

**MEMO# 25722**

December 16, 2011

# **CFTC Proposes Process for Making a Swap "Available to Trade;" Call Scheduled for January 4**

[25722]

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TO: DERIVATIVES MARKETS ADVISORY COMMITTEE No. 49-11

SEC RULES COMMITTEE No. 106-11

CLOSED-END INVESTMENT COMPANY COMMITTEE No. 54-11 RE: CFTC PROPOSES PROCESS FOR MAKING A SWAP "AVAILABLE TO TRADE;" CALL SCHEDULED FOR JANUARY 4

The Commodity Futures Trading Commission (the "Commission") recently proposed rules that would establish a process for a designated contract market ("DCM") or swap execution facility ("SEF") to make a swap "available to trade" for purposes of Section 2(h)(8) of the Commodity Exchange Act ("Proposed Rules"). [\[1\]](#) The Proposed Rules are summarized briefly below.

Comments on the Proposed Rules are due to the SEC no later than February 13, 2012. We will hold a conference call on January 4, 2012, at 2 p.m. Eastern time, to discuss ICI comments relating to the Proposed Rules. The dial-in number is 888-282-9639 and the passcode is 18036. Please let Jennifer Odom ([jodom@ici.org](mailto:jodom@ici.org) or 202-326-5833) know if you will participate on the call.

## **Proposed Rules**

Section 723 of the Dodd-Frank Wall Street Reform and Consumer Protection Act added new Section 2(h) to the Commodity Exchange Act, which provides that transactions involving swaps that are required to be cleared must be executed on a DCM or SEF unless no board of trade or SEF "makes the swap available to trade" or the transaction is subject to the clearing exception for end-users. [\[2\]](#)

The Proposed Rules provide that a DCM or SEF would submit "make available to trade" ("MAT") determinations for swaps to the Commission, either for approval or self-certification, pursuant to the Commission's existing filing procedures. [\[3\]](#) Under the approval procedure, the DCM or SEF would submit its MAT determination to the Commission. The DCM or SEF would be required to include in its filing, among other things,

an explanation and analysis of its consideration, as appropriate, of the factors set out in the Proposed Rules. [4] The Commission would have a 45-day period to review the determination, any time during which it could notify the DCM or SEF that it was not going to approve its MAT determination because it is inconsistent or appears to be inconsistent with the Commodity Exchange Act or the Commission's rules. [5]

Under the certification procedure, the DCM or SEF would be required to submit its MAT determination to the Commission and provide the same analysis regarding its consideration of the factors set out in the Proposed Rules as would be required under the approval procedure. The Commission would have 10 business days to review a MAT determination before it would be deemed certified and could be made effective, unless the Commission issued a stay of the certification for an additional 90 days.

If the Commission either approved a DCM's or SEF's MAT determination, or permitted a certified MAT filing to become effective, then the swap involved would be deemed available to trade. All other SEFs and DCMs listing or offering for trading that swap or any "economically equivalent swap" would be required to make those swaps available to trade for purposes of the trade execution requirement of Section 2(h)(8) of the Commodity Exchange Act. [6] Under the Proposed Rules, "economically equivalent swap" is defined as "a swap that the swap execution facility or designated contract market determines to be economically equivalent with another swap after consideration of each swap's material pricing terms."

The Proposed Rules also would require that DCMs and SEFs perform an annual review and assessment to evaluate whether swaps previously determined to be available to trade should continue to be treated in that manner. The Commission notes that, in this review, DCMs and SEFs also should evaluate their swaps that have not been deemed available to trade and submit MAT determinations to the Commission for these swaps if appropriate. The Proposed Rules would require that, upon completion of the annual review, the DCM or SEF must submit a report of its review electronically to the Commission, no later than 30 days after its fiscal year end.

The Release discusses the process for notifying the public that a DCM or SEF has made a swap available to trade. Under the Commission's existing rules, DCMs and SEFs would be required to post a notice and copy of their MAT submission on their website at the same time they file the submission with the Commission. The Commission also would post DCM and SEF MAT submissions on its website. The Commission states that it currently is assessing the feasibility of posting notices of all swaps that are determined to be made available to trade on an easily accessible page on its website.

