# CLIENT ALERT

## Regulators to Consider Changes to Margin Requirements for Retail FX Transactions

**January 21, 2015**

On January 20, the National Futures Association (NFA) announced that it would consider, at its next board meeting (currently scheduled for February 19), increasing margin requirements for over-the-counter foreign exchange (FX) transactions that NFA members enter into with retail U.S. customers.

Although the NFA has not yet provided details on how it might change margin requirements, news reports indicate that the NFA is seeking to make margin requirements for the over-the-counter retail FX transactions consistent with on-exchange contracts. Some commentators have suggested that regulators should also consider other rule changes – for example, requiring segregation of customer assets or review of concentrated positions. It remains to be seen whether regulators or SROs will adopt regulatory changes beyond increases in margin requirements.

Margin requirements – often referred to as leverage limits – are a critical issue in the over-the-counter FX market. Existing regulations of the Commodity Futures Trading Commission (CFTC), adopted in 2010, require 2 percent margin (thereby permitting 50:1 leverage) for trading in "major" currency pairs (British pound, the Swiss franc, the Canadian dollar, the Japanese Yen, the Euro, the Australian Dollar, the New Zealand Dollar, the Swedish Krona, the Norwegian Krone and the Danish Krone) and 5 percent margin (or 20:1 leverage) for other currency pairs. There were no set retail FX leverage limits prior to the 2010 CFTC regulations, and some FX market participants reportedly allowed even higher leverage limits (in excess of 100:1). The initial version of the CFTC's 2010 regulations proposed lowering leverage limits to 10:1, but the CFTC adopted the 50:1 and 20:1 leverage limits described above in response to industry criticism.

The background to the NFA's action has been widely reported – FX markets have been hit with turmoil in the aftermath of last week's surprise move by the Swiss National Bank to remove the Swiss Franc – Euro cap. Both retail and institutional FX participants have been hit hard by resulting volatility in FX markets, and news reports indicate that many FX brokers and trading platforms have seen significant declines in their capital.

Under the Commodity Exchange Act (CEA), the CFTC has jurisdiction over FX futures, FX options and certain other FX transactions entered into with U.S. retail customers. Only certain types of registered entities can enter into over-the-counter FX transactions with U.S. retail customers – namely, CFTC-registered futures commission merchants, CFTC-registered retail foreign exchange dealers, U.S.-based financial institutions (e.g., banks and savings associations), financial holding companies, and SEC-registered broker-dealers (and certain affiliates of those entities). The NFA is the self-regulatory organization overseeing retail FX transactions for applicable CFTC registrants, but other retail FX transactions are overseen by other regulators and self-regulatory organizations such as FINRA (which has jurisdiction over broker-dealers that enter into over-the-counter FX transactions with U.S. retail customers). Thus, even if the NFA does change its leverage limits, action by other regulators would be necessary to fully implement a change in leverage limits for retail FX transactions.

Crowell & Moring's attorneys are available to discuss the impact of any proposed rule changes on market participants, and to assist in providing comments on proposed rules.

For more information, please contact the professional(s) listed below, or your regular Crowell & Moring contact.

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