September 13, 2019

Secretariat of the Basel Committee on Banking Supervision Bank for International Settlements
Secretariat of the International Organization of Securities Commissions
Board of Governors of the Federal Reserve System
European Banking Authority
European Central Bank
European Commission
European Securities and Markets Authority
Farm Credit Administration
Federal Deposit Insurance Corporation
Federal Housing Finance Agency
Financial Conduct Authority
Office of the Comptroller of the Currency
U.S. Commodity Futures Trading Commission
U.S. Department of the Treasury
U.S. Securities and Exchange Commission
Australian Prudential Regulation Authority
Brazil National Monetary Council
Canada Office of the Superintendent of Financial Institutions
Central Bank of Brazil
Central Bank of Ireland
Hong Kong Monetary Authority
Japan Financial Services Agency
Luxembourg Commission de Surveillance du Secteur Financier
Monetary Authority of Singapore
Korean Financial Supervisory Service
Swiss Financial Market Supervisory Authority
South African Prudential Authority
South African Financial Sector Conduct Authority

Re: Margin Requirements for Non-Centrally Cleared Derivatives – Remaining Stages of Initial Margin Phase-In

Dear Sirs and Madams:

The Asset Management Group of the Securities Industry and Financial Markets Association ("**AMG**")[1] is writing in regards to several scoping and implementation issues that asset managers and their clients are facing in the remaining phases of the implementation of initial margin ("**IM**") requirements for non-centrally cleared derivatives (commonly referred to as the "**Uncleared Margin Rules**" or "**UMRs**").

We support the recent July 23, 2019 joint statement of the Basel Committee on Banking Supervision ("**BCBS**") and the International Organization of Securities Commissions ("**IOSCO**") (the "**July 23, 2019 Statement**") recommending extending implementation of the remaining phases of the UMRs (by splitting Phase V into two phases). We encourage global regulators to adopt the July 23, 2019 Statement for regulatory certainty and clarity.[2] In particular, and consistent with the July 23, 2019 Statement, an intermediary phase-in

[1] SIFMA AMG brings the asset management community together to provide views on U.S. and global policy and to create industry best practices. SIFMA AMG's members represent U.S. and global asset management firms whose combined assets under management exceed $45 trillion. The clients of SIFMA AMG member firms include, among others, tens of millions of individual investors, registered investment companies, endowments, public and private pension funds, UCITS and private funds such as hedge funds and private equity funds.

[2] We applaud the Farm Credit Administration, the Federal Deposit Insurance Corporation, the Federal Housing Finance Agency, the Office of the Comptroller of the Currency (U.S. Department of the Treasury), the Board of Governors of the Federal Reserve System

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period between Phase IV and Phase V set at an amount above EUR/USD 50 billion[3] would allow market participants and regulators to assess and hopefully address difficulties in implementation prior to the rush of counterparties coming within scope at the EUR/USD 8 billion threshold,[4] and would allow for the tapered development of market infrastructure necessary for successful compliance.

We also support the March 5, 2019 joint statement of BCBS/IOSCO (the "**March 5, 2019 Statement**")[5] clarifying that "the [UMR] framework does not specify documentation, custodial or operational requirements if the bilateral initial margin amount does not exceed the framework's [EUR/USD] 50 million IM threshold," and we appreciate that this clarification was effectively adopted in an Advisory issued on July 9, 2019 by the Division of Swap Dealer and Intermediary Oversight ("**DSIO**") of the Commodity Futures Trading Commission ("**CFTC**") (the "**Advisory**"). As you know, a number of buy-side entities will become subject to the current UMRs in Phases IV and V solely as a result of their aggregate average notional amount ("**AANA**") exposures, because many of these entities do not necessarily present systemic risk, and even though a significant portion of the AANA may be made up of transactions not subject to margin obligations, such as physically settled FX transactions. In order to help ensure that the UMRs do not impose undue burdens on these buy-side entities and their sell-side counterparties, we urge global regulators to promptly adopt or publicly support the clarification provided in the March 5, 2019 Statement and the Advisory.[6]

While global regulatory adoption of both the March 5, 2019 Statement and the July 23, 2019 Statement would provide some much-needed certainty to the industry, those statements do not fully resolve other important scoping and implementation challenges presented by the UMRs. The time provided by the intermediary phase-in period recommended by the July 23, 2019 Statement will allow additional time that should be used by regulators to address the fundamental scoping and implementation issues discussed herein.[7] For the reasons described further in this letter, we respectfully request that regulators take the following actions:

<u>Scoping</u>

- *In the context of a beneficial owner with multiple separately managed accounts through multiple asset managers (each account, an "**SMA**"), permit the calculations of the EUR/USD 50 million IM threshold ("**IM Threshold**") to be done annually, rather than daily, using the same measurement period that is used for performing the AANA calculations*. As further described herein, approaching the IM Threshold calculation in this way allows it to be an effective scoping tool for the UMRs; alternative

(together, the "**Prudential Regulators**"), the Australian Prudential Regulation Authority, the Hong Kong Monetary Authority, the Monetary Authority of Singapore and the South Korean Financial Supervisory Service for expressing support for BCBS/IOSCO's push-out approach and for their efforts to develop rules extending the implementation timeline.

