and the PR Final Margin Rules. References to "**Final Margin Rules**" indicate that the concept being discussed is applicable to both the CFTC Final Margin Rules and the PR Final Margin Rules. Material differences have been highlighted, as applicable.

## 1. Background

One of the key regulatory reforms contained in the Dodd-Frank Wall Street Reform and Consumer Protection Act was to require each registered Swap Dealer ("**SD**"), Security-Based Swap Dealer ("**SBSD**"), Major Swap Participant ("**MSP**") and Major Security-Based Swap Participant ("**MSBSP**") that enters into swap and security-based swap transactions that are not cleared to exchange both initial margin ("**IM**") and

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\* This Client Alert was updated on August 8, 2016 to include references to our client alert on the CFTC's final cross-border uncleared swap margin rules released on May 24, 2016, as well as certain other conforming changes.

<sup>1</sup> The five Prudential Regulators are the Federal Deposit Insurance Corporation, the Department of the Treasury (the Office of the Comptroller of the Currency), the Board of Governors of the Federal Reserve System, the Farm Credit Administration and the Federal Housing Finance Agency.

<sup>2</sup> The text of the final rule is set out in Margin and Capital Requirements for Covered Swap Entities, 80 FR 74839 (November 30, 2015), available at <https://federalregister.gov/a/2015-28671>; the text of the interim final rule is set out in Margin and Capital Requirements for Covered Swap Entities, 80 FR 74915 (November 30, 2015), available at <https://federalregister.gov/a/2015-28670>. The Prudential Regulators have requested comments on all aspects of the interim final rule. The prior proposed rule releases of the Prudential Regulators are as follows: Margin and Capital Requirements for Covered Swap Entities; Proposed Rule, 76 FR 27563 (May 11, 2011) and Margin and Capital Requirements for Covered Swap Entities; Proposed Rule, 79 FR 57347 (September 24, 2014)).

<sup>3</sup> Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 81 FR 635 (January 6, 2016), available at <https://federalregister.gov/a/2015-32320>. The prior proposed rule releases of the CFTC are as follows: Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 76 FR 23732 (April 28, 2011) and Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 79 FR 59897 (October 3, 2014).

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variation margin (“VM”) with its counterparties to those uncleared swaps and security-based swaps with the aim of protecting such entities from the risks arising from such transactions and to also generally cushion the US financial system at times of systemic stress.

## 2. Covered Swap Entities

The PR Final Margin Rules apply to a registered SD, MSP, SBSB and MSBSP that is regulated by a Prudential Regulator. SDs and MSPs that are not regulated by a Prudential Regulator will be subject to the CFTC Final Margin Rules, whilst SBSBs and MSBSPs that are not regulated by a Prudential Regulator will be subject to the initial and variation margin requirements of the Securities and Exchange Commission (“SEC”).

The PR Final Margin Rules refer to a registered SD, MSP, SBSB or MSBSP that is regulated by a Prudential Regulator and therefore subject to the PR Final Margin Rules as a “covered swap entity” or “CSE”. Similarly, the CFTC Final Margin Rules refer to a registered SD or MSP that is not regulated by a Prudential Regulator and therefore subject to the CFTC Final Margin Rules as a “covered swap entity” or “CSE”. The SEC is expected to adopt its own initial and variation margin rules applicable to SBSBs and MSBSPs.

For the purposes of this Client Alert:

- references to a “CSE” shall refer to both a CSE under the PR Final Margin Rules and a CSE under the CFTC Final Margin Rules, unless otherwise indicated; and
- references to a “Swap Entity” shall refer to, with respect to the PR Final Margin Rules, a registered SD, MSP, SBSB and MSBSP (irrespective of whether they are regulated by a Prudential Regulator, the CFTC or the SEC) and, with respect to the CFTC Final Margin Rules, a registered SD and MSP.

## 3. Covered Swaps

The PR Final Margin Rules apply to swaps and security-based swaps that are not cleared with a derivatives clearing organization registered with the CFTC (or exempted from such registration) or a clearing agency registered with the SEC (or exempted from such registration). The CFTC Final Margin Rules apply to swaps (not security-based swaps) that are not cleared with a derivatives clearing organization registered with the CFTC (or exempted from such registration).

The Final Margin Rules do not apply to:

- swaps or security-based swaps that are cleared by clearing organizations that have received an exemption by order or rule from registration with the CFTC or the SEC;
- foreign exchange swaps, foreign exchange forwards and the portion of a cross-currency swap that is the fixed physically settled exchange of principal.<sup>4</sup> Although such swaps are not subject to the initial and variation margin requirements of the Final Margin Rules, they are still relevant in determining whether a Financial End User has a Material Swaps Exposure (see the section entitled “Material Swaps Exposure” below) and the applicable compliance date for the Final Margin Rules (see the section entitled “Implementation” below);
- any swap or security-based swap where the CSE’s counterparty is a TRIPRA Excluded Entity (see the section entitled “TRIPRA Excluded Entities” below).

For the purposes of this Client Alert, swaps and security-based swaps that are subject to the Final Margin Rules are referred to as “Covered Swaps”.

## 4. Covered Counterparties

The nature of a CSE’s obligations under the Final Margin Rules will depend on which of the following categories its counterparties fall into:

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<sup>4</sup> Determination of Foreign Exchange Swaps and Foreign Exchange Forwards Under the Commodity Exchange Act, 77 FR 69694 (November 20, 2012), available at <https://federalregister.gov/a/2012-28319>.

- Swap Entities
- Financial End Users with a Material Swaps Exposure
- Financial End Users without a Material Swaps Exposure
- Affiliates of a CSE
- Other Counterparties

Each CSE is required to categorize each of its counterparties into one of these five groupings. In particular, we note that affiliates of CSEs have specific requirements and we have addressed these below as well.

## Financial End Users

The definition of Financial End User broadly captures entities that engage in financial activities that are subject to US Federal or State regulation, including deposit-taking and lending, securities and swaps dealing, investment advisory activities and asset management as well as certain non-bank lending and retail payment firms. It also includes commodity pools and other entities or arrangements that raise or accept money from investors or clients for investing or trading in loans, swaps, securities or other assets as well as any entity that would be a Swap Entity or Financial End User if it were organized in the US.

