Standard Chartered

Margin Reform

The rules and their impact

2016

Here for good

What are the new Margin Requirements?

New rules

- The new rules will require all financial firms and systemically important non-financial entities (“covered entities”) to exchange initial and variation margin for non-centrally cleared derivatives.
- Variation margin collateralises the current exposure from changes in the mark-to-market value of the contract. The amount of variation margin reflects the size of this current exposure. Initial margin collateralises the potential future exposure that could arise from changes in the mark-to-market value of the contract during the time it takes to close out and replace the position in the event that a counterparty defaults.
- The methodologies for calculating initial and variation margin, the assets that can be used as collateral, and how and when margin has to be exchanged are all prescribed by the rules.
- EU Financial Counterparties (FCs) and Non-Financial Counterparties over the clearing threshold (NFC+s) must exchange margin with all covered entities, regardless of their jurisdiction. Standard Chartered Bank will have to exchange margin with both EU and non-EU firms. Note, covered entities do not include the vast majority of corporate end users.
- Some – but not all - jurisdictions will develop their own margin rules. Many G20 jurisdictions will do so, as they were signatories to the international commitment to reform derivative markets after the financial crisis.

Which OTC derivatives need to be margined

- Margin is required for all non-centrally cleared OTC derivatives, with some limited exceptions for FX derivatives. Broadly, most OTC derivatives that are not cleared on either a voluntary or a mandatory basis will be subject to the margin rules.

What are the implementation deadlines?

- Compliance dates are determined by the calculation of the Average Aggregate Notional Amount (AANA) of all the uncleared OTC derivatives that a group transacts. The calculation includes all uncleared derivatives, even those for which margin may not have to be exchanged under the new rules. Page 3 illustrates the timetable in more detail.
- Only new non-cleared derivative trades are subject to the Margin Requirements. Existing trades prior to implementation deadlines are exempt.

Margin reform - Initial and Variation Margin

Initial Margin (IM)

- Reflects potential future exposure of the portfolio
- Two thresholds must be met before exchange is required
- IM threshold per group: US $50m/ EU €50m
- Exchanged ‘gross’ – both parties must post to each other
- Calculated at regular intervals and at least every 10 days, collected on a T+1 basis
- Held in a segregated third party custodian account and cannot be re-hypothecated
- Amount calculated either via Initial Margin Model (SIMM) or standardised tables. SIMM is subject to regulatory approval in many jurisdictions

Variation margin (VM)

- Reflects the current exposure of the portfolio
- Zero threshold
- Calculated and collected on a T+1 basis
- Re-hypothecation permitted

- Both IM and VM must be collected and posted – i.e. counterparties exchange margin.
- There is a minimum transfer amount of $/ € 500k which can be shared across IM and VM.

What do you need to do next?

Rule application

- Find out if margin rules have been developed in your own jurisdiction. They may have been produced by your prudential or your markets regulator, or both. For an indicative list of jurisdictions that have or will implement margin rules, please see page 6 – but bear in mind that the list is not exhaustive, and you need to check locally.
- Review if and how you may be subject to the new rules. Consult your legal and compliance teams to make sure you understand what you need to do to be compliant. If you are a financial counterparty, and your jurisdiction has implemented its own rules, you are likely to be in scope. You may also be in scope if you are not a financial counterparty. Your counterparties may require you to exchange collateral even if you are not subject to any local rules directly. This will be the case for European FCs and NFC+s, who have to exchange margin with all in-scope counterparties, regardless of where they are domiciled.

AANA thresholds and disclosures

- Determine which entities form a part of your consolidated group, and calculate your AANA for the prescribed dates to determine how you are affected by the phasing-in of the rules.
- Engage with your counterparties to disclose this information, particularly the AANA threshold.
- Consider using the ISDA Amend self-disclosure service as it becomes available. This will allow you to share and disclose your details once to all your counterparties who use it, rather than make individual notifications.

