Kramer Levin

How much margin to post? That depends on your swaps exposure

In order to better manage risk in the swaps market, the U.S. prudential regulators (PR) and the CFTC each issued final rules requiring covered swap dealers to collect and (in some cases) post both initial and variation margin for certain noncleared swaps. Investment funds trading noncleared swaps with such dealers may thus face new margin requirements, depending largely on whether or not a fund has "material swaps exposure" (MSE).

Fund with MSE

Initial margin

Covered swap dealers must *collect and post* amount required by rule or approved margin model (except under CFTC rules, which do not impose collection requirements on any fund that is an affiliate of the dealer).

Threshold of up to $50M permitted between covered swap dealer and a fund (and their respective affiliates) (but only $20M under PR rule when the fund is an affiliate of the dealer).

Segregation with third-party independent custodian required, subject to limited exceptions for affiliates.

Variation margin

Covered swap dealer must *collect and post* mark-to-market amounts daily.

No threshold permitted.

No segregation required.

Once the final rules are effective for a fund, if a fund exceeds the MSE threshold based on June, July and August of the previous calendar year, then the stricter margin requirements applicable to a fund with MSE will apply *only for trades entered into after the change in status is effective,* on Jan. 1 of the following year.

Material Swaps Exposure > $8B*

If a fund no longer has MSE based on June, July and August of the previous calendar year, then the less-strict margin requirements will apply for all trades, *including any outstanding trades at the time the change in status is effective.*

Fund without MSE

Initial margin

Covered swap dealers must *collect only* at times and in forms/amounts the dealer determines under the PR rule. No related requirement under CFTC rule.

Threshold of up to $50M permitted between covered swap dealer and a fund (and their respective affiliates) (but only $20M under PR rule when the fund is an affiliate of the dealer).

No segregation required for margin posted by fund.

Variation margin

Covered swap dealers must *collect and post* mark-to-market amounts daily.

No threshold permitted.

No segregation required.

Collateral and haircuts

Eligible collateral includes G11 currencies and certain liquid equity and debt securities. Noncash collateral will have specified haircuts applied based on a table in the final rule. An 8% cross-currency haircut applies in certain circumstances.

* A fund has **material swaps exposure** if it (combined with its affiliates) has an average daily aggregate notional amount of non-cleared swaps, foreign exchange forwards and foreign exchange swaps for June, July and August of the previous calendar year (calculated only for business days and counting affiliate trades only once) exceeding $8B.

Minimum transfer amount

Parties to one or more noncleared swaps may agree that a covered swap dealer will not be required to collect or post margin unless the combined initial and variation margin required exceeds $500,000 (or a lesser agreed-upon amount).

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