A summary of the entities contained in the definition of Financial End User is set out in the side-bar and a complete extract is set out in the Appendix. The definition of Financial End User is presented as an exhaustive list and is different and distinct from the definition of “financial entity” used in, for example, the end-user clearing exception.<sup>5</sup>

The following entities are specifically excluded from the definition of Financial End User and are thus treated as other counterparties (see the section entitled “Other Counterparties” below):

- the government of any country (but not a state of the US), including its agencies, departments and ministries;
- central banks;
- multilateral development bank;
- Bank for International Settlements;

Definition of “Financial End User”
<p>A Financial End User is any counterparty that is not, with respect to the PR Final Margin Rules, a registered SD, MSP, SBSD or MSBSP and, with respect to the CFTC Final Margin Rules, a registered SD or MSP, and that is (among others) any of the following:</p> <p>(a) Bank holding company, savings and loan holding company, certain US intermediate holding companies, certain non-bank financial institutions supervised by the Federal Reserve, depository institution, foreign bank, federal or state credit union; industrial loan company or bank, trust or fiduciary company, industrial loan company or industrial bank;</p> <p>(b) State licensed credit or lending entity or money services business;</p> <p>(c) Certain entities regulated by the Federal Housing Finance Agency or the Farm Credit Administration;</p> <p>(d) Securities holding company, broker or dealer, registered investment advisor, registered investment company, regulated business development company, private fund or certain exempt investment companies;</p> <p>(e) Commodity pool, commodity pool operator, commodity trading advisor, floor broker, floor trader, introducing broker or futures commission merchant;</p> <p>(f) Employee benefit plan;</p> <p>(g) Insurance company;</p> <p>(h) Certain entities that primarily engage in trading, investing or in facilitating the investing in loans, securities, swaps, funds or other assets;</p> <p>(i) any foreign entity that, if it were organized under the laws of the US or any State, would be a Financial End User;</p> <p>(j) [CFTC Final Margin Rules only] a registered SBSD or MSBSP.</p>

<sup>5</sup> The Prudential Regulators and the CFTC have modified the definition of Financial End User from that set out in their respective proposals to: (i) add certain US intermediate holding companies as well as floor brokers, floor traders, introducing brokers and, with respect to the CFTC Final Margin Rules only, registered SBSDs and MSBSPs; (ii) broaden the entities that primarily engage in trading, investing or in facilitating the investing in loans, securities, swaps, funds or other assets; and (iii) remove the proposed provision that would have permitted the Prudential Regulators and the CFTC to designate any other entity as a Financial End User (this provides greater certainty to the market participants, although the Prudential Regulators and the CFTC both noted that they may consider future rulemaking should they decide to amend the definition of Financial End User).

- certain captive finance companies and agent affiliates exempt from the mandatory clearing requirement;<sup>6</sup>
- an eligible treasury affiliate that the CFTC has exempted by rule from the clearing requirement (see also the section entitled “TRIPRA Excluded Entities” below).<sup>7</sup>

## Material Swaps Exposure

The burdens of the Final Margin Rules are greater for Financial End Users that have a “Material Swaps Exposure” than for those that do not. A CSE is only required to exchange IM with a Financial End User that has a “Material Swaps Exposure”.

A Financial End User will have a “Material Swaps Exposure” when it and its affiliates, together, have an average daily aggregate notional amount of uncleared swaps, security-security based swaps, foreign exchange forwards, and foreign exchange swaps that are not excluded under TRIPRA (see the section entitled “TRIPRA Excluded Entities” below) with all counterparties (including its affiliates,<sup>8</sup> but without double counting) for June, July and August of the previous calendar year that is more than US\$8 billion, where such amount is only calculated on business days (i.e., any day other than a Saturday, Sunday or legal holiday).<sup>9</sup> This represents a substantial increase from the originally proposed US\$3 billion and is consistent with the €8 billion set out in the BCBS-IOSCO framework.<sup>10</sup>

## Other Counterparties

### Application

The Final Margin Rules only apply to Covered Swaps entered into by a CSE with a Swap Entity or a Financial End User. Covered Swaps entered into by a CSE with any other counterparty (including a TRIPRA Excluded Entity) are not subject to the Final Margin Rules.<sup>11</sup>

The PR Final Margin Rules do require, however, that a CSE assess the credit risk posed by its counterparties when entering into Covered Swaps and, where the CSE determines appropriate, impose initial and/or variation margin to address the credit risk posed by the counterparty and the risks of such Covered Swaps. As the CFTC has removed the proposed documentation and hypothetical margin calculation requirements, the CFTC Final Margin Rules no longer contain any requirements with respect to Covered Swaps not subject to the CFTC Final Margin Rules.

<sup>6</sup> A captive finance company refers to an entity that is excluded from the definition of financial entity under section 2(h)(7)(c)(iii) of the CEA for purposes of the requirements to submit certain swaps for clearing. An agent affiliate refers to an entity that is an affiliate of a person that qualifies for an exception from the requirement to submit certain trades for clearing under section 2(h)(7)(D) of the CEA.

<sup>7</sup> Whilst the PR Final Margin Rules do not include this specific exclusion, the Prudential Regulators indicated that to the extent the CFTC acts to exempt eligible treasury affiliates from clearing by rule, then such entities would also be excluded from the definition of Financial End User under the PR Final Margin Rules. As of the date of this Client Alert, the CFTC had yet to release such a rule, but we note that, following the recent amendments to the Commodity Exchange Act and the Securities Exchange Act (as discussed in the section entitled “TRIPRA Excluded Entities” below), eligible treasury affiliates are now exempt from the clearing and margin requirements. It is therefore expected that the CFTC will issue rules with respect to this exemption.

<sup>8</sup> Whether an entity is an “affiliate” is determined by reference to accounting consolidation principles.

<sup>9</sup> Swaps and security-based swaps that are excluded from the application of the Final Margin Rules pursuant TRIPRA are not included in the Material Swaps Exposure calculation (see the section entitled “TRIPRA Excluded Entities” below).

<sup>10</sup> Basel Committee on Banking Supervision (“**BCBS**”) and Board of the International Organization of Securities Commissions (“**IOSCO**”), Margin requirements for non-centrally cleared derivatives (March 2015), available at <http://www.bis.org/bcbs/publ/d317.htm>.

<sup>11</sup> Entities that do not fall within the categories of Swap Entity, Financial End User with a Material Swaps Exposure (with respect to the IM requirements) and Financial End User (with respect to the VM requirements) are referred to as “non-financial end users” in the CFTC Final Margin Rules and “other counterparties” in the PR Final Margin Rules. As swaps and security-based swaps entered into with a TRIPRA Excluded Entity are completely excluded from the CFTC Final Margin Rules and the PR Final Margin Rules, TRIPRA Excluded Entities are not subject to the classification system set out in these rules.

