



U.S. COMMODITY FUTURES TRADING COMMISSION

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Division of
Swap Dealer and
Intermediary Oversight

CFTC Letter No. 12-21
No-Action
October 12, 2012
Division of Swap Dealer and Intermediary Oversight

Re: Time Limited No-action Relief: Foreign Exchange Swaps and Foreign Exchange Forwards Not to be Considered in Calculating Aggregate Gross Notional Amount for Purposes of Swap Dealer De Minimis Exception or in Calculating Substantial Position in Swaps or Substantial Counterparty Exposure for Purposes of the Major Swap Participant Definition;

Time-Limited No-action Relief for persons that meet the definitions of Commodity Pool Operators and Commodity Trading Advisors Solely as a Result of their Foreign Exchange Swap and Foreign Exchange Forward Activities

Ladies and Gentlemen:

This letter is in response to requests from multiple parties received by the Division of Swap Dealer and Intermediary Oversight (“Division”) of the Commodity Futures Trading Commission (“Commission”) requesting relief from the obligation to include foreign exchange swaps and foreign exchange forwards in the calculation of a person’s substantial position in swaps or substantial counterparty exposure for purposes of determining if a person is a major swap participant under Commission Regulation 1.3(hhh),¹ or the calculation of the aggregate gross notional amount of swaps connected with swap dealing activity for purposes of determining when and if a person is no longer entitled to rely on the de minimis exception from swap dealer registration set forth in Commission Regulation 1.3(ggg)(4)² and must register with the Commission as a swap dealer, pending a determination by the Secretary of the Treasury (“Secretary”) to exempt foreign exchange swaps and foreign exchange forwards from the Commodity Exchange Act (“CEA”). This letter also is in response to requests that, pending such determination, persons who would meet the definitions of the terms commodity pool operator (“CPO”) and commodity trading advisor (“CTA”) in the CEA solely as a result of their foreign exchange swap and forward activity not be required to register in those capacities.

¹ 17 CFR 1.3(hhh), 77 FR 30596, 30746 (May 23, 2012).

² 17 CFR 1.3(ggg)(4), 77 FR at 30744.

The CEA, as amended by the Dodd-Frank Act, provides that “foreign exchange forwards”³ and “foreign exchange swaps”⁴ shall be considered “swaps” under the swap definition unless the Secretary issues a written determination that either foreign exchange swaps, foreign exchange forwards, or both: (i) should not be regulated as swaps; and (ii) are not structured to evade the Dodd-Frank Act in violation of any rule promulgated by the Commission pursuant to section 721(c) of the Dodd-Frank Act.⁵ The Secretary published in the Federal Register on October 28, 2010, a request for comment as to whether an exemption from the swap definition for foreign exchange swaps, foreign exchange forwards, or both, is warranted, and on the application of the statutory factors that the Secretary must consider in making a determination regarding whether to exempt these products.⁶ Subsequently, the Secretary published in the Federal Register on May 5, 2011, a proposed determination to exempt both foreign exchange swaps and foreign exchange forwards from the definition of the term “swap” in the CEA.⁷ A final determination to exempt has not yet been issued by the Secretary.

Pursuant to their authority under the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”),⁸ the Commission and the Securities and Exchange Commission (“SEC”) adopted joint rules to explicitly define the term “swap” to include foreign

³ A foreign exchange forward is defined in the CEA as “a transaction that solely involves the exchange of two different currencies on a specific future date at a fixed rate agreed upon on the inception of the contract covering the exchange.” CEA section 1a(24), 7 U.S.C. 1a(24).

⁴ A foreign exchange swap is defined as in the CEA as follows:
a transaction that solely involves—

- (A) an exchange of 2 different currencies on a specific date at a fixed rate that is agreed upon on the inception of the contract covering the exchange; and
- (B) a reverse exchange of the 2 currencies described in subparagraph (A) at a later date and at a fixed rate that is agreed upon on the inception of the contract covering the exchange.

CEA section 1a(25), 7 U.S.C. 1a(25).

