BENEFITS PASSPORT

Updates and Information on International Benefits

BP 2012-05
October 8, 2012

Prepared by *Lynn Dudley, Senior Vice President, Policy*

AMERICAN BENEFITS COUNCIL

AMERICAN BENEFITS INSTITUTE

The American Benefits Institute is the education and research affiliate of the American Benefits Council. The Institute conducts research on both domestic and international employee benefits policy matters to enable public policy officials and other stakeholders make informed decisions. The Institute also serves as a conduit for global companies to share information about retirement, health and compensation plan issues.

LATEST DEVELOPMENTS ON MARGIN REQUIREMENTS FOR UNCLEARED SWAP TRADES

COUNCIL JOINS GLOBAL PENSION COALITION, WRITES U.S. AND INTERNATIONAL REGULATORS REGARDING MARGIN REQUIREMENTS FOR UNCLEARED SWAPS

The Council continues to pursue regulatory flexibility at the federal and international level with regard to the treatment of "swap" derivative trades, which are commonly used by defined benefit pension plans to hedge or mitigate risks endemic to plan liabilities and investments. Without the use of swaps, defined benefit pension funding obligations would become more volatile and force employers to find other less efficient ways to manage that risk — including setting aside large sums of cash to cover potential funding obligations.

On April 28, 2011, the U.S. Commodity Futures Trading Commission (CFTC) issued **proposed regulations regarding margin requirements for uncleared swaps**. Under these rules, ERISA plans would be treated as "high-risk financial end users," and, as such, would be required to post initial and variation margin (i.e., collateral). The proposed rules would also apply restrictions on the type of assets that plans may use to post margin.

The Council has joined with the Committee on Investment of Employee Benefit Assets (CIEBA), the European Federation for Retirement Provision (EFRP), the European Association of Paritarian Institutions (AEIP), the National Coordinating Committee for Multiemployer Plans (NCCMP) and the Pension Investment Association of Canada (PIAC) to form the Global Pension Coalition and write a series of letters to U.S. and international regulators expressing serious concerns about this rule.

In **a September 14 letter to the CFTC**, the coalition noted that "[u]nlike some other market participants that may take risks with derivatives for business and competitive reasons, pension plans do not have such business or competitive motivations and exist solely to provide retirement security for pensioners and utilize derivatives primarily to hedge market risks which could jeopardize such retirement security."

The letter also addressed the "prudential regulators," i.e., the Federal Housing Finance Agency, the Farm Credit Administration, the Office of the Comptroller of the Currency, the Federal Reserve System and the Federal Deposit Insurance Corporation with regard to their collective proposed regulations on Margin and Capital Requirements for Covered Swap Entities, issued May 11, 2011.

The coalition's letter makes a number of recommendations for re-proposal of these rules, including the incorporation of certain elements set forth in the Consultative Document Margin requirements for non-centrally-cleared derivatives, issued by the Working Group on Margining Requirements of the Basel Committee on Banking Supervision (BCBS) and the Board of the International Organization of Securities Commissions (IOSCO) in July (prompted by a 2011 agreement among G20 nations). ***Most significantly, the letter recommends that pension plans be excluded from any uncleared swap initital margin requirements in light of the lack of risk posed by pension plans.***

In **a September 28 letter to the BCBS and IOSCO**, the coalition reiterates the core point about pension plans and expresses gratitude "that the international regulators are seeking to coordinate their margin standards for uncleared swaps because we strongly believe that consistent international regulation of derivatives margining is essential to smooth and efficient markets."

While the coalition favors several elements set forth in the consultative document, as noted above, and "strongly encourages all regulators to incorporate the appropriate aspects of the final BCBS/IOSCO approach," the letter discusses at length the appropriateness of treating pension plans differently due to the lack of risk that they pose.

In light of the Consultative Document, the prudential regulators have reopened the comment period on their proposed rules on the margin requirements for uncleared swaps; the comment period will remain open until November 26, 2012.