## TRIPRA Excluded Entities

On January 12, 2015, President Obama signed into law the Terrorism Risk Insurance Program Reauthorization Act of 2015 (“**TRIPRA**”),<sup>12</sup> which amended both the Commodity Exchange Act (which governs the regulation of swaps by the CFTC) and the Securities Exchange Act (which governs the regulation of security-based swaps by the SEC) to completely exclude certain swaps and security-based swaps entered into by a CSE with specified counterparties from the Final Margin Rules. The purpose of TRIPRA was to provide for additional exclusions similar to those provided to cleared transactions for certain commercial end users that enter into swaps and security-based swaps that are not subject to mandatory clearing but would otherwise have been subject to compliance with the Final Margin Rules.

Unfortunately, TRIPRA did not address all types of commercial end users that benefit from the clearing exception as transactions between a CSE and an affiliate were not included in TRIPRA whilst such transactions are generally exempt from the clearing requirement. The Final Margin Rules do, however, include special rules that provide a limited set of exemptions for certain affiliates (see the section entitled “Affiliates of a CSE” below).

As required by TRIPRA, both the Prudential Regulators and the CFTC issued interim final rules which collectively result in swaps and security-based swaps entered into with the following counterparties being completely excluded from the Final Margin Rules:

- a non-financial entity (including a small financial institution and a captive finance company) that qualifies for an exception from the clearing requirement pursuant to section 2(h)(7)(A) of the Commodity Exchange Act in conjunction with CFTC Rule 50.50 or section 3C(g)(1) of the Securities Exchange Act;
- a cooperative entity that qualifies for an exemption from the clearing requirement pursuant to CFTC Rule 50.51; or
- a treasury affiliate of a non-financial entity within the same corporate group that is itself entitled to elect the exception from the clearing requirements pursuant to section 2(h)(7)(D) of the Commodity Exchange Act or section 3C(g)(4) of the Securities Exchange Act.<sup>13</sup>

For the purposes of this Client Alert, each of the excepted counterparties set out above shall be referred to as a “**TRIPRA Excluded Entity**”.

### Affiliates of a CSE

Both the PR Final Margin Rules and the CFTC Final Margin Rules include their own special rules that provide full or partial relief for certain affiliate transactions from the requirement to post and collect IM. However, as the special rules do not apply to VM, VM will need to be posted and collected with all affiliate counterparties in accordance with both the PR Final Margin Rules and the CFTC Final Margin Rules.

The table in the side-bar provides a broad summary of the affiliate special rules, which are more fully explained below.

Application of the Final Margin Rules to Affiliate Transactions		PR Final Margin Rules	CFTC Final Margin Rules
IM	Post	No	No, except if collection is required by the PR Final Margin Rules
	Collect	Yes, subject to a threshold	No, except in certain circumstances and provided certain requirements are met
VM	Post	Yes	Yes
	Collect	Yes	Yes

<sup>12</sup> Pub. L. 114-1, 129 Stat. 3 (2015).

<sup>13</sup> The Consolidated Appropriations Act of 2016 (Pub. L. 114-113 (2016)) amended section 2(h)(7)(D) of the Commodity Exchange Act and section 3C(g)(4) of the Securities Exchange Act to exempt certain treasury affiliates of commercial end users from the margin and clearing requirements. Prior to the enactment of these amendments, treasury affiliates were reliant on CFTC No-Action Letter 14-144 for exemption from the margin and clearing requirements. The requirements set out in these amendments are very similar to the no-action relief requirements in CFTC No-Action Letter 14-144. Treasury affiliates are also excluded from the definition of Financial End User (see above).

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## PR Final Margin Rules

With respect to the IM requirements under the PR Final Margin Rules:

- A CSE is not required to post IM with respect to any Covered Swap entered into with an affiliate counterparty, although the CSE will be required to calculate the amount of IM it would have had to post to an affiliate counterparty that is a Financial End User with a Material Swaps Exposure and provide documentation of such amount to that counterparty on a daily basis.
- Whilst a CSE is still required to collect IM from affiliate counterparties, this is subject to a threshold amount in an aggregate credit exposure of US\$20 million per affiliate counterparty (i.e., it is not on a consolidated basis).
- Should a CSE collect IM in the form of non-cash collateral<sup>14</sup> from an affiliate counterparty, the custodian for such collateral need not be a third party, as is required for non-affiliate transactions. Instead, the custodian may be the CSE itself or one of its affiliates. The custody requirements are discussed in the section entitled “Segregation of Collateral” below.
- Where an affiliate counterparty is a treasury affiliate that is excluded from the clearing requirement (see the section entitled “TRIPRA Excluded Entities” above), certain adjustments are made to the calculation and netting of IM where the CSE is utilizing a model. The model approach of calculating IM is discussed in the section entitled “Initial Margin Requirements” below.

## CFTC Final Margin Rules

A CSE is not required to collect IM from an affiliate counterparty where:

- the Covered Swaps are subject to a centralized risk management program that is reasonably designed to monitor and to manage the risks associated with the Covered Swaps; and
- the CSE exchanges VM with the affiliate counterparty in accordance with the CFTC Final Margin Rules.

However, each CSE must still collect IM from each of its non-US affiliate counterparties that satisfy all of the following requirements: (i) are a Financial End User, (ii) directly or indirectly enter into swaps with third parties that would be subject to the CFTC Final Margin Rules if the affiliate were a SD or MSP, and (iii) are located in a jurisdiction that is not eligible for substituted compliance and do not collect IM for such swaps in a manner that would comply with the CFTC Final Margin Rules. If the exemption does not apply, then the custodian for any IM collected need not be a third party, as is required for non-affiliate transactions, and may instead be the CSE itself or one of its affiliates. The custody requirements are discussed in the section entitled “Segregation of Collateral” below.

A CSE is not required to post IM to an affiliate counterparty, except where the CSE enters into a Covered Swap with an affiliate counterparty that is a Swap Entity subject to the PR Final Margin Rules; the PR Final Margin Rules do not provide an affiliate exemption to the IM collection requirement above the threshold (see above). In these circumstances, the CSE will be required to post IM with that counterparty in an amount equal to the amount that the counterparty is required to collect under the PR Final Margin Rules.

