

# PS11/22 – Margin requirements for non- centrally cleared derivatives: Amendments to BTS 2016/2251

PRA Policy Statement 11/22 | FCA Policy Statement 22/16

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# 1. Overview

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1.1 This Prudential Regulation Authority (PRA) and Financial Conduct Authority (FCA) Policy Statement (PS) provides feedback to responses to [Consultation Paper \(CP\) 11/22 — ‘Margin requirements for non-centrally cleared derivatives: Amendments to BTS 2016/2251’](#). It also contains the PRA’s and FCA’s final policy, in the form of amendments to Binding Technical Standards (BTS) 2016/2251.

1.2 This PS is relevant to PRA-authorised firms that are financial counterparties for the purposes of Article 2 of the European Market Infrastructure Regulation (UK EMIR).[1] In addition, this PS is relevant to all FCA solo-regulated entities and non-financial counterparties in scope of the margin requirements under UK EMIR.

## Background

1.3 In CP11/22, the PRA and FCA proposed to:

- specify the treatment of third-country funds as eligible collateral, including European Economic Area (EEA) Undertakings for Collective Investment in Transferable Securities (UCITS);
- provide a fall-back transition period to address practical issues where firms face immediate application of the bilateral margining requirements; and
- update the criteria for a central counterparty (CCP) to be excluded from the requirements.

## Summary of responses

1.4 The PRA and FCA received two responses to the CP. The responses were generally supportive of the proposals on the treatment of third-country funds as eligible collateral. They were also supportive of the proposed criteria for a CCP to be excluded from the margin requirements. Respondents made a number of observations and requests on the proposals for providing a fall-back transition. These are set out in Chapter 2.

## Changes to draft instrument

1.5 The PRA and FCA consider that the differences between the final Technical Standards and the draft consulted in CP11/22 are not significant.[2]

1.6 In response to the comments made during the consultation, the PRA and FCA have made a change to the transition period to extend the eligibility of EEA UCITS as collateral. The specific change and rationale are set out in Chapter 2. The PRA and FCA consider that providing firms who have to apply new requirements on the treatment of third-country funds as eligible collateral

with a longer implementation period will give certainty to market participants in the short term.

1.7 The PRA and FCA have also made a change to increase the fall-back transition period for circumstances where firms come into scope of the margin requirements for the first time, and the rules would otherwise apply immediately. This is discussed in more detail in Chapter 2.

1.8 The impact from the two changes outlined above is not anticipated to be any different for mutuals.

1.9 When making rules, the PRA and FCA are required to comply with their duties in the Financial Services and Markets Act 2000 (FSMA), including considering responses to consultation and publishing an explanation of the PRA's and FCA's reasons for believing that making the proposed rules is compatible with their objectives and with their duty to have regard to the regulatory principles.<sup>[3]</sup> In CP11/22, the PRA set out this explanation in Chapter 3 'The PRA's statutory obligations', and in Chapter 2 of this PS, the PRA and FCA have provided an updated explanation to take into account consultation responses.

1.10 The PRA and FCA consider the final rules have taken into account concerns raised by respondents and considers the final rules continue to support the have regards on 'proportionality'. The PRA and FCA consider the responses to the consultation did not significantly affect their consideration of the matters to which they must have regard in implementing these proposals, though it should be noted that some responses to the consultation were not taken forward as they were not assessed to be proportionate. These responses are noted further below.

1.11 The PRA and FCA have considered the equality and diversity issues that may arise from the final rules in this PS. The PRA and FCA do not consider that the changes materially impact any group with protected characteristics under the Equality Act 2010.

1.12 The PRA and FCA have taken into account the impact of the final rules on their cost benefit analysis (CBA). In the consultation, no feedback was received on the CBA. Furthermore, the PRA and FCA do not consider the limited changes to the final rules would result in any material changes to their original CBA. The main impact would potentially be the higher indirect costs of firms not having the benefit, and therefore the protection, of margining for a longer period due to the extended transition period. Still, these changes would not materially impact the estimates set out in their original CBA; therefore, the PRA and FCA consider that the CBA as consulted on remains appropriate.

## **Implementation and next steps**

1.13 The requirements will be effective on publication of this PS, which is when the final technical standards instrument by the PRA and FCA comes into force.

1.14 Unless otherwise stated, any remaining references to EU or EU-derived legislation refer to the version of that legislation which forms part of retained EU law.[4]

## 2. Feedback to responses

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2.1 Before making any proposed technical standards, the PRA and FCA are required by FSMA to have regard to any representations made to them, and to publish an account, in general terms, of those representations and their feedback to them.[5]

2.2 The PRA and FCA have considered the responses received to the CP. This chapter sets out the PRA's and FCA's feedback to those responses, and final decisions.

2.3 The sections below have been structured broadly along the same lines as the chapters of the CP. The responses have been grouped as follows:

- List of instruments as eligible collateral;
- Fall-back transitional provisions; and
- Application of the margin requirements to CCPs.

### List of instruments as eligible collateral

2.4 The PRA and FCA proposed to retain the expiry date of EEA UCITS as eligible collateral for meeting the margin requirements for non-centrally cleared derivatives. The PRA and FCA will instead update the list of eligible collateral to include funds from all third-countries that meet a set of principles and that only invest in otherwise eligible government securities and cash. Where firms accept third-country funds as collateral, the PRA and FCA expect firms to be able to demonstrate that they have completed the risk assessment that confirms a jurisdiction's legal framework for the relevant funds provides comparable risk management protections to those applied to UK UCITS.

