

MEMO# 25505

September 20, 2011

CFTC Proposes Implementation Schedules for Certain Swaps Rules; Conference Call September 26

[25505]

September 20, 2011

TO: DERIVATIVES MARKETS ADVISORY COMMITTEE No. 38-11
SEC RULES COMMITTEE No. 80-11 RE: CFTC PROPOSES IMPLEMENTATION SCHEDULES FOR CERTAIN SWAPS RULES; CONFERENCE CALL SEPTEMBER 26

The Commodity Futures Trading Commission (“CFTC”) has proposed two implementation schedules to phase in compliance with many of the Dodd-Frank Act requirements for swap transactions – one for the clearing and trade execution requirements and one for the trading documentation and margining requirements. [1] The proposed schedules set forth time frames of 90, 180, or 270 days by which different swap entities would be required to comply with the final rule requirements. The schedules are summarized below.

Comments on the proposed implementation schedules are due to the CFTC no later than November 4, 2011. We have scheduled a conference call for Monday, September 26, 2011, at 2:00 p.m. ET to discuss potential comments by the Institute on the proposed schedules. If you would like to participate in the call, please contact Ruth Tadesse at rtadesse@ici.org or 202/326-5836.

Implementation Schedule: Clearing and Trade Execution Requirements

The CFTC has proposed an implementation schedule to assist market participants in complying with the mandatory clearing and trade execution requirements being enacted through rules it is adopting pursuant to the Dodd-Frank Act. The proposed schedule includes multiple steps. First, it identifies a series of rules that must be finalized by the CFTC before market participants could be required to comply with either the clearing or the trade execution requirements. With respect to clearing, the CFTC must finalize rules that further define “swap,” “swap dealer,” and “major swap participant,” set forth the end-user exception to mandatory clearing, and provide for the protection of cleared swaps customer contracts and collateral. With respect to trade execution, the CFTC must finalize all of the rules related to the clearing requirement and adopt final rules related to swap execution facilities (“SEFs”) and designated contract markets (“DCMs”).

Second, the schedule includes triggering events for the proposed compliance time line. For the clearing requirement, the triggering event would be the CFTC's issuance of a mandatory clearing determination for a swap, or group, category, type, or class of swaps. This determination would be made not later than 90 days after a derivatives clearing organization ("DCO") has presented a complete submission to the CFTC regarding its intention to accept a swap(s) for clearing. [2] The proposed trigger for the trade execution requirement would be the later of (1) the applicable deadline established under the compliance schedule for the associated clearing mandate, or (2) 30 days after the swap is made available for trading on either a SEF or DCM. [3]

The CFTC would trigger the compliance schedules each time it issues a mandatory clearing determination for a new group, category, type, or class of swaps – i.e., for any entirely new group, category, type, or class of swaps. The proposed schedules would not be triggered when a DCO begins offering a new swap that meets the requirements imposed under a previously issued clearing determination. Importantly, when issuing a mandatory clearing determination, the CFTC would set an effective date by which all market participants would have to comply. The proposed compliance schedules would be used only then the CFTC deems it necessary to phase in compliance among market participants (as discussed below).

Third, the implementation schedule would establish the compliance deadlines for the clearing and trade execution requirements based on the type of market participants entering into a swap transaction, providing for a phase in of 90, 180, or 270 days.

- Category 1 entities would include swap dealers, security-based swap dealers, major swap participants, major security-based swap participants, or active funds. [4] These entities would need to comply with the mandatory clearing requirement within the first 90 days after the CFTC issues any clearing determination.
- Category 2 entities would include commodity pools; private funds as defined in Section 202(a) of the Investment Advisors Act of 1940 other than active funds; employee benefit plans identified in paragraphs (3) and (32) of section 3 of the Employee Retirement Income and Security Act of 1974; or persons 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 the entity is not a third-party subaccount. [5] Such entities engaging in a swap transaction with a Category 1 entity or another Category 2 entity would need to comply with the mandatory clearing requirement within 180 days after the CFTC issues any clearing determination.
- Category 3 Entities would be those engaged in all other swap transactions, including those involving third-party subaccounts and those not excepted from the mandatory clearing requirement within 270 days after the CFTC issues a clearing determination.

Market participants would not be limited to the phase in schedule outlined above. They could choose to comply with the mandatory clearing requirement (and therefore the trade execution requirement) earlier than would otherwise be required for their category of entity. According to the Clearing Release, the proposed phase in and the allowance for voluntary participation by market participants ahead of the designated time frames should allow for adequate representation of market participants at the outset of implementing the new mandatory clearing and trade execution regime.