## Change in Status

Should a CSE’s counterparty change its status, then the following rules apply:

- if the change results in the imposition of stricter margin requirements, then those requirements shall apply to the CSE with respect to the Covered Swaps entered into with the applicable counterparty after that change in status;
- if the change results in the imposition of less stringent margin requirements, then the CSE may (but is not required to) comply with those less strict requirements with respect to (i) swaps or security-based swaps that are entered into with the applicable counterparty after that change in status and (ii) any outstanding swaps and security-based swaps entered into after the applicable compliance date (see the section entitled “Implementation,” below) and before the counterparty changed its status.

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<sup>14</sup> The affiliate special rules set out in the CFTC Final Margin Rules, in comparison, permit the CSE or one of its affiliates to hold IM collected in the form of both cash and non-cash collateral.

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## 5. Initial Margin Requirements

The Prudential Regulators and the CFTC have both adopted a collect and post approach which will require each CSE to:

- collect IM from each counterparty that is a Swap Entity and Financial End User with a Material Swaps Exposure; and
- post IM to each counterparty that is a Financial End User with a Material Swaps Exposure,

in each case, commencing on or before the end of the business day following the day of execution of the particular Covered Swap (which is adjusted to accommodate circumstances where the counterparties to a particular Covered Swap do not observe the same business day) and thereafter collect and post on a daily basis until the Covered Swap is terminated or expires.

The Prudential Regulators and the CFTC both recognized that, in order to meet this timing requirement, parties may need to pre-position assets at the custodian and/or use cash (rather than less readily-transferrable assets) and that, in addition, portfolio reconciliation and dispute resolution will need to occur after IM has been collected, as adjustments to the initial margin call, rather than before.

### Calculation of Initial Margin

A CSE is required to calculate IM for a Covered Swap using either a model-based approach or a standardized table-based approach. The Prudential Regulators and the CFTC have both warned that the choice to use one approach over the other must be based on fundamental considerations and not what produces the most favorable margin results, and that the Prudential Regulators and the CFTC will expect CSEs to provide them with a rationale for changing methodologies.

The required amount of IM would be the amount calculated pursuant to the applicable approach minus a threshold amount of up to US\$50 million (which is applied with respect to all Covered Swaps across the CSE's consolidated group, not individually to each entity). This IM amount would be a minimum requirement and the parties may negotiate a higher amount.

### Model-Based Approach

A model needs to satisfy, among others, the following requirements:

- One-tailed 99% confidence level over ten (10) day horizon;
- ten (10) day minimum close-out period;
- Calibrated to a period of financial stress;
- Daily calculation of IM;
- Benchmarking against observable margin standards that a clearing house would require for similar transactions.

The Final Margin Rules permit a CSE to use a model that reflects offsetting exposures, diversification and other hedging benefits for Covered Swaps that are covered by a single eligible master netting agreement within, but not across, four broad risk categories – commodities, credit, equity, and foreign exchange and interest rate (considered together as a single asset class).

CSEs regulated by a Prudential Regulator would be required to obtain the written approval of the applicable Prudential Regulator and CSEs regulated by the CFTC would be required to obtain the prior written approval of the CFTC or the US National Futures Association before using a model to calculate IM. A Prudential Regulator and the CFTC has the right to rescind its approval for a model if it determines that the model no longer complies with the requirements.

## Table-Based Approach

The table-based approach allows a CSE to calculate its IM requirements using a standardized table (set out in the sidebar). The table specifies the minimum IM amount that must be collected as a percentage of a Covered Swap's notional amount. This percentage varies depending on the asset class and, in some instances, the duration of the asset. Except as described below, a CSE would be required to calculate a minimum IM amount for each Covered Swap and aggregate all the minimum IM amounts to determine the total amount of IM.

CSEs are permitted to calculate IM using a net-to-gross ratio adjustment in order to take into account risk offsets where a portfolio of Covered Swaps is covered by a single eligible master netting agreement. Unlike under a model, the calculation is performed across transactions in disparate asset classes. The net-to-gross ratio compares the net current replacement cost of the entire portfolio of Covered Swaps that is covered under an eligible master netting agreement with the gross current replacement cost of those Covered Swaps.

Asset Class	Gross Initial Margin (% of notional exposure)
Credit (0–2, 2–5, 5+ year duration)	2%, 5%, 10%
Commodity	15%
Equity	15%
Foreign Exchange / Currency	6%
Cross-Currency Swap (0–2, 2–5, 5+ year duration)	1%, 2%, 4%
Interest Rate (0–2, 2–5, 5+ year duration)	1%, 2%, 4%
Other	15%

## 6. Variation Margin Requirements

Each CSE must collect VM from, and post VM to, each counterparty that is a Swap Entity or a Financial End User (irrespective of whether the counterparty has a Material Swaps Exposure), commencing on or before the end of the business day following the day of execution for each Covered Swap with that counterparty (which is adjusted to accommodate circumstances where the counterparties to a particular Covered Swap do not observe the same business day) and thereafter collect and post not less than daily until the termination or expiry of the Covered Swap. The amount of VM to be posted or collected with respect to a Covered Swap is the amount equal to:

- the cumulative mark-to-market change in value to a Covered Swap as determined pursuant to the applicable documentation (i.e., mid-market prices, if consistent with the agreement of the parties); *less*
- the value of all VM previously collected; *plus*
- the value of all VM previously posted.

The CSE must collect this amount if it is positive, and post this amount if it is negative.

The CFTC provided additional guidance regarding the calculation of IM under its rules. It stated that VM calculations use methods, procedures, rules and inputs that, to the maximum extent practicable, rely on recently-executed transactions, valuations provided by independent third parties, or other objective criteria. The Prudential Regulators did not provide any additional guidance.

## 7. Netting Arrangements

Where more than one Covered Swap is executed pursuant to an eligible master netting agreement (for example, a 1992 or 2002 ISDA Master Agreement), the CSE would be permitted to calculate IM and VM on an aggregate basis with respect to all Covered Swaps governed by such agreement.

A CSE is entitled to maintain multiple netting portfolios under a single eligible master netting agreement (for example, through the use of multiple credit support annexes). This facilitates the ability of parties to document two separate netting sets—one for Covered Swaps and another for swaps and security-based swaps that are not subject to the Final Margin Rules.<sup>15</sup>

<sup>15</sup> This represents a change from the proposals which did not permit the use of separate netting sets, with the consequence of applying the initial and variation margin requirements to swaps and security-based swaps entered into before the applicable compliance date.