[3] We recognize that not all regulators will use this number or its equivalent, but the EUR/USD figures will be used throughout for reference because it most closely reflects the figures in the March 2019 Statement.

[4] In addition, we believe that the EUR/USD 8 billion threshold should be raised, as discussed in Part I, Section (b) of this letter.

[5] BCBS/IOSCO Statement on the Final Implementation Phases of the Margin Requirements for Non-centrally Cleared Derivatives, dated March 5, 2019, available at https://www.bis.org/press/p190305a.htm.

[6] We commend the Prudential Regulators, the Australian Prudential Regulation Authority, the Canada Office of the Superintendent of Financial Institutions and the Hong Kong Monetary Authority for also supporting the March 5, 2019 Statement.

[7] We recognize that the Securities and Exchange Commission's ("**SEC**") final uncleared margin rules for security-based swaps are not yet effective; however, as those rules come into effect, largely the same concerns will apply to security-based swap dealers, and adjustments in regulations should apply similarly to security-based swap dealers to the extent any such adjustments are made. *See* 84 Fed. Reg. 43872 (August 22, 2019) (SEC's uncleared margin rules regarding Security-Based Swap Dealers and Major Security-Based Swap Participants).

approaches are unduly burdensome from an operational and documentation perspective, create uncertainty and may result in unworkable deadlines and trading disruptions.[8]

- *Provide an exemption, to the extent not already available, from consolidating seeded investment funds with their sponsors for purposes of AANA calculations.* Consolidation is not warranted given the limited and passive nature of the relationship between seeded funds and their sponsors, as described in this letter; moreover, such consolidation is not required for UCITS-regulated funds under the EU's adoption of the UMRs, which may create an opportunity for regulatory arbitrage and competitively disadvantage U.S. and other markets.

- *Provide an exemption for physically settled foreign exchange ("**FX**") swaps and forwards from AANA calculations.* Including physically settled FX swaps and forwards is not warranted because they are short-dated and highly liquid transactions that present low long-term or systemic risk and do not require the exchange of IM under the rule.

- *Provide an exemption for single-stock equity options and index options from margin requirements.* The EU's equity option derogation is set to expire in January 2020, but the reasons for such derogation or extension still exist, as US regulations do not apply UMRs to equity options, which will result in market fragmentation and regulatory arbitrage when the derogation expires.[9] Other jurisdictions have afforded similar flexibility with respect to security-index options and security options. Where these exemptions are time-delimited, we urge regulators in all relevant jurisdictions to make such exemptions permanent.

<u>Implementation</u>

- *To the extent the IM Thresholds could not be calculated using the standard AANA measurement period, provide a grace period for SMAs following notice from the applicable swap dealer that aggregate IM is near or exceeds the IM Threshold during which the SMA, through its respective asset manager, must complete the necessary documentation and system set-ups.* An expectation of immediate action would be unreasonable considering that asset managers lack the transparency to predict when a client's aggregate IM (across all of its asset managers) with a swap dealer and its affiliates is at or near the IM Threshold. Without such a grace period, swap dealers may decide to halt trading with some or all of the asset managers for an SMA without much advanced notice until they comply with the new UMRs. This could negatively impact managers' performance and may force them to novate or early terminate existing transactions, thus causing clients to suffer unnecessary costs or losses in their portfolios. Additionally, once the aggregate IM is near or exceeds the IM Threshold, there may be complications in determining how to sub-allocate the IM Threshold across asset managers and a swap dealer (and its affiliates, if any) for purposes of determining how much IM should be collected from each SMA of a beneficial owner. Similar to minimum transfer amounts ("**MTAs**") as discussed below, sharing or allocating IM Thresholds dynamically would be challenging and impractical from an operational and documentation perspective, potentially requiring multiple amendments to reallocate sub-allocations of the IM Thresholds as the number of asset managers and/or volume of trading activities change.

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[8] As discussed briefly in Part I of this letter, the failure to adopt the proposed annual approach to calculating the IM Threshold would make it even more critical to implement other scoping adjustments, such as raising the AANA thresholds for the remaining UMR phases and removing deliverable foreign exchange swaps and forwards from the AANA calculation.

[9] Commission Delegated Regulation (EU) 2016/2251(43), October 4, 2016.