## **Statements of Commissioners Sommers and O'Malia**

Commissioner Sommers voted against the Proposed Rules, stating in her opening statement that she believed the Commission's approach was "deeply flawed" and that "the proposal, if finalized, would allow a single DCM or SEF to bind the entire marketplace to a trade execution requirement through an ill-defined analysis that the Commission will be unable to reject unless it finds that the determination is inconsistent with the Act or Commission regulations." [7] She expressed the view that it is unlikely that the Commission could meet this standard given the lack of mandatory, objective criteria in the Proposed Rules. She noted that, once a swap is deemed available to trade, all over-the-counter participants also would have to determine whether a swap they trade or would like

to trade is the same or economically equivalent, as OTC trading would no longer be permitted in the approved swap. She also expressed concern regarding the definition of “economically equivalent.”

Although Commissioner O’Malia voted for the Proposed Rules, he expressed concern in his opening statement that the “proposal is permitting those that have the greatest financial incentives to force all trading onto a platform to determine which swaps must be executed on such platform.” [8] He expressed the view that the proposed process has implications particularly for those on the buy-side, and noted that many on the buy-side already have urged the Commission to play a more active role in the mandatory clearing process. He also recommended that the Commission hold a roundtable to “engage market participants in an open and public discussion of the mandatory trading requirement,” a suggestion Chairman Gensler took up at the open meeting and recommended that the staff schedule during the comment period.

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Senior Counsel

#### **endnotes**

[1] *Process for a Designated Contract Market or Swap Execution Facility To Make a Swap Available To Trade*, 76 FR 77728, (December 14, 2011), available at <http://www.cftc.gov/ucm/groups/public/@lrfederalregister/documents/file/2011-31646a.pdf> (“Release”).

[2] See Section 2(h)(8) of the Commodity Exchange Act.

[3] Proposed Rules 37.10 and 38.12 under the Commodity Exchange Act. Rules 40.5 and 40.6 under the Commodity Exchange Act set out the Commission’s existing filing procedures for trading protocols. The Commission requests comment in the Release on whether it should allow a DCM or SEF to submit its MAT determination with respect to a group, category, type, or class of swaps and, if so, how the Commission should define those terms.

[4] These factors are: (1) whether there are ready and willing buyers and sellers; (2) the frequency or size of transactions on SEFs, DCMs, or of bilateral transactions; (3) the trading volume on SEFs, DCMs, or of bilateral transactions; (4) the number and types of market participants; (5) the bid/ask spread; (6) the usual number of resting firm or indicative bids and offers; (7) whether a SEF’s trading system or platform or a DCM’s trading facility will support trading in the swap; or (8) any other factor that the SEF or DCM may consider relevant. Proposed Rules 37.10(b) and 38.12(b) under the Commodity Exchange Act. The Commission states that “[n]o single factor would be dispositive, as the DCM or SEF may consider any one factor or several factors to make a swap available to trade.” Release, *supra* note 1 at 77732. The Commission also notes that “as the swaps markets evolve and the Commission gains experience with overseeing these markets, it may consider setting objective factors based upon an empirical analysis of swap trading data in a future rulemaking.” *Id.*

[5] This review period may be extended by the Commission for an additional 45 days under certain circumstances.

[6] The Commission notes, however, that if a DCM or SEF makes a swap available to trade, the Proposed Rules would not require other DCMs and SEFs to list or offer that swap or an economically equivalent swap, for trading.

[7] Commissioner Jill E. Sommers, *Opening Statement Before the Sixth Open Meeting to Consider Final Rules Pursuant to the Dodd-Frank Act* (December 5, 2011), available at <http://www.cftc.gov/PressRoom/SpeechesTestimony/sommersstatement120511>.

[8] Commissioner Scott D. O'Malia, *Opening Statement of Commissioner Scott D. O'Malia* (December 5, 2011), available at <http://www.cftc.gov/PressRoom/SpeechesTestimony/omaliastatement120511>.

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