## 8. Minimum Transfer Amount

A CSE would only be required to collect or post IM or VM when the combined amount of both IM and VM required to be collected or posted exceeds US\$500,000. This only affects the timing of margin transfers, not the amount—that is, once the threshold is crossed, the full amount of IM and VM is required to be transferred.

## 9. Satisfaction of Collection and Posting Requirements

A CSE would not be deemed to have violated its obligation to collect IM or VM where its counterparty fails or refuses to transfer the required IM or VM, provided the CSE makes the necessary efforts to attempt to collect the IM or VM, including the timely initiation and continued pursuit of formal dispute resolution mechanisms, or otherwise demonstrated upon request to the satisfaction of the applicable Prudential Regulator or the CFTC that it has made appropriate efforts to collect the required IM or VM or commenced termination of the relevant Covered Swap.

## 10. Collateral

### Eligibility

The below table sets out the types of eligible collateral that may qualify for IM and VM. The Final Margin Rules provide that the types of collateral that are eligible for VM will depend on the type of counterparty, whilst eligible collateral for IM applies across all counterparty types. A CSE that enters into a Covered Swap with a Financial End User is permitted to use the same list of eligible collateral to satisfy the IM and VM requirements. However, whilst a CSE that enters into a Covered Swap with a Swap Entity can utilize the same list of eligible collateral to satisfy the IM requirements, it may only use cash to satisfy the VM requirements.

Asset Class	Initial Margin	Variation Margin	
	All Counterparties	Swap Entities	Financial End Users
US dollars	✓	✓	✓
A currency in which the payment obligations under the Covered Swap are required to be settled	✓	✓	✓
Other major currencies: Canadian Dollar, Euro, United Kingdom Pound, Japanese Yen, Swiss Franc, New Zealand Dollar, Australian Dollar, Swedish Kroner, Danish Kroner, Norwegian Krone and any other currency designated by the Prudential Regulators or the CFTC	✓	✓	✓
US Treasury securities	✓	x	✓
Certain securities guaranteed by the US government	✓	x	✓
Certain redeemable securities in a pooled investment fund	✓	x	✓
Certain securities issued or guaranteed by the European Central Bank, a sovereign entity, the Bank for International Settlements, the International Monetary Fund or a multilateral development bank.	✓	x	✓
Certain corporate debt securities	✓	x	✓
Certain equity securities maintained in major indices	✓	x	✓
Gold	✓	x	✓

The following assets are excluded as eligible collateral for both IM and VM:

- securities issued by a party (or any affiliate of that party) posting that security;
- securities issued by bank holding companies, depository institutions and market intermediaries; and
- securities issued by certain systemically important non-bank financial institutions.

## Haircuts

All non-cash eligible collateral is subject to a haircut (or discount) that varies by the type of asset and, in some instances, the length of its maturity (see the table in the side-bar).

The Final Margin Rules also require that a cross-currency haircut of 8% is applied (in addition to any other asset-specific haircut that might apply) whenever eligible collateral (including cash) posted as either IM or VM is denominated in a currency other than the currency in which regularly occurring payment obligations related to a Covered Swap are to be discharged under the applicable agreement. However, this additional cross-currency haircut does not apply to:

- non-cash collateral posted as IM that is denominated in a single termination currency designated as payable to the non-posting party under an eligible master netting agreement (or a netting portfolio within that agreement); and
- immediately available cash funds in US dollars or another major currency (see above) posted as VM.

## 11. Segregation of Collateral

Any IM that is:

- posted by a CSE subject to the CFTC Final Margin Rules to satisfy its IM obligations under those rules;
- posted by a CSE subject to the PR Final Margin Rules to satisfy any margin obligations (other than variation margin), irrespective whether required under the PR Final Margin Rules or otherwise (e.g. a bilateral agreement); or
- collected by any CSE pursuant to the IM requirements of the PR Final Margin Rules or the CFTC Final Margin Rules,

must be held by one or more custodians that are not the CSE, the counterparty, or any of their affiliates. However, with respect to certain affiliate transactions, the custodian for all IM collected pursuant to the CFTC Final Margin Rules and IM collected in the form of non-cash collateral pursuant to the PR Final Margin Rules need not be a third party, as is required for non-affiliate transactions, and may instead be the CSE itself or one of its affiliates (see the section entitled “Affiliates of a CSE” above).

Each CSE must enter into custodial agreements with each custodian that:

- prohibits the custodian from rehypothecating, repledging, reusing or otherwise transferring the custodied assets;
- limits the rights of substitution and reinvestment to funds or other property that are eligible collateral; and
- is legal, valid, binding and enforceable under the laws of all relevant jurisdictions including in the event of bankruptcy, insolvency or a similar proceeding.

Asset Class	Haircut
Cash	0%
Eligible government and related debt	Residual maturity: <ul style="list-style-type: none"> <li>• less than one year: 0.5%</li> <li>• between one and five years: 2%</li> <li>• greater than five years: 4%</li> </ul>
Eligible corporate and US government sponsored entity debt securities	Residual maturity: <ul style="list-style-type: none"> <li>• less than one year: 1%</li> <li>• between one and five years: 4%</li> <li>• greater than five years: 8%</li> </ul>
Equities included in S&P 500 or related index	15%
Equities included in S&P 1500 Composite or related index but not included in S&P 500 or related index	25%
Gold	15%
Additional (additive) cross-currency haircut	8%

These segregation requirements do not apply to any collateral collected or posted as VM.

Under the PR Final Margin Rules, a CSE would also not be required to post collateral as IM with respect to a Covered Swap where that CSE is a foreign branch of a US depository institution or a foreign subsidiary of a US depository institution, Edge corporation or agreement corporation where certain additional requirements are satisfied, including:

- that it is legally or operationally impractical to post any form of IM in compliance with the segregation requirements;
- the CSE is only permitted to transact with its counterparty through an establishment in the foreign jurisdiction and the foreign jurisdiction does not allow for the posting of initial margin in compliance with the third party custodian requirements outside the foreign jurisdiction;
- its counterparty is not guaranteed by a US entity or a branch or office of a US entity;
- the CSE collects IM and collects and posts VM in the form of cash collateral; and
- the applicable Prudential Regulator gives its written approval.