- *Expand the list of eligible collateral, in particular, by removing the unduly restrictive conditions to the use of money market funds ("**MMFs**").* The current restrictions on the use of MMFs broadly disqualify many (if not most) MMFs, which would result in economic and operational inefficiencies and create unnecessary burdens on asset managers and their clients.

- *Adopt relief similar to that provided in CFTC No-Action Letter 17-12 to permit asset managers to adopt a fixed sub-MTA at each SMA level rather than having to actively share the aggregate MTA per each SMA owner with each swap dealer.* With the implementation of regulatory IM, there is an even more pressing need to ensure that allocations of MTA, which represents a combined amount of required IM and required variation margin, are handled effectively and efficiently; the flat allocation approach in CFTC Letter 17-12[10] ensures that the regulatory purpose of MTAs is served while minimizing operational challenges and documentation burdens for asset managers.

- *Remove back-testing and internal governance process requirements for non-dealers' use of globally accepted IM models.* As summarized in a recent letter to EU regulators,[11] non-dealers coming into scope during Phases IV and V should not be subject to internal back-testing requirements and should not be required to go through the initial approval process when using globally approved IM models such as ISDA SIMM.

We discuss these issues in more detail below. We recognize that there are differences among various jurisdictions' rules, and therefore the issues in this letter may be more or less relevant in one jurisdiction than another. Ultimately, we have advocated for, and continue to support, a level global regulatory playing field. Accordingly, our views on the issues identified herein are directed towards the establishment of a global standard and minimization of cross-border inconsistencies.

I. SCOPING ISSUES

(a) The IM Threshold Can Serve as an Effective Scoping Tool if it is Calculated Annually Using the Same Time Period as the AANA Calculation.

In former CFTC Chairman Giancarlo's April 29, 2019, letter to the Federal Reserve Board of Directors,[12] the then-Chairman acknowledged that in the absence of certain relief under the UMRs (e.g., raising the AANA threshold from $8 billion to $50 billion), the IM Threshold becomes an even more important scoping tool for determining which entities should be subject to regulatory IM requirements, including documentation, custodial, and operational requirements. Specifically, the former Chairman set forth his view that "[e]ntities with notional amounts greater than $8 billion but calculated margin less than $50 million [i.e., calculated margin that does not exceed the IM Threshold]" should be "spared the expense of preparing to exchange margin." We wholeheartedly support the former Chairman's balanced approach.

Precisely how often the IM Threshold should be calculated is not, however, described in the former Chairman's letter, in the Advisory, or under the UMRs. For instance, in adopting the UMRs, U.S. regulators did not explicitly identify the *frequency* of the IM threshold calculation, instead focusing on its *methodology*: "The

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10 CFTC Letter No. 17-12 (dated, February 13, 2017) available at https://www.cftc.gov/sites/default/files/idc/groups/public/@lrlettergeneral/documents/letter/17-12.pdf.

11 See International Swaps and Derivatives Association ("**ISDA**"), Association of the Luxembourg Fund Industry ("**ALFI**") and SIFMA letter to the European Securities and Markets Authority ("**ESMA**"), European Banking Authority ("**EBA**") and European Insurance and Occupational Pensions Authority ("**EIOPA**"), March 17, 2019 at https://www.isda.org/a/Y3tME/2019.05.17_EU-Letter_IM-Models_FINAL.pdf.

12 CFTC Chairman Giancarlo's Letter to Federal Reserve Board Vice Chairman Randal K. Quarles on Phase Five Implementation, dated May 2, 2019, available at https://www.cftc.gov/PressRoom/PressReleases/7922-19.

$50 million threshold is measured as the amount of initial margin for the relevant portfolio of non-cleared swaps and non-cleared security based swaps, pursuant to either the internal model or standardized initial margin table used by the covered swap entity [and its consolidated affiliates]."[13] As a result, there is some latent ambiguity regarding the frequency with which such calculations should be made.

If the IM Thresholds are required to be calculated daily on an aggregate basis, a host of complications and challenges may arise, particularly in the context of SMAs. An SMA client may have multiple strategies executed through separate asset managers. The SMA approach achieves a diversity of investment perspectives/expertise and asset allocations for the invested assets and mitigates concentration risks. In these SMA arrangements, each asset manager for a SMA client generally trades under agreements it negotiates on behalf of its SMA client, maintains separate assets under management for its strategy and has no transparency nor control as to the derivatives activities executed through other asset managers nor to the client's (and the client's consolidated affiliates') aggregate exposures across all of its derivatives positions. While an individual swap dealer may not have transparency to the SMA client's AANA across all swap dealers, it, however, will have visibility across that SMA client's trades through all asset managers with the swap dealer and its affiliates. Additionally, under certain UMRs, it is the covered swap entity (i.e., the swap dealer) who is expected to calculate the amounts of IM that are required to be exchanged between itself and its counterparties and, solely with respect to its counterparties whose AANAs exceed the threshold for the relevant year, to monitor whether the aggregate IM requirements would exceed the IM Threshold.

