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ISDA RESPONSE TO CP5/25 – Margin Requirements for non-centrally cleared derivatives: Amendments to BTS 2016/2251

The International Swaps and Derivatives Association, Inc. (ISDA) appreciates the opportunity to respond to the joint consultation by the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) (jointly, the "regulators") **CP5/25** - **Margin Requirements for non-centrally cleared derivatives: Amendments to BTS 2016/2251.** ISDA supports the adoption of the proposed amendments while requesting some clarifications on the scope of application, as further explained below, and consents to the disclosure of this response.

Proposal 1 – Bilateral margin requirements for single-stock equity options and index options contracts

ISDA strongly supports the regulators' proposal to indefinitely exempt single-stock and index equity options from their bilateral margining requirements to reduce global market fragmentation, bolster UK hedging liquidity and eliminate the competitive disadvantage for UK firms.

ISDA has advocated with UK and EU authorities to enable harmonisation with other jurisdictions, notably the U.S., in which both single name and index options on equity underliers are excluded from margin requirements for non-cleared derivatives. Temporary exemptions have protected these markets from a migration of equity option trading to other jurisdictions. The EU's recent adoption of a permanent exemption under EMIR 3 has provided long-term certainty and upheld the competitiveness of the EU market.

The adoption of a permanent exemption for equity options in the UK will bring clarity and finality to foster equity derivatives trading which supports hedging of exposures, diversification of portfolios and convertible bond issuance for UK investors, pension funds and corporates. The permanent exemption will place UK dealers on a level-playing field with U.S. and EU dealers for transacting with non-UK clients and align with UK competitiveness and growth objectives introduced by the Financial Services and Markets Act 2023.

Proposal 2 – Amendments for legacy contracts for counterparties that fall under the AANA threshold

ISDA supports the regulators' proposal to remove the requirement for a counterparty to exchange IM for legacy contracts once its group level average aggregate notional amount (AANA) no longer exceeds the €8 billion minimum threshold established by BCBS and IOSCO in their *Margin Requirements for Non-Centrally Cleared Derivatives* ("Margin Framework"). This threshold is intended to limit the application of regulatory IM requirements to systemically important counterparties. Furthermore, the Margin Framework provides in section 8.11 that the application of "initial margin requirements to existing directives contracts is not required."

ISDA identified a discrepancy with the Margin Framework whereby the rules of the UK, EU, Singapore and Australia require the continued application of regulatory IM to derivatives transactions entered into during the period a counterparty was subject to IM requirements ("legacy contracts") even after the counterparty is no longer subject to IM for new contracts. This retention of IM requirements creates significant operational complexity and unnecessary costs to manage the isolated subset of transactions and puts entities in these jurisdictions at a competitive disadvantage. Moreover, it runs counter to the intention to mitigate systemically important derivatives exposures, and therefore, we agree with the conclusion of the regulators that the counterparties impacted by this amendment are not systemically important.

The regulators' recognition of ISDA's assessment of the matter is greatly appreciated. The proposed amendments would eliminate the impact of IM retention for legacy contracts for UK firms and their counterparties and further harmonize global regulatory requirements for non-cleared derivatives.

We note that the Proposal 2 amendment will facilitate harmonisation on the date when initial margin may both cease to be collected and may be returned in the event a portfolio is no longer subject to regulatory IM exchange as a result of the proposed disapplication of IM requirements to legacy transactions. We suggest that the FCA align the text in Article 28(1D) of its draft BTS 2016/2251 with the PRA's text which includes the clarifying acknowledgement of the ability to "release initial margin already collected."

ISDA requests the amendment to take effect immediately following their publication to allow time for firms to prepare accordingly before the January 1, 2026 compliance date for IM requirements.

Proposal 3 – Amendments to allow firms to align dates with other jurisdictions

ISDA supports the proposed amendments to permit UK firms to use another jurisdiction's threshold assessment calculation periods and dates of entry into scope of IM requirements when transacting with a counterparty subject to the margin requirements of another jurisdiction. Global harmonization of these dates is preferable, but in the alternative the proposed amendments will provide some mitigation for cross-border relationships impacted by AANA changes which affect IM application. To understand the potential limitations of the proposed amendments, we request clarification on their intended application to certain scenarios, as discussed below.

Date of Entry into Scope

Although the UK margin requirements are substantively aligned with the Margin Framework, they differ regarding the application date of IM requirements resulting from a change in status following an annual AANA assessment in which a group of counterparties newly exceeds or falls below the EUR 8 billion minimum threshold for application of regulatory IM requirements. The UK is not alone in its deviation but is among the minority[1].

The Margin Framework specifies a September 1 application date following the AANA calculation assessed at month-end for March, April and May of the same year. Although we recognize the value of the additional preparation time afforded by a compliance date on January 1 of the following year, our members believe this benefit is outweighed by the complexity of managing different application dates among jurisdictions.

To ensure the scope and limitations of the proposed amendment are understood by UK firms and their counterparties, we request clarification on whether the entry into force date of the counterparty's jurisdiction would be allowed in the following instances:

- A counterparty is indirectly caught by the margin rules of its local jurisdiction. For instance, only swap dealers are subject to non-cleared margin requirements in the US, but their domestic counterparties are required to calculate AANA based on the US rules.
- A UK entity transacts with another UK entity that also has a regulatory margin obligation in another jurisdiction. For instance, a UK entity whose obligations are guaranteed by a U.S. Person or the London branch of a foreign entity. If that counterparty was no longer subject to the IM requirements in the other jurisdiction as of September 1, the parties might otherwise still have to continue IM application in the UK until the following January 1.

[1] AANA Calculation Periods and Compliance Dates

If these scenarios are not covered by the amendments, then it would only be relevant for firms directly subject to both foreign and UK margin rules, limiting its ability to resolve some cross-border relationships impacted by the discrepancy of entry into force following a change to IM application.

AANA Calculation Period

The UK's AANA assessment period is aligned with the Margin Framework, but that is not the case for all jurisdictions, compounding the potential for operational complexity, misalignment and dispute. The flexibility provided by the proposed amendment may mitigate these challenges while ISDA continues to engage with other regulators to promote further harmonisation.

We understand that the proposed amendment intends only to allow use of the counterparty's AANA assessment period and not the other aspects of that jurisdictions AANA calculation requirements, including the method (i.e. daily vs. month-end averaging), threshold amount and product scope). If that's the case, then in order to benefit from the amendment, the counterparty would need to conduct an additional hybrid AANA calculation, adding effort and complexity which may limit its value.

We appreciate the regulators' recognition of the impact created by these discrepancies and support the proposed amendments which will alleviate the associated risk and burden by allowing UK firms to align the dates relevant to IM application with their counterparty in certain cases. Nonetheless, we request your consideration of the scenarios explained above on the basis that the relief may otherwise be limited. In either event, clarification on the scope and limitations of the amendments will be useful for implementation.

ISDA requests the amendments to take effect immediately following their publication to allow time for firms to prepare accordingly before the next AANA calculation period or compliance date for IM requirements in the relevant jurisdiction(s).

Thank you for consideration of our responses. For questions regarding this response, please contact **Tara Kruse** (**tkruse@isda.org**).