The Prudential Regulators noted that a CSE would need to demonstrate that foreign regulatory restrictions would not allow the Covered Swap to occur in another jurisdiction that would accommodate the posting and segregation of collateral. For information on the equivalent rule applicable to CSEs subject to the CFTC Final Margin Rules, please see our client alert available [here](#).

## 12. Documentation Requirements

A CSE and a counterparty that is a Swap Entity or Financial End User must enter into documentation that provides the CSE with a contractual right and obligation to exchange IM and VM in such amounts, in such form, and under such circumstances as are required by the Final Margin Rules. The documentation must include the methodology and data sources to be used to value positions and to calculate IM and VM, and the valuation dispute resolution procedures.

## 13. Cross-Border Application

### PR Final Margin Rules

#### Exclusion

The PR Final Margin Rules exclude any “foreign non-cleared swap or foreign non-cleared security-based swap” of a “foreign covered swap entity” from the rule’s margin requirements. These terms are defined in the side-bar.

That is, only a CSE that is organized under foreign law and is not a subsidiary of a US company would be a “foreign covered swap entity.” Neither a foreign branch of a US bank or a foreign subsidiary of a US company would be a “foreign covered swap entity,” although they may be eligible to take advantage of a substituted compliance determination of the Prudential Regulators (see below).

The Prudential Regulators noted that they would generally consider the entity to which the Covered Swap

Foreign Covered Swap Entity
<p>A “foreign covered swap entity” is any CSE that is not:</p> <ul style="list-style-type: none"> <li>(a) an entity organized under US or State law (<u>including</u> a US branch, agency, or subsidiary of a foreign bank;</li> <li>(b) a branch or office of any entity organized under US or State law; or</li> <li>(c) an entity that is a subsidiary of an entity organized under US or State law.</li> </ul>
Foreign Non-Cleared Swap and Foreign Non-Cleared Security-Based Swap
<p>A “foreign non-cleared swap” or “foreign non-cleared security-based swap” covers any swap or security-based swap to which neither the counterparty nor any guarantor (on either side) is:</p> <ul style="list-style-type: none"> <li>(a) an entity organized under US or State law (including a US branch, agency, or subsidiary of a foreign bank) or a natural person who is a resident of the United States;</li> <li>(b) a branch or office of an entity organized under US or State law; or</li> <li>(c) a SD, MSP, SBSD or MSBSP that is a subsidiary of an entity organized under US or State law.</li> </ul> <p>Guarantee is defined to mean an arrangement under which one party to a non-cleared swap or security-based swap has rights of recourse against a third party guarantor, with respect to its counterparty’s obligations under any such swap.</p>

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was booked as the counterparty. This is in contrast to the approach used in the Volcker Rule, CFTC Staff Advisory 13-69,<sup>16</sup> the SEC in its final rules on the application of certain of the security-based swap rules to cross-border transactions,<sup>17</sup> and the CFTC in its proposed rule regarding the application of its initial and variation margin requirements to cross-border transactions,<sup>18</sup> where the methodology used (or proposed) to determine whether a swap was executed by a branch of a non-US person was whether any personnel who *arranged, negotiated or executed* the applicable swap were located in that branch.

### Full Substituted Compliance (Non-US CSE)

A CSE that does not have its obligations guaranteed by an entity organized under the laws of the US or any State (other than a US branch or agency of a foreign bank) or by a natural person who is a US resident and that is:

- a foreign covered swap entity;
- a US branch or agency of a foreign bank; or
- an entity that is not organized under the laws of the US or any State and is a subsidiary of a depository institution, Edge corporation or agreement corporation,

is eligible to satisfy the requirements of the PR Final Margin Rules through substituted compliance with a non-US regulatory framework for Covered Swaps where the Prudential Regulators have made a substituted compliance determination.

Unlike with the exclusion from the PR Final Margin Rules (see above):

- a CSE is permitted to be guaranteed by a US branch or agency of a foreign bank;
- A US branch or agency of a foreign bank may be eligible for compliance with a foreign margin regime provided a substituted compliance determination has been made and all other conditions have been satisfied.

### Partial Substituted Compliance (US CSE)

A CSE that is not itself eligible for the exclusion or full substituted compliance (see above) because it does not satisfy the applicable foreign eligibility requirements will nonetheless be entitled to satisfy its IM posting requirement under the PR Final Margin Rules by posting to its foreign counterparty IM in the form and amount, and at such times, that its foreign counterparty is required to collect pursuant to a foreign regulatory framework where:

- the Prudential Regulators have made a substituted compliance determination with respect to the applicable foreign regulatory framework;
- the foreign counterparty is subject to the foreign regulatory framework; and
- the obligations of the foreign counterparty with respect to the Covered Swap are not guaranteed by (i) an entity organized under the laws of the United States or any State (including a US branch, agency or subsidiary of a foreign bank) or a natural person who is a resident of the United States; or (ii) a branch or office of an entity organized under the laws of the United States or any State.

As this would only apply to the IM posting requirement of the CSE, the CSE will still be subject to the VM collection and posting requirements and the IM collection requirements of the PR Final Margin Rules.

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<sup>16</sup> For further information on CFTC Staff Advisory 13-69 please refer to our client alert available [here](#).

<sup>17</sup> Security-Based Swap Transactions Connected With a Non-US Person's Dealing Activity That Are Arranged, Negotiated, or Executed by Personnel Located in a US Branch or Office or in a US Branch or Office of an Agent; Security-Based Swap Dealer De Minimis Exception; Final Rule, 81 FR 8597 (February 19, 2016), available at <https://federalregister.gov/a/2016-03178>.

<sup>18</sup> Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants-Cross-Border Application of the Margin Requirements; Proposed Rule (July 14, 2015), 80 FR 41375, available at <https://federalregister.gov/a/2015-16718>. For further information on the CFTC's proposed cross-border rule please refer to our client alert available [here](#).

## Substituted Compliance Determinations

The Prudential Regulators, using an outcomes-based approach, will make substituted compliance determinations on a jurisdiction-by-jurisdiction basis, either conditionally or unconditionally. The Prudential Regulators will take into account such factors as scope, objective, specific provisions of the foreign regulatory framework and its supervisory effectiveness.