⁵ See section 1a(47)(E)(i) of the CEA, 7 U.S.C. 1a(47)(E)(i). Under the Dodd-Frank Act, if foreign exchange forwards or foreign exchange swaps are no longer considered swaps due to a determination by the Secretary, nevertheless, certain provisions of the CEA added by the Dodd-Frank Act would continue to apply to such transactions. Specifically, those transactions still would be subject to certain requirements for reporting swaps, and swap dealers and major swap participants engaging in such transactions still would be subject to certain business conduct standards. See, e.g., sections 1a(47)(E)(iii) and (iv) of the CEA, 7 U.S.C. 1a(47)(E)(iii) and (iv) (reporting and business conduct standards, respectively). In addition, a determination by the Secretary does not exempt any foreign exchange forward or foreign exchange swap traded on a designated contract market or a swap execution facility, or cleared by a derivatives clearing organization, from any applicable antifraud or anti-manipulation provision under the CEA. See sections 1a(47)(F)(i) and 1b(c) of the CEA, 7 U.S.C. 1a(47)(F)(i) and 1b(c). Nor does it affect the CFTC’s jurisdiction over retail foreign currency agreements, contracts, or transactions pursuant to section 2(c)(2) of the CEA, 7 U.S.C. 2(c)(2). See section 1a(47)(F)(ii) of the CEA, 7 U.S.C. 1a(47)(F)(ii).

⁶ See *Determinations of Foreign Exchange Swaps and Forwards*, 75 FR 66829 (Oct. 28, 2010).

⁷ See *Determination of Foreign Exchange Swaps and Foreign Exchange Forwards Under the Commodity Exchange Act, Notice of Proposed Determination*, 76 FR 25774 (May 5, 2011) (“Notice of Proposed Determination”). The comment period on the Secretary’s proposed determination closed on June 6, 2011.

⁸ See section 712(d) of the Dodd-Frank Act.

exchange forwards and foreign exchange swaps (as those terms are defined in the CEA), in order to include in one rule the definitions of those terms and the related regulatory authority with respect to foreign exchange forwards and foreign exchange swaps.⁹ The final rules incorporate the provision of the Dodd-Frank Act that foreign exchange forwards and foreign exchange swaps will no longer be considered swaps if the Secretary issues the written determination described above to exempt such products from the swap definition. They also reflect the continuing applicability of certain reporting requirements and business conduct standards in the event that the Secretary makes such a determination. These joint final rules become effective on October 12, 2012.

After the October 12, 2012 effective date, all swaps entered into by a person in connection with the person's swap dealing activities are relevant in determining whether the person is within the swap dealer definition and therefore must register as a swap dealer. Also, beginning on October 12, 2012 a person must begin to calculate whether it is within the definition of major swap participant in Commission Regulation 1.3(hhh). This would include foreign exchange swaps and foreign exchange forwards, unless the Secretary determines to issue the written determination described above and such determination becomes effective before October 12, 2012.¹⁰ Similarly, among the changes made by the Dodd-Frank Act to the CEA were to include within the CPO definition the operator of a collective investment vehicle that trades swaps, and to include within the CTA definition a person who provides advice concerning swaps,¹¹ which in both cases would include foreign exchange forwards and foreign exchange swaps absent a determination by the Secretary described above, and may require registration in those capacities absent an exemption or exclusion.

Several parties have commented that for a number of parties who are solely or primarily engaged in foreign exchange swap and forward activity, whether they will be required to apply to be registered as swap dealers or major swap participants will be dependent upon whether the Secretary issues a final determination to exempt foreign exchange swaps and forwards. If the Secretary does so before October 12, 2012, such parties would not be required to apply to be registered. If the Secretary does so shortly after October 12, 2012, these parties state that it is unclear whether or not such parties would still be required to apply to be registered due to their activities prior to the Secretary's determination to exempt such instruments by a deadline which

⁹ *Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping*, issued July 18, 2012 (to be codified at 17 CFR pt. 1), 77 FR 48207 (August 13, 2012). The Commission also adopted anti-evasions rules, including an anti-evasion rule with respect to foreign exchange swaps and forwards. Under that rule, an interest rate swap or currency swap (including certain foreign exchange transactions that the Commissions have provided in their regulations are not foreign exchange swaps or foreign exchange forwards) that is willfully structured as a foreign exchange forward or foreign exchange swap to evade any provision of Subtitle A of Title VII of the Dodd-Frank Act shall be deemed a swap for purposes of Subtitle A and the Commission's regulations thereunder.

