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Architecture of Industry Form Documentation for Done-With Transactions

by

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I. Background.

In December 2023, the SEC passed a rule,[1] requiring SEC-registered Clearing Agencies to require their members to submit for clearing certain U.S. Treasury cash transactions and almost all repurchase transactions ("repos") in U.S. Treasury securities by the end of 2026, for cash transactions, and June 30, 2027, for repo. To prepare for this transition, in late 2024, SIFMA published versions of an industry form (the "Industry Form") designed for use as a stand-alone document or as an annex to an existing Master Repurchase Agreements or Global Master Repurchase Agreement (each, an "MRA" or "GMRA", respectively) for the clearing of repo and cash transactions that the clearing firm executed bilaterally with customers ("done-with trades").[2] SIFMA and industry participants are also working on a form for repo and cash transactions entered into by customers with executing counterparties and given up to a clearing member for clearing (so-called "done-away trades"). This writing focuses on done-with trades under the published Industry Form.

Clearing of done-with trades provides balance sheet benefits to an executing firm through the substitution of a central clearing counterparty in the place of the different bilateral counterparties with which a particular clearing member is doing Treasury cash or repo trades.[3] As a result, many clearing members have already been clearing U.S. Treasury repos through The Fixed Income Clearing Corporation ("FICC") with their repo counterparties on a voluntary basis using bespoke documentation annexed to their MRAs or GMRAs. Because of the upcoming clearing mandate and the market transition to the new SIFMA industry form for done-with transactions, however, many clearing members are moving to a version of the Industry Form for clearing done-with U.S. Treasury repo trades. The Industry Form can also be used for cash trades, although it may be cumbersome if used solely for that purpose.

II. General Structure of New Industry Documentation.

The Industry Form consists of either (x) an Annex to a clearing member's negotiated MRA or GMRA or (y) a stand-alone Agreement that can be used alongside the clearing member's negotiated MRA or GMRA with the customer. The Annex or Agreement both contain general terms applicable to clearing (such as novation terms, representations, covenants, security interest grant, defaults (including cross-default), remedies, indemnity, limitation of liability and termination. Choosing between them is a matter of preference for clearing members and

[1] *See Standards for Covered Clearing Agencies for U.S. Treasury Securities and Application of the Broker-Dealer Customer Protection Rule With Respect to U.S. Treasury Securities*, 89 Federal Register 2714 (2024). Compliance dates were pushed out in 2025. *See* 90 Federal Register 11134 (2025).
[2] *See https://www.sifma.org/resources/market-practices-model-documentation/treasury-clearing-documentation*.
[3] By substituting multiple counterparties for one central counterparty, the executing firm can net down on its balance sheet exposures with the central counterparty that would otherwise remain gross exposures facing separate bilateral counterparties.

customers, although sometimes customers seek to use the standalone version as a way to separate U.S. Treasury cleared repos from other bilateral repo business.

Accompanying the Annex/Agreement are a Schedule of elections that a clearing member and its customer will make and Modules for different cleared products, platforms and margin mechanics.

A. <u>Schedule</u>.

The Schedule is the heart of the Industry Form and involves elections of certain terms, akin to how an ISDA Schedule would work. One difference is that the elections are in the form of check boxes with all options visible to negotiating parties in the standard template.

Key terms for clearing members to negotiate with their customers include:

(i) What happens if the repo transaction is rejected for novation (reverts to bilateral, unwinds and is canceled or is terminated with damages paid);[4]

(ii) What obligations are secured by collateral granted under the Industry Form (it is presumed that the bilateral MRA/GMRA will be so secured unless an opt-out is selected in the Schedule);[5]

(iii) Does collateral under other agreements secure the Annex/Agreement (it is presumed that rights of the customer under the bilateral MRA/GMRA secure the Industry Form unless an opt-out is selected in the Schedule);[6]

(iv) Does cross-default apply and to what obligations (it is presumed that the Industry Form and associated MRA/GMRA cross-default with each other unless an opt-out is selected in the Schedule);[7]

(v) Is porting available and under what conditions, which is a provision that clearing members and customers at the time of this writing are finding difficult to negotiate since no porting operability is yet available at the clearing agencies;[8]

(vi) Usual provisions such as cure periods, whether events of default must be continuing, when notice of default/exercise of remedies is to be given and whether these operate the same as in the MRA/GMRA;[9]

(vii) Is mini-closeout, a customary market remedy in bilateral repo market, optional or mandatory;[10]

[4] *See* Part 2(d) of the Schedule.
[5] *See* Part 2(g) of the Schedule.
[6] *Id*.
[7] *Id*.
[8] *See* Part 2(i) of the Schedule.
[9] *See* Part 2(j) of the Schedule.
[10] *Id*.