## Non-Netting Jurisdictions

If a CSE cannot conclude after sufficient legal review, on a well-founded basis, that a netting agreement with a counterparty in a foreign jurisdiction meets the definition of “eligible master netting agreement” (see the section entitled “Netting Arrangement” above), then the CSE is permitted to calculate initial and variation margin requirements on a net basis in determining the amount of margin that it is required to post, provided that certain conditions are satisfied. However, in determining the amount of initial and variation margin it is required to collect, it must make this determination on a gross basis (i.e. netting is not permitted).

## CFTC Final Margin Rules

For information on the final cross-border uncleared swap margin rules of the CFTC, please see our client alert available [here](#).

# 14. Implementation

## Initial Margin

The compliance date for IM requirements depends on the average daily aggregate notional amount of uncleared swaps, uncleared security-based swaps, foreign exchange forwards and foreign exchange swaps in March, April and May of a given year for both:

- the applicable CSE combined with all of its affiliates; and
- its counterparty combined with all of its affiliates.

In undertaking this calculation, a CSE only counts those instruments between itself and its counterparty once (i.e., there is no double-counting) and shall not count a swap or security-based swap that is exempt from the Final Margin Rules (see the section entitled “TRIPRA Excluded Entities” above). With respect to the CFTC Final Margin Rules only, a CSE shall also not count a security-based swap that is exempt pursuant to section 15F(e) of the Securities Exchange Act (15 U.S.C. 78o-10(e)).

The IM requirements are phased-in year by year from the largest CSEs to the smallest, as set out in the sidebar, which have been amended from the prior proposal to reflect the updated implementation schedule for the BCBS-IOSCO framework.<sup>19</sup> A CSE may well have multiple compliance dates as the triggers are dependent on both the CSE itself and its counterparties. Once a CSE and its counterparty are subject to the Final Margin Rules, they will both remain subject from that period forward.

Initial Margin Compliance Date	Average Notional Amount Triggers
September 1, 2016	If average daily aggregate notional amount of uncleared instruments > US\$3 Trillion in March, April and May of 2016
September 1, 2017	If average daily aggregate notional amount of uncleared instruments >US\$2.25 Trillion in March, April and May 2017
September 1, 2018	If average daily aggregate notional amount of uncleared instruments >US\$1.5 Trillion in March, April and May 2018
September 1, 2019	If average daily aggregate notional amount of uncleared instruments >US\$0.75 Trillion in March, April and May 2019
September 1, 2020	For any other CSE with respect to uncleared instruments entered into with any other counterparty

<sup>19</sup> See BCBS and IOSCO “Margin requirements for non-centrally cleared derivatives” (March 2015), available at <http://www.bis.org/bcbs/publ/d317.htm>.

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## Variation Margin

The compliance dates for VM have been altered from those originally proposed. The compliance date for the VM requirements is calculated in the same way as for the IM requirements (see above), except that the phase-in period is much shorter, as set out in the side-bar. As with the IM compliance dates, a CSE may well have multiple compliance dates as the triggers are dependent on both the CSE itself and its counterparties. Once a CSE and its counterparty are subject to the Final Margin Rules, they will both remain subject from that period forward.

Variation Margin Compliance Date	Average Notional Amount Triggers
September 1, 2016	If average daily aggregate notional amount of uncleared instruments >US\$3 Trillion in March, April and May 2016
March 1, 2017	For any other CSE with respect to uncleared instruments entered into with any other counterparty

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## Appendix

### Definition of Financial End User

#### PR Final Margin Rules

*Financial end user* means:

- (1) Any counterparty that is not a swap entity and that is:
  - (i) A bank holding company or an affiliate thereof; a savings and loan holding company; a US intermediate holding company established or designated for purposes of compliance with 12 CFR 252.153; or a nonbank financial institution supervised by the Board of Governors of the Federal Reserve System under Title I of the Dodd-Frank Wall Street Reform and Consumer Protection Act (12 U.S.C. 5323);
  - (ii) A depository institution; a foreign bank; a Federal credit union or State credit union as defined in section 2 of the Federal Credit Union Act (12 U.S.C. 1752(1) & (6)); an institution that functions solely in a trust or fiduciary capacity as described in section 2(c)(2)(D) of the Bank Holding Company Act (12 U.S.C. 1841(c)(2)(D)); an industrial loan company, an industrial bank, or other similar institution described in section 2(c)(2)(H) of the Bank Holding Company Act (12 U.S.C. 1841(c)(2)(H));
  - (iii) An entity that is state-licensed or registered as:
    - (A) A credit or lending entity, including a finance company; money lender; installment lender; consumer lender or lending company; mortgage lender, broker, or bank; motor vehicle title pledge lender; payday or deferred deposit lender; premium finance company; commercial finance or lending company; or commercial mortgage company; except entities registered or licensed solely on account of financing the entity's direct sales of goods or services to customers;
    - (B) A money services business, including a check casher; money transmitter; currency dealer or exchange; or money order or traveler's check issuer;
  - (iv) A regulated entity as defined in section 1303(20) of the Federal Housing Enterprises Financial Safety and Soundness Act of 1992, as amended (12 U.S.C. 4502(20)) or any entity for which the Federal Housing Finance Agency or its successor is the primary federal regulator;
  - (v) Any institution chartered in accordance with the Farm Credit Act of 1971, as amended, 12 U.S.C. 2001 *et seq.*, that is regulated by the Farm Credit Administration;
  - (vi) A securities holding company; a broker or dealer; an investment adviser as defined in section 202(a) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-2(a)); an investment company registered with the U.S. Securities and Exchange Commission under the Investment Company Act of 1940 (15 U.S.C. 80a-1 *et seq.*); or a company that has elected to be regulated as a business development company pursuant to section 54(a) of the Investment Company Act of 1940 (15 U.S.C. 80a-53(a));
  - (vii) A private fund as defined in section 202(a) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-2(a)); an entity that would be an investment company under section 3 of the Investment Company Act of 1940 (15 U.S.C. 80a-3) but for section 3(c)(5)(C); or an entity that is deemed not to be an investment company under section 3 of the Investment Company Act of 1940 pursuant to Investment Company Act Rule 3a-7 (17 CFR 270.3a-7) of the U.S. Securities and Exchange Commission;
  - (viii) A commodity pool, a commodity pool operator, or a commodity trading advisor as defined, respectively, in section 1a(10), 1a(11), and 1a(12) of the Commodity Exchange Act of 1936 (7 U.S.C. 1a(10), 1a(11), and 1a(12)); a floor broker, a floor trader, or introducing broker as defined, respectively, in 1a(22), 1a(23) and 1a(31) of the Commodity Exchange Act of 1936 (7 U.S.C. 1a(22), 1a(23), and 1a(31)); or a futures commission merchant as defined in 1a(28) of the Commodity Exchange Act of 1936 (7 U.S.C. 1a(28));

