June 24, 2016

Department of the Treasury/Office of the Comptroller of the Currency
Docket No. OCC-2011-0008/RIN 1557-AD43s

Farm Credit Administration
RIN 3052-AC69

Board of Governors of the Federal Reserve System
Docket No. R-1415/RIN 7100 AD74

Federal Housing Finance Agency
RIN 2590-AA45

Federal Deposit Insurance Corporation
RIN 3064-AE21

Commodity Futures Trading Commission
RIN 3038-AC97

Addresses listed in Annex I

Re: Docket No. OCC-2011-0008/RIN 1557-AD43s; Docket No. R-1415 /RIN 7100 AD74; RIN 3064-AE21; RIN 3052-AC69; RIN 2590-AA45; RIN 3038-AC97

REQUEST FOR DELAY OF SWAP MARGIN REQUIREMENTS

Ladies and Gentlemen,

The International Swaps and Derivatives Association[1] ("**ISDA**") requests that the Prudential Regulators (the "**PRs**") and the Commodity Futures Trading Commission (the "**CFTC**", and together with the PRs, the "**US Regulators**") delay the implementation of swap margin requirements for covered swap entities ("**CSEs**"). This relief is requested in light of the recent statement by the European Commission of its intention to delay implementation of margin requirements for the firms that were previously scheduled to comply with the requirements starting on September 1, 2016 ("**Phase I Firms**").

Because our members are currently devoting significant resources to the margin requirements, and because the initial deadline of September 1, 2016 is fast approaching, we would greatly appreciate a prompt response to this letter.

1 Since 1985, ISDA has worked to make the global over-the-counter ("**OTC**") derivatives markets safer and more efficient. Today, ISDA has over 800 member institutions from 64 countries. These members include a broad range of OTC derivatives market participants including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure including exchanges, clearinghouses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's web site: www.isda.org.

Request:

ISDA requests the following relief:

(1) The US Regulators delay implementation of the margin requirements under the PR and CFTC margin rules (together, the "**US margin rules**") until the new implementation dates applicable under the EU margin rules. To demonstrate readiness for compliance with US margin rules, Phase I Firms would obtain initial margin (“**IM”)** model approvals, and make, exchange and agree to IM calculations starting on September 1, 2016, but would not transfer IM until the applicable implementation dates under the EU margin rules. These Phase I Firms would provide this IM data to the US Regulators upon request.

(2) If the US Regulators do not grant the above request for relief, in the alternative, ISDA requests that US Regulators modify the Phase I Requirements[2] so that the relevant CSEs would be required to exchange variation margin ("**VM**") starting on September 1, 2016. As under (1) above, to demonstrate readiness for compliance with US margin rules, Phase I Firms would obtain initial margin model approvals, and make, exchange and agree to IM calculations starting on September 1, 2016, but would not transfer IM until the applicable implementation dates under the EU margin rules. As under (1) above, these Phase I Firms would provide this IM data to the US Regulators upon request.

Either of these alternatives would avoid the market dislocation that will result from inconsistent go-live dates, achieve the regulatory objective of ensuring each non-cleared derivative trade is margined with respect to market moves, and would ensure that US banks are ready to proceed ‘at the push of a button’ when other major regulators have finalized their rules. For clarity, this proposed alternative would not result in any obligation to retroactively transfer the IM that was calculated for data exchange purposes – any obligation to make actual transfers would apply only to new trades entered into starting on the new implementation dates applicable under the EU margin rules.

Discussion:

The EU delay has resulted in a discrepancy in implementation timing between the US margin rules and the EU margin rules. Because of this, the market will face numerous obstacles, including market dislocation, disruption of cross-border trading, concentration of counterparty risk, new implementation challenges and an unlevel playing field for firms subject to the US margin rules. These disruptions will have a significant impact on markets and firms. The discrepancy in timing is also inconsistent with the cross-border harmonization that has been a guiding principle of the BCBS/IOSCO Framework.[3]

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2 The "**Phase I Requirements**" are the requirements for margin under the US margin rules that will apply to CSEs on September 1, 2016.