Implementation Schedule: Documentation and Margining

Requirements

The CFTC has proposed an implementation schedule to assist market participants in complying with the trading documentation and margining requirements being imposed pursuant to the Dodd-Frank Act. Similar to the proposed schedule for the mandatory clearing and trade execution requirements, the implementation schedule for the documentation and margining requirements involves multiple components including the completion of certain rules by the CFTC and phased in compliance based on the category of swap market participant. The outstanding rule proposals that must be completed before the compliance schedules could begin to run would include, for the documentation requirements, [6] those related to confirmation of swap transactions, the protection of collateral for uncleared swaps, the further definitions of “swap,” “swap dealer,” and “major swap participant,” and the registration of swap dealers and major swap participants. For the margining requirements, the CFTC would need to finalize the trading documentation rule, the rules further defining “swap,” “swap dealer,” and “major swap participant,” and the registration rules for swap dealers and major swap participants.

The proposed schedule would phase in market participants using the 90, 180, and 270 day-periods proposed in the Clearing Release but would separate such participants into four categories instead of three. Category 1 and 2 entities would remain the same (see above) but, in the Documentation Release, Category 3 entities would include Category 2 entities whose positions are held by a third-party subaccount and Category 4 entities would include any person not included in the first three categories. The proposed compliance periods would run from the date of publication in the Federal Register of the final CFTC rules for trading documentation and margin requirements – 90 days for Category 1 entities, 180 days for Category 2 entities, and 270 days for Category 3 and 4 entities. As with the proposed compliance schedule for clearing and trade execution, market participants could comply voluntarily with the shorter compliance periods.

Potential Rule Making Schedule

The CFTC has announced the list of swap-related rules that it may consider through the first quarter of 2012.

Remainder of 2011:

- Clearinghouse Rules
- Data Recordkeeping and Reporting
- End-User Exception
- External Business Conduct
- Internal Business Conduct (Duties, Recordkeeping, and Chief Compliance Officers)
- Position Limits
- Product Definitions/Commodity Options
- Real-Time Reporting
- Segregation for Cleared Swaps
- Trading – Designated Contract Markets and Foreign Boards of Trade

First Quarter of 2012:

- Capital and Margin
- Client Clearing Documentation and Risk Management
- Conforming Rules
- Disruptive Trading Practices
- Governance and Conflict of Interest

- Internal Business Conduct (Documentation)
- Investment of Customer Funds
- Swap Execution Facilities
- Segregation for Uncleared Swaps
- Straight-Through Trade Processing

Heather L. Traeger
Associate Counsel

endnotes

[1] Swap Transaction Compliance and Implementation Schedule: Clearing and Trade Execution Requirements under Section 2(h) of the CEA, 76 Fed. Reg. 58186 (September 20, 2011) (“Clearing Release”) and Swap Transaction and Implementation Schedule: Documentation and Margining Requirements under Section 4(s) of the CEA, 76 Fed. Reg. 58176 (September 20, 2011) (“Documentation Release”), available at <http://www.cftc.gov/ucm/groups/public/@newsroom/documents/file/federalregister090811.pdf> and <http://www.cftc.gov/ucm/groups/public/@newsroom/documents/file/federalregister090811b.pdf>.

[2] In the Clearing Release, the CFTC noted that it would begin the review process for issuing mandatory clearing determinations for swaps that DCOs are currently clearing or that a DCO has already filed a submission in the “near term.” In addition, CFTC-initiated review of swaps that have not been accepted for clearing by a DCO would take place on an ongoing basis.

[3] According to the Clearing Release, SEFs and DCMs could offer swaps for trading by market participants on a voluntary basis prior to a CFTC-issued mandatory clearing determination.

[4] An “active fund” would mean any private fund as defined in section 202(a) of the Investment Advisors Act of 1940, that is not a third-party subaccount and that executes 20 or more swaps per month based on a monthly average over the 12 months preceding the CFTC issuing a mandatory clearing determination under section 2(h)(2) of the Act. To calculate the 20 swap threshold, a fund would be required to include all swaps that it executes, not just those that are the subject of a clearing determination.

[5] A third-party subaccount would be a managed account that requires specific approval by the beneficial owner of the account to execute documentation necessary for executing, confirming, margining, or clearing swaps.

[6] The audit, recordkeeping, and reporting provisions in the CFTC’s documentation requirements would not be subject to the proposed compliance schedule. The compliance dates for these provisions would be established when the CFTC adopts final rules.

should not be considered a substitute for, legal advice.