If the IM Threshold has to be calculated on a daily basis, then the swap dealer in this scenario would be calculating at least *two* separate margin amounts every day:

(1) per each asset manager for the same SMA client (and its consolidated affiliates), the margin requirement to be exchanged based on existing margin methodology,[14] and

(2) the aggregate simulated IM requirements for the same SMA client (and its consolidated affiliates), using the swap dealer's internal model, SIMM, or standardized initial margin table, in order to see how close the simulated IM is (across all asset managers trading on behalf of the SMA client (and its consolidated affiliates) with the dealer and its affiliates) to the IM Threshold.[15]

Running a minimum of two types of calculations (potentially on a real-time basis) per day per SMA client—one pursuant to existing margin methodology and the other a simulated calculation *per each asset manager* to check against the IM Threshold and then aggregating those calculations across managers for the same SMA client (and its consolidated affiliates)—poses obvious operational costs and undue burdens on both the sell-side and the buy-side. As the Prudential Regulators have observed, it could create a "significant operational burden" to have to calculate "initial margin collection amounts on a *daily basis* even though no initial margin would be expected to be collected."[16] Furthermore, if, in the course of daily calculation and monitoring, the swap dealer determines that the IM Threshold is exceeded or close to being exceeded, then the SMA client's asset managers must immediately work with the same SMA client, SMA client's IM custodian, and the swap dealer (and any affiliates) and the swap dealer's tri-party agent to get all of the documentation and accounts in place by the relevant regulatory IM deadlines. Swap dealers may also selectively choose to prioritize the legal

[13] *See* 80 Fed. Reg. 74840, 74864 (Nov. 30, 2015) (Prudential Regulators' final uncleared margin rules); *see also* 81 Fed. Reg. 636, 653 (Jan. 6, 2016) (CFTC's final uncleared margin rules).

[14] This would be a net requirement, assuming that the asset managers would not split old trades from new trades or require variation margin to be calculated separate from voluntary IM. If the asset manager did split its legacy book from new transactions, it could further exacerbate the number of margin calls and calculations the swap dealer would have to perform on a daily basis.

[15] 12 C.F.R. § 23.154 (CFTC rule re IM models); 12 C.F.R. 45.8 (Comptroller of Currency rule re IM models); 12 C.F.R. 237.8 (Federal Reserve rule re IM models); 12 C.F.R. 349.8 (FDIC rule re IM models); 12 C.F.R. 1221.8 (FHFA rule re IM models).

[16] *See* 80 Fed. Reg. 57366 (Sept. 24, 2014) (Prudential Regulator's Proposed Margin and Capital Requirements for Covered Swaps Entities).

and operational set-up with a subset of the SMA client's asset managers, therefore effectively shutting down trading with the smaller managers or with managers doing less trading on a temporary or permanent basis. Practically speaking, however, regardless of the number of asset managers, it may be impossible to successfully accomplish this race against the clock as each manager and swap dealer simultaneously compete for the same custodian's and tri-party agent's time and resources. The process of negotiating and finalizing UMR compliant documentation and completing the operational set-up is lengthy and complex, frequently taking market participants up to a year or more to complete.

In light of the problems with a daily calculation of the IM Threshold, AMG urges regulators to confirm that the following proposal is acceptable: the IM Threshold would be calculated *annually*, using the same calculation periods used to determine whether AANA thresholds are exceeded. In adopting the calculation approach for the AANA threshold, the U.S. regulators explained that the specified time period (i.e., June, July, and August of the previous year) "is appropriate to gather a more comprehensive assessment of the financial end user's participation in the swaps market, and to address the possibility that a market participant might 'window dress' its exposure..."[17] The regulatory comfort with using a three-month period once a year to measure AANA should also apply to using the same approach for calculating the IM Threshold. Both the AANA threshold and the IM Threshold function as scoping tools and, together, they would determine and provide much needed certainty as to whether an entity is in scope for regulatory IM for the period beginning September of the relevant year (or, after the final implementation phase-in, for the period beginning January of the relevant year).

Once an asset manager(s) for an SMA client receives notice from the applicable swap dealer that the SMA client's simulated IM Threshold and AANA threshold were both exceeded during the calculation period, they would proceed to put in place required documentation for regulatory IM. If the thresholds were not exceeded, then the parties would know with certainty that the SMA client would not be subject to regulatory IM requirements at least until the next annual calculation period. This approach would remove the costs and complexities of swap dealers having to do simulated IM calculations on an ongoing basis throughout the year and, for asset managers' SMAs, it would eliminate the additional complexities around potentially negotiating (and renegotiating) the sub-allocations of IM Thresholds and monitoring IM levels across multiple asset managers[18] and unnecessary fire-drills to ensure the documentation and operational set-ups are completed by the time the aggregate regulatory IM across all asset managers is at or near $50 million.

