Commodity Futures Trading Commission
Office of Public Affairs
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581
www.cftc.gov

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Fact Sheet - Proposed Rules Regarding Capital Requirements of Swap Dealers and Major Swap Participants

The Commodity Futures Trading Commission (Commission) is proposing rules to implement its capital requirements for swap dealers and major swap participants.

Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act)

The Commission is proposing rules to implement sections 4s(e) and (f) of the Commodity Exchange Act, as added by section 731 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). Section 4s(e) requires the Commission to adopt capital requirements for swap dealers (SDs) and major swap participants (MSPs) that are not subject to prudential regulation ("Covered Swap Entities").[1] The Commission previously proposed SD and MSP capital requirements in 2011, but as global consultation on appropriate margin standards for uncleared swaps was still proceeding, no further action was taken. As the Commission's margin requirements are now final and being implemented, the Commission is re-proposing capital standards for Covered Swap Entities. The Commission has consulted with the prudential regulators as well as with the Securities and Exchange Commission (SEC) in developing the proposed capital rules. The proposed rules also address the capital requirements of any Covered Swap Entities that may also be registered as futures commission merchants (FCMs).

Proposed Capital Requirements

The proposed rules address a Covered Swap Entity's qualifying capital and the minimum levels of such qualifying capital that the Covered Swap Entity would be required to maintain. The proposal would also include amendments to existing Commission regulations governing FCM capital requirements. The proposed rules also address when internal models may be used for purposes of the required capital calculations.

- SDs and MSPs that are also FCMs. Covered Swap Entities that are dually-registered as FCMs would be required to meet existing FCM requirements to hold minimum levels of adjusted net capital, which include amendments to establish market and credit risk charges specifically applicable to swaps and security-based swaps. Such Covered Swap Entities would be required to maintain a minimum amount of adjusted net capital that is equal to or greater than the greatest of: (1) $20 million; (2) 8 percent of the margin required on cleared and uncleared swaps, security-based swaps, futures and foreign futures positions carried for customers and 8 percent of the margin required on the Covered Swap Entities' cleared and uncleared swaps and security-based swap positions; or (3) the amount of capital required by the National Futures Association (NFA). The Commission also is proposing to permit these Covered Swap Entities to use approved internal models to calculate market and credit risk capital charges in lieu of rules-based standardized capital charges. Covered Swap Entities approved to use models would be required to maintain capital of $100 million prior to the imposition of market risk and credit risk capital charges. In addition, the proposal provides that SDs that are registered with the SEC as brokers or dealers and are already approved by the SEC to use capital models as Alternative Net Capital firms will be permitted to continue to follow existing capital requirements set by the SEC.

- SDs that are not FCMs. These SDs would be permitted to elect one of two approaches to computing their regulatory capital. The first approach is based upon the capital requirements adopted by the prudential regulators for banking

[1] The "prudential regulators" are defined in the Dodd-Frank Act as the Federal Reserve Board, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Farm Credit Administration, and the Federal Housing Finance Agency.

entities. The second approach is a net liquid asset capital standard that is consistent with the SEC's proposed security-based swap dealer capital. Under the bank-based approach, an SD would have to maintain a minimum level of capital equal to or greater than the greatest of: (1) $20 million of common equity tier 1 capital; (2) common equity tier 1 capital equal to or in excess of 8 percent of the SD's risk weighted assets; (3) common equity tier 1 capital equal to or greater than 8 percent of the margin required on the SD's cleared and uncleared swaps, security-based swaps, futures and foreign futures positions; or (4) the amount of capital required by the NFA. Under the net liquid asset approach, and SD would have to maintain a minimum level of adjusted net capital equal to or greater than the greatest of: (1) $20 million; (2) 8 percent of the margin required on the SD's cleared and uncleared swaps, security-based swaps, futures and foreign futures positions; or (3) the amount of capital required by the NFA.

- SDs predominantly engaged in non-financial activities and MSPs. In addition to the bank-based and net liquid asset-based approaches, SDs that are predominantly engaged in non-financial activities would have the ability to meet a tangible net worth capital requirement provided the SD's financial assets are not more than 15 percent of its consolidated assets and its revenues from financial activities are not more than 15 percent of its consolidated revenues. An SD's tangible net worth generally would be based on net equity as determined under U.S. Generally Accepted Accounting Principles, adjusted to exclude certain intangible assets such as goodwill. An SD qualifying to use the tangible net worth approach would need to meet a minimum capital requirement of the greater of: (1) $20 million plus market and credit risk charges on its swaps positions that are related to its dealing activities; (2) 8 percent of the margin required on the SD's cleared and uncleared swaps, security-based swaps, futures and foreign futures positions; or (3) the amount of capital required by the NFA.

  MSPs must maintain positive tangible net worth or the minimum amount of capital required by the NFA.

Application for Approval of Internal Models

Under the proposed rules, a Covered Swap Entity may apply to the Commission or to the NFA for approval to use internal models for purposes of computing its regulatory capital. The capital models must meet proposed qualitative and quantitative requirements that are similar to existing qualitative and quantitative requirements set forth in the capital rules of the prudential regulators and the SEC.

Liquidity Requirements

Under the proposed rules, SDs that elect the bank-based and the net liquid asset capital approaches would be subject to liquidity requirements. For SDs electing the bank-based approach the liquidity requirement is based on the requirements established by the prudential regulators. For SDs electing the net liquid asset approach the liquidity requirement is based on proposed SEC liquidity requirements. The liquidity requirements are designed to address the potential risk that an SD may not be able to efficiently meet both expected and unexpected current and future cash flow and collateral needs as a result of adverse events impacting the SD's daily operations and financial condition.

Financial Reporting, Recordkeeping and Notification Requirements

The proposed rules would require Covered Swap Entities to report monthly financial statements and keep current books and records in accordance with U.S. Generally Accepted Accounting Principles, or if permitted, in accordance with International Financial Reporting Standards.   In addition, Covered Swap Entities will be required to submit annual certified financial reports with an opinion expressed by an independent certified public accountant.   SDs and MSPs subject to a prudential regulator will be required to submit certain quarterly financial information to the Commission. All SDs and MSPs will be subject to certain notification requirements pertaining to the changes in the respective capital positions and will be required to provide weekly position and margin information.