3 *See* the margin framework for non-centrally cleared derivatives issued by the Basel Committee on Banking Supervision ("**BCBS**") and the International Organization of Securities Commissions ("**IOSCO**") in March 2015 at http://www.bis.org/bcbs/publ/d317.pdf (the "**BCBS/IOSCO Framework**").

1. Market Dislocation, Disruption of Cross-Border Trading, Concentration of Counterparty Risk

The EU delay will cause fragmentation in the market and a reduction in liquidity. Certain Phase I Firms ("**Subject Entities**") will remain subject to the US margin rules even if they face non-US counterparties. Subject Entities will include US CSEs and non-US CSEs with a US parent, facing non-US counterparties. Other firms ("**Delayed Entities**") will not be subject to the US margin rules when facing non-US counterparties, even when one or both parties are registered as swap dealers under Dodd-Frank. Delayed Entities will include non-US CSEs (without a US guarantee or a US parent) facing non-US counterparties.[4] The disparate treatment of non-US CSEs with US parents and non-US CSEs without US parents goes beyond the distinctions created by the US clearing and trade execution mandates, which apply the same exemption to non-US CSEs regardless of whether they have US parents or not.

Following the EU delay, Delayed Entities will be strongly incentivized to trade with other Delayed Entities, rather than with Subject Entities, in order to avoid the costs of the US margin rules. The costs to Delayed Entities of trading with Subject Entities are illustrated by the examples set out in Appendix I, based on a 12 month cost basis. In these examples, the additional cost to a Delayed Entity of trading with a Subject Entity, rather than with another Delayed Entity, range as high as more than twice a typical bid/offer spread.

These same pricing pressures could encourage a Subject Entity that has an affiliate that is a Delayed Entity (for example, a non-US affiliate that is not a CSE) to shift its trading volume to the affiliated Delayed Entity, leading to strains on the market resulting from a shift in trading volume. It is likely that separate US and non-US markets will develop. This scenario will result in market fragmentation with two distinct liquidity pools and increased risk concentration within each market, transferring costs to market participants including end-users.

Any EU delays of the VM requirements that are scheduled to take effect on March 1, 2017 (the "**Phase II Requirements**") will result in further market fragmentation and reductions in liquidity for client-facing swaps because Subject Entities, but not Delayed Entities, will be required to collect VM from clients. Lack of synchronization will mean that, at every stage, counterparties in non-US jurisdictions will prefer to trade with Delayed Entities rather than with Subject Entities and, as a result, a tiered market will develop.

2. New Implementation Challenges

The timing discrepancy between the EU margin rules and the US margin rules will result in new implementation challenges for CSEs due to uncertainty about the final EU margin requirements at the time the US requirements must be implemented as well as due to the complexity of having to modify systems and documents to comply with regulations at least twice (first with respect to the US margin rules and then again with respect to the finalized EU margin rules).

4 Similar reasoning will apply to entities subject to the margin rules of other jurisdictions, such as Japan, Switzerland and Canada. However, we have limited the analysis here to entities subject to/not subject to the US margin rules, because at the time of this letter, it is unknown whether other jurisdictions will also delay their margin rules for Phase I and/or beyond.

Final EU Margin Rules Uncertain. The final text of the EU margin rules is not yet certain, and the EU has not specified which aspects of its margin rules will change. Firms will need to ensure that their models and trading systems are up and running in order to meet the US timeline, while trying to accommodate future adjustments based on the EU margin rules without knowing what the final content of the EU margin rules will be. This challenge arises in addition to the obstacles already being faced by firms that need to accommodate future finalization of rules in multiple other jurisdictions, including Singapore, Hong Kong and Australia. Systems that will need to be able to handle multiple cross-border trades and multi-jurisdiction compliance at a highly intricate level will need to be running and fully functional well before essential inputs from major jurisdictions are available.