An added advantage of this approach is that, unlike AANA thresholds where only underlying clients with differing levels of sophistication have full transparency into their aggregate notional exposures, the IM Threshold can be calculated on an annual basis accurately and relatively simply by swap dealers. Additionally, the swap dealers could calculate the IM Thresholds for the relevant AANA calculation periods and pre-determine the narrower client base who may potentially be in scope of the regulatory IM requirements well in advance of receiving confirmation whether such clients have exceeded the AANA thresholds. The IM Threshold calculations could essentially drive where AANA calculations are necessary, greatly increasing precision, reducing work needed to identify in scope accounts, and providing much needed predictability for all parties.

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[17] *See* 80 Fed. Reg. 74840, 74857 (Nov. 30, 2015).

[18] Any approach involving a "flat" sub-allocation of the IM Threshold would also be problematic. Under that approach, if an SMA exceeds its assigned sub-allocation (representing a portion of the $50 million unmargined credit exposure), the SMA would potentially be subject to regulatory IM requirements even though it is unlikely to present systemic risk and, on an aggregate basis, the SMA client might not have exceeded the IM Threshold.

(b) Failure to Adopt an Annual Approach to Calculating the IM Threshold Would Make it Even More Critical to Implement Other Scoping Adjustments.

If the proposal set forth above for annual calculation of the IM Threshold is not adopted, then it is unlikely that the IM Threshold would be a workable and effective scoping tool. It would then be even more critical to raise the current gross notional threshold of EUR/USD 8 billion for Phase V, in addition to implementing an intermediary phase-in as recommended by the July 23, 2019 Statement.[19] The gross notional threshold of EUR/USD 8 billion should be adjusted because most of the counterparties that will come into scope do not contribute materially to systemic risk but will incur the undue costs of compliance.[20]

(c) Seeded Funds Should Not Be Consolidated with Their Sponsors for Scoping Purposes.

The AMG continues to urge regulators to not require a seeded fund to aggregate its notional exposures with those of its parent or other commonly consolidated entities for purposes of calculating its AANA.[21] A seeded investment fund is a fund which has received a large portion of its starting capital from a larger fund (a "**sponsor**"). The relationship between a sponsor and a seeded fund is not analogous to the relationship between a parent company and its subsidiaries. While the sponsor may retain a passive, equity interest in the seeded fund, neither it nor its commonly consolidated entities controls or has transparency into the management or trading of the fund. The seeded fund retains independent management and investment discretion and has independent fiduciary duties to the other investors in the fund (if any). Additionally, the sponsor's exposure to the seeded fund is capped at its investment, similar to any other passive investment. In the Volcker Rule, the Prudential Regulators recognized that it is common practice to seed funds (in particular, retail funds) in order to build a track record in performance and attract third party investors.[22] Seeded funds typically do not have uncleared swaps exposures that pose significant risks to swap counterparties or the financial system and most will never exchange IM under the UMRs (absent the consolidation requirements) because their swaps exposures will be below the IM Threshold.

It is also worth noting that the EU adoption of the UMRs do not require consolidation for UCITS-regulated funds. This principle should be expanded in the EU to apply to all seeded funds regardless of whether they are EU-regulated and consistently adopted in other jurisdictions. Absent any changes to the AANA consolidation requirements for seeded funds under the existing UMRs, it may become prohibitively expensive for newly seeded funds to use derivatives or FX because of the mandatory IM requirements that they may be subject to and the resulting substantial costs on returns for investors. This would not be due to the fund's individual swap activity presenting any systemic risk, but solely as a result of the UMR requirement to aggregate its AANA calculations with a sponsor or commonly consolidated entities that may have material swaps exposures, despite those entities having neither transparency as to, nor control over, the fund's trading. In addition, given the disparity between the EU's approach and other jurisdictional requirements, EU regulated funds may choose to only trade with EU dealers and thus, this may result in a shift in liquidity and a competitive

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[19] Managed Funds Association, October 25, 2018 letter to BCBS and IOSCO https://www.managedfunds.org/wp-content/uploads/2018/11/MFA-Letter-UMR-Implementation-Challenges-for-Final-Stages-of-IM-Phase-in.pdf

[20] See CFTC Analysis, *Initial Margin Phase 5,* October 24, 2018. Can be found at: https://www.cftc.gov/sites/default/files/About/Economic%20Analysis/Initial%20Margin%20Phase%205%20v5_ada.pdf. (referred to hereafter as "CFTC Analysis"). See also Margin Requirements for Non-Centrally Cleared Derivatives – Final Stages of Initial Margin Phase-In, at: https://www.isda.org/a/5evEE/Initial-Margin-Phase-In-Implementation-Joint-Trade-Association-Comments.pdf. (referred to hereafter as "ISDA Data").