(viii) What happens if the clearing organization ceases to act for the clearing member;[11]

(ix) Indemnity and limitation of liability provisions, which are substantially streamlined in the Industry Form, and the extent of any carveouts;[12] and

(x) A Part 7 for optional terms, which many clearing members are building out, akin to Part 5 in an ISDA Schedule (these optional terms typically include correction to or expansion/limitation of provisions in the Annex/Agreement and bespoke terms that the parties may draw from their bespoke documentation).

B. Modules.

The Industry Form contains Modules, which are tied to available clearing options, are described below. SIFMA expects to add new modules as additional cleared products, either from FICC or new clearing agencies planning to clear U.S. Treasuries, such as CME or ICE Clear Credit, become available. As of this writing, no current industry module yet exists for the FICC new Collateral-in-Lieu product, although we understand one is in process. Nor are there modules for clearing at CME or ICE Clear Credit.

Below is a high-level description of the existing clearing Modules along with discussion of how clearing works under them.

1. Module I of Industry Form: FICC Sponsored Repo: DVP

(a) Clearing Relationship. In Module I, the clearing member is a Sponsoring Member of FICC. The customer is a sponsored member of FICC, which means that the customer has a direct relationship with FICC on each trade that is novated and is a limited purpose member of FICC.

(b) Novation Process. The clearing member enters into the start leg, or on-leg, with the Customer bilaterally, and securities and cash are exchanged with respect to the on-leg as in any bilateral trade, without the involvement of FICC. Only the off-leg of the repo (i.e., the requirement on the original seller's part to repurchase the securities sold in the repo and to return the cash (together with interest) and the requirement on the original buyer's part to sell the securities back to the original seller) is novated and cleared in FICC. In other words, the deliver, receive and related payment obligations between the customer, as sponsored member, and the clearing member (as executing firm) are terminated and replaced with deliver, receive and related payment obligations between FICC and each of the sponsored member and sponsoring Member (in its role as executing firm and clearing member of FICC). The clearing member, in its role as executing firm, is now liable under the novated off-leg of its own trade with FICC and is no longer a party (other than providing the guarantee described below) to the transaction between FICC and the customer. Instead, the deliver, receive and related payment obligations are due and owing between FICC and the sponsored member, as principals. Once novated, the transactions are known as sponsored member transactions.

[11] *Id*.
[12] *See* Part 2(l) of the Schedule.

(c) **Sponsoring Member Obligations.** The clearing member, as sponsoring member, guarantees its customer's obligations under the sponsored member transactions novated to FICC and serves as processing agent for the customer.

(d) **Customer Obligations.** The customer has payment and delivery obligations to the clearing member, such as variation margin payments described below, settlement payment or delivery obligations, fee and indemnity obligations.

(e) **Variation Margin.** During the term of a sponsored member transaction, FICC will mark each sponsored member transaction to market. Such mark-to-market calculation may result in an amount owed by FICC to the sponsored member or by the sponsored member to FICC ("Funds Only Settlement" or "FOS").[13] Settlement for FOS occurs on a net basis for an omnibus account for all of the clearing member's sponsored members.

The FICC rules describe variation margin or FOS as a settlement payment and requires it to be made in cash. The clearing member acts as processing agent for these FOS payments for all of its sponsored members and may advance some of the amounts due to timing issues. If the repo trade is overnight, the trade may be novated after 12:00 p.m. to limit the need for FOS payments intraday.

