

MEMO# 26355

July 30, 2012

CFTC Adopts Schedule to Phase in Compliance with Swap Clearing Requirements

[26355]

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TO: CLOSED-END INVESTMENT COMPANY MEMBERS No. 49-12
DERIVATIVES MARKETS ADVISORY COMMITTEE No. 38-12
SEC RULES MEMBERS No. 70-12 RE: CFTC ADOPTS SCHEDULE TO PHASE IN COMPLIANCE WITH SWAP CLEARING REQUIREMENTS

The Commodity Futures Trading Commission (“CFTC” or “Commission”) recently adopted regulations to establish a schedule (“Schedule”) to phase in compliance with the clearing requirements under new section 2(h)(1)(A) of the Commodity Exchange Act (“CEA”), which was added by Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act. [\[1\]](#) The Schedule, which was proposed last September in conjunction with a separate schedule relating to trading documentation and margining requirements, [\[2\]](#) is described below. The Commission will undertake a separate rulemaking to adopt a schedule relating to the trading documentation and margining requirements at the same time that it finalizes the underlying documentation and margin rules.

In conjunction with the Schedule, the Commission issued its first proposed clearing requirement determination (a “Clearing Requirement determination”). [\[3\]](#) The Schedule, which will become effective on September 28, 2012, will be triggered by the finalization of the first Clearing Requirement determination. The Schedule provides the Commission with discretion to determine whether it should apply in connection with any particular Clearing Requirement determination. [\[4\]](#)

The Schedule, which was adopted as § 50.25 under the CEA, defines three categories of market participants that are largely the same as those described in the Proposal. A Category 1 Entity is defined to include a swap dealer (“SD”), security-based SD, major swap participant (“MSP”), major security-based swap participant, or an “active fund.” [\[5\]](#) A Category 2 Entity is defined to include a commodity pool, a private fund as defined in section 202(a) of the Investment Advisers Act of 1940 other than an active fund, or a person predominantly engaged in activities that are in the business of banking, or in activities that are financial in nature as defined in section 4(k) of the Bank Holding Company Act of 1956, provided that, in each case, the entity is not a “third-party

subaccount.”

A “third-party subaccount” is defined in the Schedule as “an account that is managed by an investment manager that (1) is independent of and unaffiliated with the account’s beneficial owner or sponsor, and (2) is responsible for the documentation necessary for the account’s beneficial owner to clear swaps.” [6] In response to comments, including those of ICI, the CFTC expanded the definition of third-party subaccount from the Proposal to not require specific approval by the beneficial owner, and excluded ERISA Plans from Category 2. As a result, these accounts will be entitled to the longest period of time to comply with the Clearing Requirement, as described below.

If the Commission determines that a compliance schedule is warranted in connection with a particular Clearing Requirement determination, a Category 1 Entity will be required to comply with the Clearing Requirement no later than 90 days after the publication of a Clearing Requirement determination in the Federal Register. [7] A Category 2 Entity will be required to comply with the Clearing Requirement within 180 days after the Clearing Requirement determination is published in the Federal Register, and all other market participants are required to comply with the Clearing Requirement no later than 270 days after the Clearing Requirement determination is published in the Federal Register. These timeframes are unchanged from the Proposal. A swap between entities in two different categories is subject to the clearing deadline of the counterparty entitled to the later compliance date. The Schedule explicitly provides that a market participant subject to a later compliance date may elect to clear a swap earlier (and the Commission states that, in that event, the market participant’s counterparty is required to oblige). [8]

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endnotes

[1] Swap Transaction Compliance and Implementation Schedule: Clearing Requirement under Section 2(h) of the CEA, 77 Fed. Reg. 44441 (July 30, 2012) (“Final Release”), available at <http://www.cftc.gov/ucm/groups/public/@lrfederalregister/documents/file/2012-18383a.pdf>.

[2] See ICI Memorandum No. 25505 (Sept. 20, 2011), available at http://www.ici.org/my_ici/memorandum/memo25505; Swap Transaction Compliance and Implementation Schedule: Trading Documentation and Margining Requirements under Section 4s of the CEA, 75 Fed. Reg. 78176 (September 20, 2011); and Swap Transaction Compliance and Implementation Schedule: Clearing and Trade Execution Requirements under Section 2(h) of the CEA, 75 Fed. Reg. 58186 (September 20, 2011) (“Proposal”).

[3] Clearing Requirement Determination under Section 2(h) of the CEA, RIN 3038-AD86 (July 24, 2012), available at <http://www.cftc.gov/ucm/groups/public/@newsroom/documents/file/federalregister072412.pdf>.

[4] The Commission states, in this regard, that it “while the schedule may be necessary in connection with some Clearing Requirement determinations, especially those covering new classes of swaps, there also may be determinations that are sufficiently similar to prior

ones that no compliance schedule is necessary. As such, the Commission will determine whether or not to apply the . . . compliance schedule as part of its analysis in connection with each Clearing Requirement determination.” Final Release, supra note 1, at 44446.

[5] An “active fund” is defined as “any private fund as defined in section 202(a) of the Investment Advisers Act of 1940, that is not a third-party subaccount and that executes 200 or more swaps per month based on a monthly average over the 12 months preceding the Commission issuing a clearing requirement determination under section 2(h)(2) of the Act.” This definition was modified from the Proposal, which would have set the threshold at 20 or more swaps per month.

[6] The Commission notes in the Final Release, however, that “if the investment manager has no responsibility for documenting the clearing arrangements, then that account would be required to clear its swaps subject to required clearing within 180 days” (the time frame applicable to Category 2 Entities, as described below). Final Release, supra note 1, at 44445.

[7] ICI had sought clarification that a market participant can determine whether it is an MSP for purposes of the Schedule at the same time it is required to review its status as an MSP under other Commission and Securities and Exchange Commission rules. The Commission stated in the Final Release that a potential MSP can review its obligation to register as an MSP at the same time it reviews its obligations under the Schedule, but that if it discovers it has crossed the threshold established under the MSP rules and must register during the 90-day period for Category 1 Entities, the Commission “would consider allowing that entity to petition for additional time to come into compliance with the Clearing Requirement.” The Commission expressed a similar view with respect to potential SDs. Id. at 44446 and n.19.

[8] Id. at 44442.