

VIA CFTC PORTAL

2 November 2017

Mr Christopher Kirkpatrick
Commodity Futures Trading Commission
115 21st Street NW
Three Lafayette Centre
Washington DC 20581

LCH Limited Self Certification: rule changes on the use of FCM Buffer as Variation Margin

Dear Mr Kirkpatrick

Pursuant to CFTC regulation §40.6(a), LCH Limited ("LCH"), a derivatives clearing organization registered with the Commodity Futures Trading Commission (the "CFTC"), is submitting for self-certification changes to its rules regarding the payment of USD denominated Variation Margin by Futures Commission Merchants of its SwapClear service (thereafter "FCM Clearing Members").

Part I: Explanation and Analysis

LCH proposes to amend its rules to allow FCM Clearing Members to opt to use available buffer collateral to cover USD Variation Margin ("VM") requirements, in respect of the losses generated by their Customers' accounts. The amount of buffer collateral eligible for such use will be the amount not allocated to any specific Customer to cover ongoing initial margin liabilities, following the operation of existing processes to return excess funds to the FCM's buffer account at end of day. The "Eligible FCM Buffer" defined in the revised rules is the lesser of this amount, and the total VM loss incurred by the FCM Clearing Member in respect of its Customers' accounts. Any amount of VM that remains outstanding following the above payment shall remain payable by the FCM Clearing Member in accordance with the LCH Rulebook.

This is an optional service for FCM Clearing Members and once an election has been made it will be applied on each business day. LCH will require advance notice in the event a FCM Clearing Member wished to opt out of the service, in accordance with LCH rules.

The rule changes will go live on, or after, November 22, 2017.

Part II: Description of Rule Changes

A new section 4.9 titled "Treatment of Unallocated Excess and Return of FCM Buffer" has been added to Part 4 ("Collateral") of the FCM Procedures. A clarification that this section applies to FCMs of the SwapClear service has been added. Further, section 4.9 now includes a new paragraph "4.9.2 Use of FCM Buffer as Variation Margin", which sets out the process for FCM Clearing Members to

fulfil a VM requirement using Eligible FCM Buffer. The paragraph also includes details on how to opt in and out of the service and a definition of the term "Eligible FCM Buffer".

As a result of the addition of the new paragraph, other paragraphs in the same section have been renumbered.

The text of the changes to the FCM Procedures are attached hereto as **Appendix I**.

Part III: Core Principle Compliance

LCH has reviewed the changes against the requirements of the Core Principles, in particular Core Principle F, and finds that they will continue to comply with all the requirements and standards therein.

Part IV: Public Information

LCH has posted a notice of pending certification with the CFTC and a copy of the submission on LCH's website at:

<http://www.lch.com/rules-regulations/proposed-rules-changes>

Part V: Opposing Views

There were no opposing views expressed to LCH by governing board or committee members, members of LCH.Clearent or market participants that were not incorporated into the rule.

Certification

LCH hereby certifies to the Commodity Futures Trading Commission, pursuant to the procedures set forth in the Commission regulation § 40.6, that attached rule submission complies with the Commodity Exchange Act, as amended, and the regulations promulgated there under.

Should you have any questions please contact me at julian.oliver@lch.com.

Yours sincerely



Julian Oliver
Chief Compliance Officer
LCH Limited

Appendix I
FCM Procedures



FCM PROCEDURES OF THE CLEARING HOUSE

LCH LIMITED

4.6.3 **Withholding tax – Depositories**

A Depository may offer a recovery service for overseas taxes on government bonds. The Clearing House will assist in the recovery process and remit to FCM Clearing Members any relevant recovery in withholding tax credited to the Clearing House's account by the relevant Depository.

In certain cases, the Clearing House or the relevant Depository will withhold tax on a Coupon if the correct documentation is not lodged with the Clearing House or such Depository.

4.7 **References**

These FCM Procedures should be read in conjunction with the relevant contractual provisions, user guides and/or manuals of the relevant Depository. Please also refer to each relevant Depository for the relevant settlement deadlines in particular those for deliveries from local markets to Clearing House accounts.

4.8 **Contingency Arrangements**

In the event of an outage of the CMS, the Clearing House will notify FCM Clearing Members via member circular and FCM Clearing Members may send certain instructions, using the appropriate form in the Schedules of these FCM Procedures, to the Clearing House by fax and email (see Section 4.1.4 of these FCM Procedures).

Normal service hours and deadlines will apply to such instructions.

The Clearing House will notify FCM Clearing Members via a member circular when the CMS is available again.

4.9 **Treatment of Unallocated Excess and Return of FCM Buffer**

~~4.8.~~4.9.1 **Return and Reapplication of Unallocated Excess and Return of FCM Buffer**

Upon the request of an FCM Clearing Member, the Clearing House shall return all or a portion of such FCM Clearing Member's available Unallocated Excess or FCM Buffer (as requested) to such FCM Clearing Member; **provided, that** (i) FCM Clearing Members are not entitled to request the return of Encumbered FCM Buffer, and (ii) the Clearing House shall not be required to return FCM Buffer if the FCM Clearing Member is a Defaulter. The FCM Clearing Member's request must contain the specific details of the amount of funds requested and whether such FCM Clearing Member is requesting the return of FCM Buffer or Unallocated Excess, and any other information reasonably requested by the Clearing House. The end of day report delivered to the FCM Clearing Member by the Clearing House shall constitute conclusive evidence of the amount of any FCM Buffer or Unallocated Excess returned to such FCM Clearing Member during that day, unless the Clearing House determines such report contained an error and subsequently delivers an amended report or other notice to the FCM Clearing Member in respect of such amounts.