(f) **Initial Margin.** Initial margin in FICC today is comprised of actual initial margin (ie, potential futures exposure on the transaction) and clearing fund for loss allocation. While the Agreement/Annex allows the parties to elect this to be passed through to the sponsored member, clearing members today typically pay this to FICC, with the clearing member covering the risk and cost through haircut and pricing of the repo. However, see margin module discussion below.

(g) **Settlement.** In the DVP module, settlement of the off-leg occurs through a pre-settlement process where the clearing member will settle first with the party (FICC or the customer) that must deliver securities. The clearing member typically will front cash for the settlement process in settling with that party. This module is called DVP, but settlement actually involves this two-step process. Further, settlement for the sponsored member transactions with FICC occurs on a net basis per CUSIP for all of the clearing member's sponsored members. The Industry Form also provides for pre-positioning by the sponsored member, but this is not as customary across the board today.

If FICC owes a net amount, it will deliver the cash or securities it owes to the Sponsoring Member's omnibus account at the Bank of New York Mellon, which is an account held in the name of the Sponsoring Member for the benefit of its sponsored members. FICC's delivery of the net amount into such omnibus account satisfies its obligations to each of the clearing member's sponsored members to which it owes cash or securities.

Similarly, if, once netting occurs, the sponsored members owe cash or securities to FICC, the clearing member will deliver such net amount or securities to the omnibus account, and then to FICC, to satisfy the obligations of the clearing member's sponsored members to FICC.

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[13] Note that FOS includes amounts in addition to mark-to-market.

As processing agent, the clearing member is responsible for moving cash and securities to and from the omnibus account to and from its sponsored members. Depending on netting, the clearing member may need to also move amounts and securities between sponsored members to ensure that they receive what they are owed from FICC and pay or deliver what they owe to FICC. A new clearing member covenant in the Industry Form requires the clearing member to pass to the Customer what the Customer is entitled to receive.

(h) **Security.** The clearing member takes a security interest in an account opened by the clearing member on its books and records for the customer to which cash or securities relating to the customer's sponsored repo transactions are credited. A clearing member also takes a security interest in the customer's receivables from FICC, its rights under any bilateral repo, along with any purchased securities delivered by the Customer in bilateral repo, and in any omnibus account held by clearing member relating to sponsored repo, in each case to secure the Customer's Annex/Agreement and MRA/GMRA obligations (unless the scope of the lien has been amended in the Schedule).

As noted above, a clearing member may take a broader security interest in the customer's rights under other agreements relating to transactions under other master agreements with the customer to secure obligations under all such agreements. Such collateral and obligations may also be expanded to affiliates of the clearing member. Perfection under U.S. state law is achieved by a UCC financing statement filing and control over the account. Local law steps may be needed if the customer is located outside the U.S.

2. Module II: Sponsored Repo: GC

Module II is the same as Module I except as discussed below.

(a) **Novation Process.** The on-leg settles in tri-party at the Bank of New York Mellon (the "Tri-Party Custodian").

(b) **Variation Margin.** Variation margin is handled by the Tri-Party Custodian, other than a small FOS amount relating to a small amount of margin collected or provided by FICC to address changes in ambient interest rates. A clearing member may select FOS Satisfaction for this to allow it to keep this amount, if paid by FICC, in exchange for paying this amount, if owed to FICC. This avoids having to collect this separately from the customer.

In this module, variation margin is paid on a gross basis (there is no omnibus account netting).

(c) **Settlement.** In this module, while clearing member still acts as processing agent, settlement payments and deliveries are handled by the Tri-Party Custodian. Payment or delivery by clearing member to the customer's account at the Tri-Party Custodian and by the customer to clearing member's account at the Tri-Party Custodian is deemed a payment or delivery by FICC. In this module, settlement is made on a gross basis (there is no omnibus account netting).

(d) **Security.** Clearing member also takes a security interest in the accounts at the Tri-Party Custodian, which gives clearing member a pledge back of the repo securities delivered to the customer, for instance. Moreover, a clearing member may add an optional provision that if a FICC default occurs, the clearing member controls the delivery of any notice by the customer to the Tri-Party Custodian and handling of any excess securities in the customer's tri-party account.