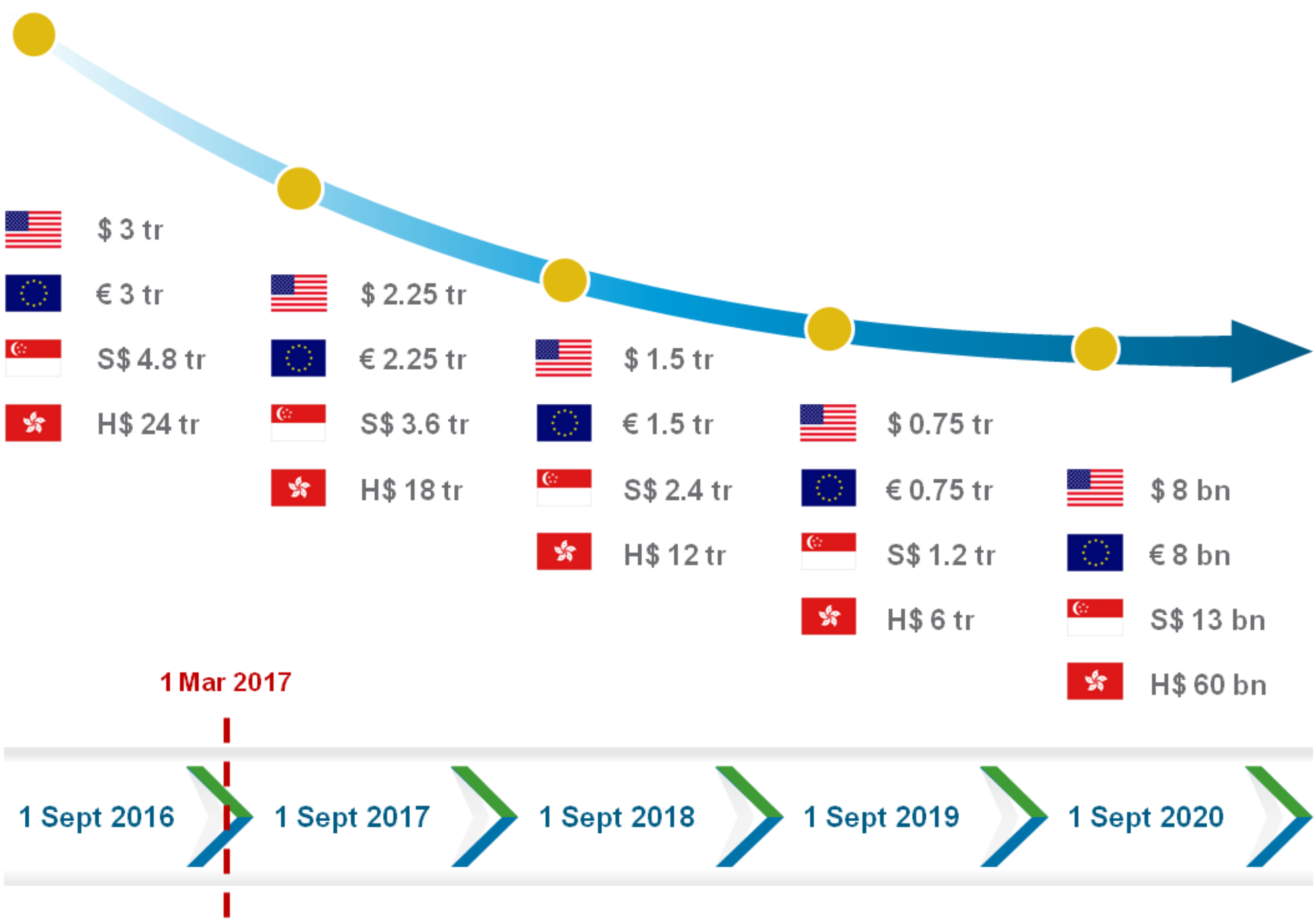
Legal and documentation

- Talk to your legal team to consider the relevant trading documentation you may need to put in place to allow you to exchange margin. This may mean you need to have an ISDA Master Agreement and/or a new regulatory-compliant Credit Support Agreement (CSA). If you trade under an ISDA Master and an existing CSA already, you will still need a new CSA. You should consider if you will want to use the ISDA Amend Protocol as it becomes available.
- If you are in scope for initial margin, you will need to sign additional documentation with your counterparties and with custodians.
- Legal documentation takes time to negotiate across all multiple trading counterparties. You will avoid bottlenecks by starting early.

Timelines – IM Sept 2016, VM March 2017

- The initial margin rules take effect when both counterparties in a trading pair exceed the AANA threshold. For EU Financial Counterparties such as Standard Chartered Bank, the first calculation period is March, April, May 2016, to determine eligibility for 1 September 2016. All groups that are over the €3 trillion AANA threshold this year will be in the first phase of implementation, starting from 1 September. They must also exchange variation margin from the same date.
- All other in-scope firms must begin to exchange variation margin from 1 March 2017. Initial margin is phased in over the next four years, based on the AANA threshold – again, both counterparties must be over the threshold for initial margin to be exchanged.
- Each counterparty will need to disclose when it expects to breach the AANA thresholds as prescribed by the rules. It will also need to disclose whether it is subject to the rules, and in which jurisdiction. Other disclosures may be needed, based on the applicable regulatory regime/s.

IM phase-in by AANA threshold



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Margin Reform globally

Jurisdiction*	Status	Go Live	Further Information
Global	Final		Margin requirements for non-centrally cleared derivatives
Canada	Final	1 Sept 2016	OSFIC - Margin Requirements for Non-Centrally Cleared Derivatives
EU	Draft	1 Sept 2016	Final Draft Regulatory Technical Standards on risk-mitigation techniques for OTC-derivative contracts not cleared by a CCP - March 2016
Switzerland	Final	1 Sept 2016	Federal Act on Financial Market Infrastructures and Market Conduct in Securities and Derivatives Trading
US	Final	1 Sept 2016	Federal Reserve PR - Margin and Capital Requirements for Covered Swap Entities CTFC Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants
Australia	Draft	TBC	APRA - Margining and risk mitigation for non-centrally cleared derivatives
Hong Kong	Draft	TBC	HKMA consultation paper Dec 2015
Japan	Final	1 Sept 2016	JFSA - English translation of final Japan margin rule announced on 31 Mar 2016
Singapore	Draft	TBC	Policy Consultation on Margin Requirements for Non-Centrally Cleared OTC Derivatives
South Africa	Draft	TBC	Treasury RSA - Regulating OTC Derivative Markets in South Africa
Taiwan	Draft	TBC	Taiwan – Financial Supervisory Commission (Chinese) English Translation of Dec 29 2015 new measures

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