ISDA Publishes 2016 Credit Support Annex for Variation Margin

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PRACTICES Finance, Commodities, Financial Regulatory

On April 14, 2016, the International Swaps and Derivatives Association, Inc. ("**ISDA**") published a new version of Credit Support Annex to help market participants comply with new margin requirements for uncleared swaps. The 2016 Credit Support Annex for Variation Margin (the "**2016 VM CSA**") is intended to be used with New York law ISDA Master Agreements and is the first in a series of documents to be published by ISDA over the next few months to facilitate compliance with uncleared swap margin requirements coming into effect in several different jurisdictions.

Background

Following the financial crisis, the Basel Committee on Banking Supervision and the International Organization of Securities Commissions ("**BCBS/IOSCO**") jointly established a new set of minimum standards for margin requirements for non-centrally cleared derivatives (the "**BCBS/IOSCO Margin Requirements**") . Regulators in several jurisdictions including the U.S., the European Union and Japan have since published rules to implement their own versions of the BCBS/IOSCO Margin Requirements in their respective jurisdictions.

In the U.S., final uncleared swap margin rules were published in October 2015 (for entities subject to the jurisdiction of U.S. prudential banking regulators) and in December 2015 (for entities subject to the jurisdiction of the U.S. Commodity Futures Trading Commission ("**CFTC**")); the U.S. Securities and Exchange Commission ("**SEC**") has not yet published its own set of final uncleared swap margin rules but is expected to do so in the near future. In March 2016, regulators in Japan published final uncleared swap margin rules and regulators in the European Union also published final draft regulatory technical standards for collateralization of uncleared swaps.

Although the final rules issued by each regulator vary as to certain details, as a general matter, the new requirements for collection and/or posting of variation margin and initial margin will become effective for the largest derivatives users (based on volume of uncleared swap transactions) as of September 1, 2016. Variation margin requirements for other covered entities will become effective as of March 1, 2017, while initial margin requirements for other covered entities will be phased in over a four-year period. As such, swap dealers and their counterparties will need to prepare for the new rules in order to ensure they are in compliance prior to the relevant effective dates.

2016 VM CSA

The 2016 VM CSA contains significant revisions from its predecessor, the 1994 Credit Support Annex (New York law). The 2016 VM CSA follows the same overall documentation architecture of the 1994 Credit Support Annex by supplementing, forming part of, and constituting a "Credit Support Document" under, the ISDA Master Agreement. Margin delivery and return amount calculation and transfer mechanics are set forth in a broadly similar pre-printed standard form annex, subject to modification for individually negotiated elections and variables in Paragraph 13 thereof.

Because the 2016 VM CSA only addresses variation margin requirements and contemplates use of a separate Credit Support Annex to address initial margin requirements (if applicable), however, significant changes have been made to various calculations and defined terms to reflect such bifurcation. Other modifications have been made to comply with additional regulatory requirements regarding variation margin, such as changes to eligible collateral types, valuation haircuts, dispute resolution procedures and interest payments. The 2016 VM CSA also now contemplates a certain subset of transactions being designated as “covered transactions” while other transactions would be excluded, to permit the 2016 VM CSA to be used only for in-scope transactions and parties under the applicable rules.

In addition to the 2016 VM CSA, ISDA also plans to publish a form of New York law Credit Support Annex for Initial Margin, as well as forms of English law and Japanese law credit support documents for variation margin and initial margin, and a set of Protocol documents to allow parties to amend existing ISDA documentation to comply with the new rules in a manner similar to previous ISDA Protocols. As with other ISDA and derivatives agreements, parties may also modify or use customized documentation along with or in place of these templates to comply with the new uncleared swap margin rules. ISDA also has an internal group working on developing a new Standard Initial Margin Model (“**SIMM**”) to provide a regulatory-compliant model for initial margin calculations.

Given the complexity of the new margin rules, the number of documentation and compliance initiatives underway and the updates or amendments that may be needed to ensure proper compliance, market participants should continue to monitor developments in this area. For more information on the margin requirements for uncleared swaps, the 2016 VM CSA or any of the other new documents or initiatives regarding variation margin or initial margin, please contact one of the lawyers listed below.

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[1] Basel Committee on Banking Supervision and International Organization of Securities Commissions, “Margin Requirements for Non-Centrally Cleared Derivatives,” March 2015 (originally published September 2013). The BCBS/IOSCO Margin Requirements were published by BCBS/IOSCO in consultation with the Committee on Payment and Settlement Systems and the Committee on the Global Financial Systems (collectively known as the “Working Group on Margining Requirements” or “WGMR”).