3. Module III: Agency Clearing

(a) Clearing Relationship. In Module III, the clearing member acts as agent for the customer and enters into the transaction with FICC on behalf of the customer. FICC treats the clearing member as principally liable. This is akin to how futures transactions work. The customer has no direct relationship with FICC. FICC knows the customer's identity only through its LEI number.

(b) Novation Process. The clearing member enters into the on-leg with the customer bilaterally as in the DVP clearing model, and securities and cash are exchanged on the on-leg as in any bilateral trade, without the involvement of FICC. Only the off-leg of the repo is novated and cleared in FICC. In other words, the deliver, receive and related payment obligations between the customer and clearing member are terminated and replaced with deliver, receive and related payment obligations between FICC and clearing member and between FICC and clearing member on behalf of the customer. Clearing member is liable under the novated off-leg of its own trade with FICC and also of that entered into by it on behalf of the customer.

(c) Clearing Member Obligations. Because clearing member is principally liable to FICC, clearing member implicitly is guaranteeing its customer's obligations to FICC.

(d) Customer Obligations. The customer has payment and delivery obligations to clearing member, as well as indemnity obligations.

(e) Variation Margin. Clearing member is obligated to FICC for all FOS payments, which are determined on a net basis for the agent clearing member omnibus account into which clearing member will book all agent clearing transactions. Clearing member can demand/seek reimbursement from the customer for amounts paid.

(f) Initial Margin. For agent clearing, FICC calculates initial margin on a net basis for all agent clearing transactions booked in the agent clearing member omnibus account, unless individual segregation is selected by any customer, in which case initial margin for that customer is calculated gross and separately. This is different from sponsored repo and a potential advantage from a clearing member perspective (to the extent it lower the amount of clearing fund the clearing member is obligated to post to FICC). See also the margin module discussion below.

(g) Settlement. In this module, settlement of the off-leg occurs through a pre-settlement process where clearing member will settle first with the party (FICC or the customer) that must deliver securities. Clearing member will front cash for the settlement process in settling with that party, although pre-position is also available as an option. Settlement thus involves a two-step process, like sponsored repo. Further, settlement occurs on a net basis per CUSIP for all of clearing member's agent clearing transactions.

If FICC owes a net amount, it will deliver the cash or securities it owes to the agent clearing member omnibus account at the Bank of New York Mellon. FICC's delivery of the net amount into such omnibus account satisfies its obligations to clearing member.

Similarly, if, once netting occurs, clearing member owes cash or securities to FICC for agent clearing transactions, clearing member will deliver such net amount to the omnibus account, and then to FICC, to satisfy those obligations.

As processing agent, clearing member is responsible for moving cash and securities to and from the omnibus account to and from its customers doing agent clearing. Depending on netting, clearing member may need to also move amounts between customers to ensure that they all receive what they are owed and pay what they owe. A new clearing member covenant in the new industry form requires clearing member to pass to the customer what the customer is entitled to receive.

(h) **Security.** Clearing member takes a security interest in an account opened by clearing member on its books and records for the customer to which cash or securities relating to the customer's agent clearing transactions done for the customer with FICC. Clearing member also takes a security interest in its rights under any bilateral repo, along with any purchased securities delivered by the customer in bilateral repo, and in any omnibus account held by clearing member relating to agent clearing, in each case to secure the customer's Annex/Agreement and MRA/GMRA obligations (unless the lien and scope of secured obligations has been amended). Clearing member's form may also provide for the taking of a broader security interest, as discussed previously above.

Perfection is achieved by control over the account, and no UCC filing is needed, which is a key advantage of this approach. Local law steps may be needed if the customer is located outside the U.S.

4. Module IV: Margin

Clearing members have two options for initial margin collection:

(a) **Discretionary.** One version allows clearing member to call for margin on a discretionary basis or as negotiated in the module.

(b) **Independent Segregation.** The other version is for when customers select independent segregation and will allow a clearing member that is a U.S. broker-dealer to take a debit in the 15c3-3 reserve formula for any posting for the customer.[14] Under this model, the clearing member must pass through the clearing fund requirement to the customer. Registered investment companies who deliver initial margin to their clearing member for cleared Treasury repo are required to use segregation.

[14] *See* 17 CFT § 240.15c3-3a, Note H.