FCM Regulation 15 (*Margining of Swap Product Client Accounts*) contains additional provisions relating to FCM Buffer, Encumbered FCM Buffer and Unallocated Excess.

Upon written request from an FCM Clearing Member (including via email), the Clearing House will apply Margin attributable to (A) an FCM Clearing Member's Unallocated Excess Sub-Account and/or (B) all of an FCM Clearing Member's FCM Client Sub-Accounts to its FCM Buffer Sub-Account. In requesting such transfer, the FCM Clearing Member shall be deemed to represent and warrant that such reapplication of Margin: (1) is in accordance with applicable law and regulation; and (2) has been requested by an individual that is appropriately authorized to make the request. Any request from an FCM Clearing Member to reapply Margin must: (i) in the case of a request for reapplication pursuant to sub-clause (A) above, contain the specific details of the amount of Margin to be reapplied; (ii) only request the reapplication where such reapplication reflects the true characterization of the Margin held by the Clearing House (in particular, the reapplication of Margin pursuant to this paragraph should only be requested where the relevant Margin is the property of the FCM Clearing Member); (iii) in the case of a request for reapplication of Margin pursuant to sub-clause (B) above, request the reapplication of Margin attributed to all of the relevant FCM Clearing Member's FCM Client Sub-Accounts since the start of that given Business Day; and (iv) include such other information that the Clearing House may require. The reapplication of Margin shall be effected by the Clearing House in its sole and absolute discretion and in accordance with predefined parameters, and shall become effective from such time that the reapplication is reflected in the Clearing House's books and records.

4.9.2 Use of FCM Buffer as Variation Margin

Notwithstanding anything to the contrary herein, an FCM Clearing Member may elect to have Eligible FCM Buffer that the Clearing House holds at the end of each Business Day applied to its obligation to pay USD denominated Variation Margin only with respect to its C account. In the event of such election in accordance with this Section 4.9.2, the Clearing House may apply on each Business Day the full amount of Eligible FCM Buffer to the Variation Margin due from the relevant FCM Clearing Member. Any amount of Variation Margin that remains outstanding following such application shall remain payable by the FCM Clearing Member in accordance with the FCM Rulebook. Upon the application by the Clearing Member of Eligible FCM Buffer in accordance with this Section 4.9.2, the relevant FCM Clearing Member shall be deemed to acknowledge that Eligible FCM Buffer so applied by the Clearing House no longer constitutes FCM Buffer and the Clearing House shall be deemed to acknowledge that any USD denominated Variation Margin due to it with respect to the relevant FCM Clearing Member's C account shall be deemed to be reduced by an amount equal to Eligible FCM Buffer so applied.

An FCM Clearing Member that wishes to make an election to have Eligible FCM Buffer applied in accordance with this Section 4.9.2 or to cancel a previous election to do so should contact the Clearing House's Collateral

Operations team (collateral.operations@lch.com) and provide any other information reasonably requested by the Clearing House. Elections and cancellations in accordance with this Section 4.9.2 become effective upon the FCM Clearing Member receiving confirmation in writing of the election or cancellation from the Clearing House. Elections and cancellations received by the Clearing House prior to 12:00 pm EST on a Business Day are typically processed on the following Business Day.

Through making an election or cancellation in accordance with this Section 4.9.2, an FCM Clearing Member is deemed to represent and warrant that (a) it is not a Defaulter and (b) the individual making the request on behalf of the relevant FCM Clearing Member is appropriately authorized to do so.

For the purposes of this Section 4.9.2 and with respect to an FCM Clearing Member, “Eligible FCM Buffer” means, on the relevant Business Day, the lesser of: (i) its FCM Buffer that is not Encumbered FCM Buffer at the end of such Business Day; and (ii) the total USD cash held by the Clearing House in the LCH Swaps Client Segregated Depository Account at the end of such Business Day.

For the purposes of this Section 4.9, references to FCM Clearing Member shall mean an FCM Clearing Member who provides FCM SwapClear Clearing Services.

4.9.4.10 Collateral Value Reports

In accordance with FCM Regulation 15(d) (*Margining of Swap Product Client Accounts*), an FCM Clearing Member that has elected to adopt the LSOC With Excess Model is required to provide the Clearing House with an eligible CVR (Collateral Value Report as defined in the FCM Regulations) at least once per Business Day.

4.9.4.10.1 *Contents of the Collateral Value Report*

The CVR should contain details of the following:

- (a) **FCM Client Sub-Account Balance:** The value of Margin delivered for and on behalf of each FCM Client and its respective FCM Client Sub-Account.
- (b) **FCM Buffer:** The value of FCM Buffer lodged in the FCM Buffer Sub-Account.

All values provided in a CVR must be the post haircut value in USD (or such other currency as agreed in writing by the Clearing House).

Where the CVR does not contain information for all of the FCM Clients of an FCM Clearing Member, the Clearing House will assume that the FCM Client Sub-Account Balance for those FCM Clients that are not included have not changed from that which is reflected in its books and records (either through delivery of a previous CVR or as a result of an Assumed Allocation).

Unallocated Excess may be allocated to an FCM Client Sub-Account or to an FCM Buffer Sub-Account through the submission of a CVR. Any Margin that