New Complexity for September 2016, Additional Adjustments in 2017. Because of the EU delay, systems will now need to be adjusted at least twice: first to remove inputs required by the EU margin rules that were built in before the EU announced its delay, and again later to incorporate the finalized EU margin rules (the content of which is currently uncertain). These repeated adjustments will be extremely disruptive for affected firms at many levels, including compliance, modeling, operations, documentation, negotiation, portfolio reconciliation and dispute resolution. With each adjustment, tests will have to be run to check for robustness at each stage. The requested relief from the US Regulators will spare firms the costs of at least one extra implementation round.

Additional Documentation Requirement. Similar uncertainty and increased complexity will apply to the documentation process. The documentation executed for Phase I Firms in September will subsequently need to be amended to meet EU requirements when the EU margin rules become final. As a result, CSEs will need to go through an extra set of amendments for all applicable documentation. To the extent there are conflicts between the final EU margin rules and the US margin rules, such inconsistencies will have to be addressed.

Additional Netting Sets. Differences in timing between implementation dates under the EU margin rules and the US margin rules will also lead to multiple netting sets, further complicating the task of collecting and monitoring margin. If the US IM rules take effect starting on September 1, 2016, and the EU IM rules take effect starting on June 1, 2017, then the netting set for IM for swaps entered into between September 1, 2016 and June 1, 2017 is likely to be a different set than the one for swaps entered into after June 1, 2017 because these pre-June 1, 2017 swaps would otherwise become subject to EU IM requirements. The result is potentially three netting sets: one for swaps executed before September 1, 2016, one for swaps executed between September 1, 2016 and June 1, 2017 (subject to US margin rules but not EU margin rules), and a third for swaps executed after June 1, 2017 (subject to both US margin rules and EU margin rules).

3. <u>Level Playing Field</u>

The market will respond to the EU delay by seeking out the most cost-effective trades. It will become more cost-effective for EU firms to trade with counterparties that are Delayed Entities rather than to trade with counterparties that are Subject Entities due to the discrepancies in margin amounts required to be transferred. In addition, Subject Entities will face significant rises in costs overall due to the complexity caused by the EU delay, as discussed above, while Delayed Entities will not face similar cost increases. Delayed Entities will be able to price transactions at lower rates than their US competitors, resulting in the market fragmentation mentioned previously. As a result, Subject Entities will face a significant competitive disadvantage relative to Delayed Entities.

The competitive disadvantage faced by Subject Entities will be particularly pronounced for foreign CSE subsidiaries of US firms that are active in the EU. These subsidiaries will be competing directly with EU counterparties which, when facing other EU entities, will not be subject to EU margin rules. The asymmetry in these situations will deter EU firms from entering into trades with these CSE subsidiaries. Additionally, insofar as affiliates of banks from non-EU and non-US jurisdictions can trade within the EU without being subject to margin rules from their home jurisdictions, the competitive disadvantage for Subject Entities will be even more pronounced.

ISDA will submit additional data regarding market fragmentation as soon as possible.

4. Global Harmonization

A key principle of the BCBS/IOSCO Framework is that "[r]egulators should undertake a coordinated review of the margin standards once the requirements are in place and functioning to assess the overall efficacy of the standards and to ensure harmonisation across national jurisdictions as well as across related regulatory initiatives."[5] The US Regulators have themselves emphasized the importance of alignment – for example, in his opening statement in September 2014, Chairman Massad observed that "[t]he importance of international harmonization cannot be understated. It is particularly important to reach harmonization in the area of margin for uncleared swaps, because this is a new requirement and we do not want to create the potential for regulatory arbitrage in the market by creating unnecessary differences."[6]

Cross-border harmonization will be significantly reduced if the EU and the US use different implementation dates. The WGMR process has produced margin rules that are largely consistent across major jurisdictions, including with respect to timing, and relief from the US Regulators will help preserve this consistency.