[21] See AMG letter to U.S. regulators, March 24, 2016, at https://www.sifma.org/wp-content/uploads/2017/05/sifma-amg-submits-supplemental-comments-to-multiple-regulators-regarding-request-for-relief-on-final-margin-rules-for-uncleared-swaps-transactions.pdf.

[22] 12 C.F.R. §248.12(a)(1); see also https://www.federalreserve.gov/supervisionreg/faq.htm#16.

disadvantage for US and other markets as some market participants take advantage of the regulatory arbitrage opportunities.

(d) FX Swaps and Forwards Should Be Excluded From AANA Calculations.

Physically settled foreign exchange ("**FX**") swaps and forwards should be removed from calculations of AANA because these products do not, under the rules, independently require IM exchange. AMG recommends this exemption for the same reason that regulators do not require IM to be exchanged under the UMRs. FX swaps and forwards are short-dated and highly liquid transactions that present low long-term or systemic risks. According to the ISDA Data and the CFTC Analysis, approximately 30% of counterparties and relationships will be brought into scope in Phases IV & V solely because of their FX swaps and forwards activity even though their material swaps exposures do not pose a significant risk to the financial system.

It is customary in the FX market for counterparties to extend the settlement date of their trades through a mechanism called a "roll". Rolls are effected by closing out an existing trade and then reopening a new position with the new settlement date. Accounts that roll physically settled FX swaps and forwards over month-ends may account for the large number of entities that are brought into scope in the ISDA Data that do not trade marginable securities. These entities are only brought into scope because of their FX swaps and forwards activity since the value of each nominally separate trade may not be netted in the AANA calculation. As a result, gross currency positions rolled over a month-end would be included three times in the AANA calculation: once for each of the original position, the close and reopen, which artificially inflates AANA.

It is inconsistent for the UMRs to exclude physically settled FX swaps and forwards from the calculation of IM but include them in the calculation of AANA. Derivatives that do not require the exchange of IM under the rules should not be considered when determining whether a counterparty is in scope to exchange margin.

(e) The EU Equity Option Derogation (and Other Similar Exemptions) Should Be Extended Indefinitely.

Single stock equity options and stock index options are not currently considered in the calculation of IM under US, EU, Singapore, Hong Kong and Korean UMRs, but equity options will become subject to the IM requirements under those UMRs in early 2020.[23] Thereafter, different rules will apply between US and other markets, creating opportunities for regulatory arbitrage. EU, Singapore, Hong Kong and Korean UMRs should be amended to exempt equity options from IM and variation margin requirements prior to January 2020. The stated reason for the derogation in the EU UMRs still applies to UMRs across all jurisdictions: "to avoid market fragmentation and ensure a level playing field" for local counterparties and to provide a period of time to monitor regulatory developments in other jurisdictions to "ensur[e] that appropriate requirements are in place in the [local jurisdiction] to mitigate counterparty credit risk in respect of [equity options] whilst avoiding scope for regulatory arbitrage."[24]

[23] For EU UMRs, see Regulation No. 2016/2251 of October 4, 2016 Supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council of July 4, 2012 on OTC Derivatives, Central Counterparties and Trade Repositories with Regard to Regulatory Technical Standards for Risk-Mitigation Techniques for OTC Derivative Contracts Not Cleared by a Central Counterparty (as corrected by Commission Delegated Regulation (EU) 2017/323 of January 20, 2017)(the "**Margin RTS**").

[24] The Margin RTS, paragraph (43).

II. IMPLEMENTATION ISSUES

(a) Once the IM Threshold is Close to Being Exceeded or is Exceeded, Grant Time Relief as Needed for Compliance with Regulatory IM Requirements and Develop a Feasible Approach for Allocating the IM Threshold.

To the extent that the IM Thresholds could not be calculated using the same AANA measurement period, then at least a six-month "moratorium" period that begins when an asset manager receives notice from a swap dealer that the IM Threshold is exceeded should be granted to allow sufficient time for SMAs through their asset managers to complete the necessary documentation and system set-ups. Asset managers are not positioned to undertake immediate action on behalf of SMAs given that they lack transparency to predict when the SMA client's aggregate IM (across all of its asset managers) with a swap dealer and its affiliates is at or near the IM Threshold. Additionally, swap dealers may unilaterally, and without much advanced notice, decide to halt trading with some or all asset managers for SMAs until they are in compliance with the regulatory IM requirements. Although the moratorium period would be helpful to achieve compliance within a reasonable timeframe, it would not address the problem, as discussed in Part I above, that swap dealers would still need to track hypothetical IM Thresholds daily for all SMA counterparties, even before they were otherwise required to post IM.