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- (ix) An employee benefit plan as defined in paragraphs (3) and (32) of section 3 of the Employee Retirement Income and Security Act of 1974 (29 U.S.C. 1002);
  - (x) An entity that is organized as an insurance company, primarily engaged in writing insurance or reinsuring risks underwritten by insurance companies, or is subject to supervision as such by a State insurance regulator or foreign insurance regulator;
  - (xi) An entity, person or arrangement that is, or holds itself out as being, an entity, person, or arrangement that raises money from investors, accepts money from clients, or uses its own money primarily for the purpose of investing or trading or facilitating the investing or trading in loans, securities, swaps, funds or other assets for resale or other disposition or otherwise trading in loans, securities, swaps, funds or other assets; or
  - (xii) An entity that would be a financial end user described in paragraph (1) of this definition or a swap entity, if it were organized under the laws of the United States or any State thereof.
- (2) The term “financial end user” does not include any counterparty that is:
- (i) A sovereign entity;
  - (ii) A multilateral development bank;
  - (iii) The Bank for International Settlements;
  - (iv) An entity that is exempt from the definition of financial entity pursuant to section 2(h)(7)(C)(iii) of the Commodity Exchange Act of 1936 (7 U.S.C. 2(h)(7)(C)(iii)) and implementing regulations; or
  - (v) An affiliate that qualifies for the exemption from clearing pursuant to section 2(h)(7)(D) of the Commodity Exchange Act of 1936 (7 U.S.C. 2(h)(7)(D)) or section 3C(g)(4) of the Securities Exchange Act of 1934 (15 U.S.C. 78c-3(g)(4)) and implementing regulations.

## **CFTC Final Margin Rules**

*Financial end user means—*

- (1) A counterparty that is not a swap entity and that is:
- (i) A bank holding company or a margin affiliate thereof; a savings and loan holding company; a US intermediate holding company established or designated for purposes of compliance with 12 CFR 252.153; or a nonbank financial institution supervised by the Board of Governors of the Federal Reserve System under Title I of the Dodd-Frank Wall Street Reform and Consumer Protection Act (12 U.S.C. 5323);
  - (ii) A depository institution; a foreign bank; a Federal credit union or State credit union as defined in section 2 of the Federal Credit Union Act (12 U.S.C. 1752(1) and (6)); an institution that functions solely in a trust or fiduciary capacity as described in section 2(c)(2)(D) of the Bank Holding Company Act (12 U.S.C. 1841(c)(2)(D)); an industrial loan company, an industrial bank, or other similar institution described in section 2(c)(2)(H) of the Bank Holding Company Act (12 U.S.C. 1841(c)(2)(H));
  - (iii) An entity that is state-licensed or registered as:
    - (A) A credit or lending entity, including a finance company; money lender; installment lender; consumer lender or lending company; mortgage lender, broker, or bank; motor vehicle title pledge lender; payday or deferred deposit lender; premium finance company; commercial finance or lending company; or commercial mortgage company; except entities registered or licensed solely on account of financing the entity’s direct sales of goods or services to customers;
    - (B) A money services business, including a check casher; money transmitter; currency dealer or exchange; or money order or traveler’s check issuer;
  - (iv) A regulated entity as defined in section 1303(20) of the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (12 U.S.C. 4502(20)) or any entity for which the Federal Housing Finance Agency or its successor is the primary federal regulator;



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- (v) Any institution chartered in accordance with the Farm Credit Act of 1971, as amended, 12 U.S.C. 2001 *et seq.* that is regulated by the Farm Credit Administration;
  - (vi) A securities holding company; a broker or dealer; an investment adviser as defined in section 202(a) of the Investment Advisers Act of 1940 (15 U.S.C. 80b-2(a)); an investment company registered with the Securities and Exchange Commission under the Investment Company Act of 1940 (15 U.S.C. 80a-1 *et seq.*), a company that has elected to be regulated as a business development company pursuant to section 54(a) of the Investment Company Act of 1940 (15 U.S.C. 80a-53(a)), or a person that is registered with the U.S. Securities and Exchange Commission as a security-based swap dealer or a major security-based swap participant pursuant to the Securities Exchange Act of 1934 (15 U.S.C. 78a *et seq.*).
  - (vii) A private fund as defined in section 202(a) of the Investment Advisers Act of 1940 (15 U.S.C. 80-b-2(a)); an entity that would be an investment company under section 3 of the Investment Company Act of 1940 (15 U.S.C. 80a-3) but for section 3(c)(5)(C); or an entity that is deemed not to be an investment company under section 3 of the Investment Company Act of 1940 pursuant to Investment Company Act Rule 3a-7 (§ 270.3a-7 of this title) of the Securities and Exchange Commission;
  - (viii) A commodity pool, a commodity pool operator, a commodity trading advisor, a floor broker, a floor trader, an introducing broker or a futures commission merchant;
  - (ix) An employee benefit plan as defined in paragraphs (3) and (32) of section 3 of the Employee Retirement Income and Security Act of 1974 (29 U.S.C. 1002);
  - (x) An entity that is organized as an insurance company, primarily engaged in writing insurance or reinsuring risks underwritten by insurance companies, or is subject to supervision as such by a State insurance regulator or foreign insurance regulator;
  - (xi) An entity, person, or arrangement that is, or holds itself out as being, an entity, person, or arrangement that raises money from investors, accepts money from clients, or uses its own money primarily for investing or trading or facilitating the investing or trading in loans, securities, swaps, funds or other assets; or
  - (xii) An entity that would be a financial end user described in paragraph (1) of this definition or a swap entity if it were organized under the laws of the United States or any State thereof.
- (2) The term “financial end user” does not include any counterparty that is:
- (i) A sovereign entity;
  - (ii) A multilateral development bank;
  - (iii) The Bank for International Settlements;
  - (iv) An entity that is exempt from the definition of financial entity pursuant to section 2(h)(7)(C)(iii) of the Act and implementing regulations;
  - (v) An affiliate that qualifies for the exemption from clearing pursuant to section 2(h)(7)(D) of the Act; or
  - (vi) An eligible treasury affiliate that the [CFTC] exempts from the requirements of §§ 23.150 through 23.161 by rule.

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