Finally, not only would relief from the US Regulators help protect global harmonization, it may allow the Securities and Exchange Commission (the "**SEC**") time to issue its final margin rules for security-based swap dealers, allowing for harmonization in implementation timing across the PRs, the CFTC and the SEC rules, which may alleviate product scope coverage differences and would provide greater stability even in the domestic US market.

[5] BCBS/IOSCO Framework p. 5.

[6] Opening Statement of Chairman Timothy G. Massad, Open Meeting on Proposed Rule on Margin Requirements for Uncleared Swaps and Final Rule on Utility Special Entities. September 17, 2014. Available at: http://www.cftc.gov/PressRoom/SpeechesTestimony/massadstatement091714.

Conclusion:

The EU delay will result in market dislocation, disruption of cross-border trading, concentration of counterparty risk, new implementation challenges, and severe reduction in the ability of Subject Entities to compete in the global market. ISDA requests relief from the US Regulators to mitigate the negative effects of the EU delay, and to allow for a more robust and efficient margin implementation process that will benefit the global markets in the long term.

It is critical that ISDA members know as soon as possible whether the requested relief will be provided, so we would appreciate a swift response.

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Thank you for your consideration, and please contact me if you have any questions.

Sincerely,

Mary P. Johannes
Senior Director and Head of ISDA WGMR Initiative
International Swaps and Derivatives Association, Inc. (ISDA)
1101 Pennsylvania Avenue, NW, Suite 600, Washington, DC 20004
+1 202-756-4541 (o)
+1 646-732-6625 (m)
mjohannes@isda.org

Appendix I

GLOBAL MARGIN RULES FOR UNCLEARED DERIVATIVES

Cost Impact – The Small Picture

Trade Example 1: 7yr USD Zero-Coupon CPI Inflation Swap		Trade Example 2: 10yr EUR Fixed-Floating Swap		Trade Example 3: Sell 4y CDX HY Index	
Trade Size	$10mm	Trade Size	$10mm	Trade Size	$10mm
DV01	$6,800/bp	DV01	$7,500/bp	DV01	n/a
Transaction Cost*	1bp	Transaction Cost*	0.25bp	Transaction Cost*	.125 points
SIMM IM	$217,000	SIMM IM	$240,000	SIMM IM	$740,000
Annual IM Cost**	$4,340	Annual IM Cost**	$4,800	Annual IM Cost**	$14,800
Annual IM Cost in bps	0.74	Annual IM Cost in bps	0.64	Annual IM Cost in points	0.15
SIMM/Transaction Cost	64%	SIMM/Transaction Cost	256%	Annual SIMM/Transaction Cost	120%

* (Offer – Bid)/2

** Assuming 2% cost of funds

- In Example 1, the cost to a European bank of trading with a US bank is 64% higher vs. trading with another European bank
- In Example 2, the cost is 256% higher
- In Example 3, the cost is 120% higher
- The longer the inconsistency in rules remains, the larger this problem becomes

Annex I

ADDRESSES

Legislative and Regulatory Activities Division Office of the Comptroller of the Currency 400 7th St, SW, Suite 3E-218 Mail Stop 9W-11 Washington, D.C. 20219 cc: Jamey Basham	Alfred M. Pollard, General Counsel Federal Housing Finance Agency Constitution Center (OGC Eighth Floor) 400 7th St, SW Washington, DC 20024
Robert deV. Frierson, Secretary Board of Governors of the Federal Reserve System 20th Street and Constitution Avenue, NW Washington, DC 20551 cc: Sean D. Campbell	Barry F. Mardock, Deputy Director Office of Regulatory Policy Farm Credit Administration 1501 Farm Credit Drive McLean, VA 22102-5090
Robert E. Feldman, Executive Secretary Federal Deposit Insurance Corporation 550 17th Street, NW Washington, DC 20429 cc: Bobby Bean	Christopher Kirkpatrick Secretary of the Commission Commodity Futures Trading Commission Three Lafayette Center, 1155 21st St. NW Washington DC 20581