In addition, the lack of visibility that makes it practically impossible for asset managers and their SMA clients to calculate the IM Threshold also renders it practically impossible for asset managers to allocate among themselves the IM Threshold for a given SMA client. Again, only the dealers will have the necessary visibility to do so; but, again, they will be faced with serious operational challenges: IM positions, as well as the identity of asset managers a client may employ, may change, thereby potentially affecting how allocations should be made. Currently, we are unaware of any feasible solution to this problem and accordingly we ask that regulators work with market participants to formulate one.

(b) Barriers to the Use of Money Market Funds as Eligible Collateral Should Be Eliminated.

We urge global regulators to eliminate the restrictions and conditions in the various UMRs on the use money market funds as eligible IM collateral.[25] As acknowledged by global regulators, the vast majority of asset managers and end-user clients historically have used cash as margin for derivatives transactions. This was in large part due to cash being fungible and easily transferrable, and not subject to any margin haircuts. As buy-side market participants have steadily increased the use of tri-party IM segregation arrangements (for both voluntary and mandatory IM) and margin transfer deadlines continue to contract from a regulatory perspective, there has been a growing proliferation of the use of money markets funds as a secure and efficient alternative to cash margin. Many client custodians offer money market sweep programs that allow asset managers and end-user clients the continued operational ease of pledging cash into the tri-party accounts and then instructing custodians to sweep such cash into money market fund shares that are pledged as collateral to swap counterparties. The eligible money market funds invest predominantly in treasuries and other high quality, short-term government securities. These money market sweep arrangements afford the buy side the ability to efficiently meet margin calls in compressed timeframes without having personnel constantly buying or selling treasuries or other non-cash assets or dealing with odd lot sizes and other settlement issues. Additionally, asset managers and end-user clients can effectively mitigate insolvency risks to the custodians (as non-cash collateral would not be consolidated with the custodian from a supplemental leverage ratio and bankruptcy perspective) and potential negative interest rate charges. Without the ability to broadly use money market funds as eligible IM collateral, asset managers may be forced to liquidate investments and constantly buy and sell other eligible forms of non-cash assets that may be sub-optimal for, or inconsistent with, the client's portfolio strategy and

[25] See AMG joint letter to U.S. regulators, August 1, 2019, at https://www.sifma.org/wp-content/uploads/2019/08/ISDA-Letter-to-US-Regulators-Cash-and-Money-Market-Funds-as-Initial-Margin-8.1.19.pdf.

thus could result also in unnecessary costs and operational burdens, negative performance and/or tracking errors.

While the U.S. margin regulations do allow for the use of redeemable securities in a pooled investment fund that holds only U.S. Treasuries (or securities unconditionally guaranteed by the U.S. Treasury) and cash funds denominated in U.S. dollars, this form of eligible collateral is subject to the undue limitation that "*the fund's assets may not be transferred through securities lending, securities borrowing, repurchase agreements, reverse repurchase agreements or other similar means"*.[26] To the AMG's knowledge, a significant percentage of all U.S. money market funds engage in some form of these activities in order to mitigate a money market fund's insolvency exposure to its custodian and any consolidation issues with respect to any cash held at the custodian as well as to avoid any cash drag on performance. As a result, this limitation severely reduces the number of eligible money market funds that could be used under the UMRs. AMG finds the imposition of this limitation to be unwarranted and inconsistent with other regulations where regulators have recognized government money market funds as safe, high quality investments, such as CFTC Regulation 1.25 (which governs the investment of customer money by futures commission merchants ("**FCM**s") without similar restrictions).[27]

Although the EU margin regime, as described in the Margin RTS, includes as eligible collateral cash in the form of a claim for the repayment of money, such as money market deposits[28], it imposes unnecessary barriers to the use of money market funds as IM[29], such as (a) the concentration limits applicable to shares or units in UCITS under Article 8(1)(a) of the Margin RTS and (b) the requirement under Annex II of the Margin RTS that the haircut applicable to an interest in a UCIT is the weighted average of the haircuts that would apply to the assets in which the underlying money market fund is invested. Such concentration limits unjustifiably undermine and curtail the effective use of money market fund sweeps as market participants would have to actively monitor such limits and/or potentially use other forms of eligible margin. Similarly, absent the ability for market participants to actively monitor the investments of the underlying money market funds and dynamically amend the associated haircuts in their credit support documents and in their collateral management systems per each money market fund's investments, the haircut requirement is practically unworkable.