2.5 All respondents were supportive of the proposal. Respondents requested that the PRA and FCA provide an extension to the expiry date of EEA UCITS as eligible collateral to allow firms to undertake the new risk assessment.

2.6 Having considered the responses, the PRA and FCA have decided to extend the transition provision for EEA UCITS by three months, until Friday 31 March 2023. This would allow firms to continue using existing eligible EEA UCITS as collateral while undertaking the risk assessment. The PRA and FCA consider that this extension will mitigate the practical challenge of firms having to undertake a new risk assessment in a short period of time. The PRA and FCA are also concerned that not extending the transition provision could unnecessarily restrict the supply of

eligible and relevant collateral.

2.7 As such, the PRA and FCA consider there will be no additional costs imposed on firms from the extension. The PRA considers the extension remains consistent with the PRA's primary and secondary objectives. The FCA considers that the extension will support its market integrity objective.

## **Fall-back transition provisions**

2.8 The PRA and FCA proposed to introduce a fall-back transitional provision of a six-month period for circumstances where firms come into scope of the margin requirements for the first time, and the rules would otherwise apply immediately. This is reflected in new Article 35B of BTS 2016/2251 (Transitional for establishment and validation of procedures).

2.9 All respondents supported the intention of the proposal. Respondents requested clarification on how the existing transition for Initial Margin (IM) would apply with the new fall-back transitional. Respondents noted the potential challenges of undertaking the process of assessing eligibility for the IM exemption in Article 28 of BTS 2016/2251 under the proposed transition period. Respondents requested a longer transition period for IM in all circumstances where firms come into scope of the margin requirements for the first time and the rules would otherwise apply immediately.

2.10 Respondents requested a minimum of 18 months transition period for circumstances where a firm's counterparty comes into scope of the margin requirements for the first time due to a change in netting status of a jurisdiction. Respondent commented that the appropriate transition period is dependent on particular circumstances (eg whether the jurisdiction has comparable margin requirements to UK EMIR or the relative sophistication of financial market participants). Given this, respondent suggested that the transition period for individual jurisdictions should be based on a principles-based approach instead of a set end-date for all jurisdictions.

2.11 Having considered the responses, the PRA and FCA have decided to amend the new Article 35B and apply two separate transitional provisions:

- Where firms come into scope of the margin requirements for the first time due to a change in the netting status of jurisdiction, the PRA and FCA have decided to extend the fall-back transitional provision to 12 months from the date they come into scope. For clarity and consistency with the statement in CP11/22, the PRA and FCA expect this date to be from the point a firm's individual assessment concludes that the netting agreements and operational arrangements for that firm will be legally enforceable in those jurisdictions, as required when entering into a netting, or exchange of collateral, agreement.
- For all other circumstances where firms come into scope of the margin requirements for the first time and the rules apply immediately, the PRA and FCA have decided to amend the fall-

back transitional provision to six months, or until the end of the calendar year, whichever period is longest from the date the firm first comes into scope. This is to align the transition period with the process of assessing eligibility for the Article 28 IM exemption.

2.12 The PRA and FCA consider the longer transition period in both circumstances will provide enough time for firms to address the operational challenges for establishing, and internally validating, margin arrangements that comply with the BTS's requirements where firms come into scope of the margin requirements for the first time. As such, the PRA and FCA consider there will be no additional material costs imposed on firms from these extensions.

2.13 The PRA and FCA consider the longer transition period will continue to ensure the margin requirements are applied proportionately, and that firms will have time to establish risk management procedures which meet margining requirements under UK EMIR. As such, the PRA considers the updated transition period remains consistent with the PRA's primary and secondary objectives. The FCA considers the updated transition period is consistent with its market integrity objective.

## Application of the margin requirement to CCPs

2.14 The PRA proposed to exempt non-centrally cleared trades with CCPs from the margin requirements where the CCP is recognised by the Bank of England (Bank), rather than authorised by the PRA as a credit institution. This exemption is limited to those trades that are linked to the CCP's recognised activities as specified in its recognition order.

2.15 All respondents were fully supportive of the proposal. Respondents requested the PRA to clarify that the obligations are for the CCP to confirm whether the CCP's activities are eligible/ineligible for exemptions.

2.16 After considering the responses, the PRA decided to maintain the draft policy as in CP11/22. The PRA considers that a number of obligations in the BTS require information provided by the counterparty to determine the applicable treatment. This will remain applicable here.

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1. Unless stated otherwise, all references to regulations, technical standards, and rules should be read as the UK versions.
  2. Sections 138J(5) and 138K(4) of FSMA.
  3. Section 138J(2)(d) FSMA for the PRA and section 138I(2)(d) FSMA for the FCA.
  4. For further information please see [Transitioning to post-exit rules and standards](#).
  5. Sections 138J(3) and 138J(4) FSMA for the PRA and Sections 138I(3) and 138I(4) FSMA for the FCA, and for both regulator these powers should be read as modified by section 138S FSMA.

## Appendices

 [PRA Standards Instrument: The Technical Standards \(Bilateral Margining\) Instrument 2022](#)  
(PDF 0.1MB)

 [FCA Standards Instrument: The Technical Standards \(Bilateral Margining\) Instrument 2022](#)  
(PDF 0.1MB)