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[26] 12 CFR 237.6 (CFTC eligible collateral); 12 CFR 237.7 (CFTC segregation of collateral); 12 CFR 45.6 (Comptroller of Currency eligible collateral); 12 CFR 45.7 (Comptroller of Currency segregation of collateral); 12 CFR 237.6 (Federal Reserve eligible collateral); 12 CFR 237.7 (Federal Reserve segregation of collateral); 12 CFR 349.6 (FDIC eligible collateral) 12 CFR § 349.7 (FDIC segregation of collateral); 12 CRF 624.6 (FCA eligible collateral); 12 CFR 624.7 (FCA segregation of collateral); 12 CFR 1221.6 (FHFA eligible collateral); 12 CFR 1221.7 (FHFA segregation of collateral).

[27] Pursuant to Regulation 1.25(c), a money market fund is a permissible investment for customer funds by an FCM so long as it meets certain non-problematic requirements and does not voluntarily elect to be subject to liquidity fees or redemption restrictions (See CFTC Letter No. 16-68 (No Action) Aug 8, 2016). Moreover, Regulation 1.25 specifically permits, subject to certain requirements, FCMs to buy and sell otherwise permitted investments pursuant to repurchase and reverse repurchase agreements.

[28] The CFTC has published "comparability determinations" for margin regulations of the EU and Japan (78 FR 78923 and 78 FR 78878 (EU comparability determination); and 78 FR 78890 and 78 FR 78910 (Japan comparability determination)). These determinations mean that certain U.S. market participants facing European or Japanese counterparties in uncleared swaps should be able to comply with the margin rules of those jurisdictions rather than the CFTC's margin regulations. Similarly, in October 2017, the European Commission adopted an implementing decision that the CFTC margin requirements should be considered equivalent to those provided for under Article 11(3) of Regulation (EU) No 648/2012. This means that counterparties within the scope of the EU margin requirements can fulfil their obligations by complying with the CFTC's margin regulations, where at least one party to the transaction is established in the U.S. and registered with the CFTC as a swap dealer or major swap participant and is subject to the CFTC's margin requirements. While these comparability determinations are helpful, they are of limited utility to asset managers. First, they are effective only with respect to swap dealers or major swap participants that are subject to the jurisdiction of the CFTC and not with respect to the market participants under the regulatory jurisdiction of the Prudential Regulators which asset managers' clients face. Second, asset managers' clients may still be subject to the duplicative and/or conflicting margin rules of multiple jurisdictions, depending on the jurisdictions of each client and swap dealer and other factors, such as a client's principal place of business or where a swap dealer has arranged, negotiated or executed such transactions.

[29] See AMG Comment Letter, SIFMA AMG's Feedback on European Commission's EMIR Proposal, July 18, 2017, https://www.sifma.org/wp-content/uploads/2017/07/SIFMA-AMG-Provides-Comments-on-European-Commission-Proposal-to-Amend-EMIR.pdf.

(c) Asset Managers Should Be Permitted to Allocate Partial MTAs at the SMA Level.

AMG urges regulators to globally adopt the approach outlined in the CFTC's DSIO No-Action Letter 17-12 that allows for asset managers to apply no greater than a USD 50,000 MTA to each separate SMA it manages. This approach offers a workable solution to the operational and documentation burdens that asset managers otherwise have faced since March of 2017 in having to negotiate separate sub-allocations of the EUR/USD 500,000 MTA with each swap dealer *for each SMA (and subsequent amendments thereto)* despite the fact that each manager neither has any control nor transparency as to the number of other asset managers trading with the same dealer for the same SMA client. If such relief is not adopted globally, the operational and documentation challenges will continue to compound as the implementation of regulatory IM with SMAs captures increasingly more counterparties given that the MTA must be further split between regulatory IM and regulatory variation margin per each SMA, asset manager and swap dealer combination.

(d) Non-Dealers Using ISDA SIMM and Other Globally Approved Models Should Be Exempt from Back-Testing and Model Governance Rules.

With respect to AMG's request that regulators consider exempting parties using ISDA SIMM and other globally approved models, we refer to the March 17, 2019 letter referred to above.[30] Non-dealers coming into scope during Phases IV and V should not be subject to internal back-testing requirements, and should not be required to comply with the initial margin model approval process when using globally approved IM models such as the ISDA SIMM.

We appreciate your consideration of this letter and look forward to discussions that will address the issues raised. Please do not hesitate to contact Jason Silverstein, at jsilverstein@sifma.org or at +1-212-313-1176, or Tim Cameron at tcameron@sifma.org or at +1-202-962-7447.

Sincerely,

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[30] See ISDA, ALFI and SIFMA letter to ESMA, EBA and EIOPA, March 17, 2019 at https://www.isda.org/a/Y3tME/2019.05.17_EU-Letter_IM-Models_FINAL.pdf.