¹⁰ The exclusion of foreign exchange forwards and foreign exchange swaps would become effective upon the Secretary's submission of the determination to exempt to the appropriate Congressional Committees. See sections 1a(47)(E)(ii) and 1b of the CEA, 7 U.S.C. 1a(47)(E)(ii) and 1b.

¹¹ See Section 721(a) of the Dodd-Frank Act. The CPO and CTA definitions, as amended, are codified at CEA sections 1a(11) and 1a(12), 7 U.S.C. 1a(11) and 1a(12), respectively.

could be December 31, 2012 for swap dealers in certain cases, or whether they would be allowed to refrain from applying, withdraw their application to be registered or make a new application to cancel their registration. These parties state that these questions about registration are subjecting them and the foreign exchange markets generally to significant uncertainty. To avoid this uncertainty, these parties also have suggested that such market participants may withdraw from the foreign exchange swap and foreign exchange forward markets, or be forced to restructure their activities. Similar concerns have been raised with respect to operators of collective investment vehicles that trade foreign exchange swaps and forwards and persons who provide advice concerning foreign exchange swaps and forwards, and would have to apply to be registered with the Commission as commodity pool operators or commodity trading advisors solely as a result of these respective activities.

Based on the information provided by these parties, the Division believes that time-limited no-action relief is warranted in order to alleviate the uncertainty on market participants who engage solely or primarily in foreign exchange swap and foreign exchange forward swap dealing activity in the event that, shortly after October 12, 2012, the Secretary issues a determination to exempt foreign exchange swaps and foreign exchange forwards from the definition of the term “swap” in the CEA. However, the Division does not believe it is appropriate that this limited no-action relief would delay the date by which an entity must register as a swap dealer, if the entity enters into other types of swaps in connection with its swap dealing activities in excess of the de minimis thresholds.

Accordingly, the Division will not recommend enforcement action to the Commission against an entity for failure to include, in its calculation of the aggregate gross notional amount of swaps connected with its swap dealing activity for purposes of Commission Regulation § 1.3(ggg)(4), any foreign exchange swap or foreign exchange forward that is covered by an exemption by the Secretary under section 1a(47)(E)(i) of the CEA that is effective prior to December 31, 2012. However, notwithstanding the foregoing, if by December 31, 2012, an entity enters into other types of swaps in connection with its swap dealing activities in excess of either of the gross notional amount thresholds in CFTC regulation § 1.3(ggg)(4)(i),¹² then such foreign exchange swaps and foreign exchange forwards must be considered for purposes of the entity’s determination of the date by which it must apply to be registered as a swap dealer.

For example, consider an entity that, in the month of October 2012 (following October 12, 2012) enters into foreign exchange swaps in connection with its swap dealing activities with an aggregate gross notional amount of \$5 billion, and also enters into interest rate swaps in connection with its swap dealing activities with an aggregate gross notional amount of \$4 billion. Under Commission Regulation § 1.3(ggg)(4), this entity must apply to be registered as a swap dealer by no later than December 31, 2012.¹³ However, if the Secretary were to determine to

¹² Such an entity would include, for example, an entity that following October 12, 2012 and prior to December 31, 2012 enters into, in connection with its swap dealing activities, swaps that are not foreign exchange swaps or foreign exchange forwards and that, in the aggregate, exceed either of the gross notional amount thresholds in CFTC regulation § 1.3(ggg)(4)(i).

¹³ December 31, 2012 is the latest date that swap dealers which exceed a de minimis threshold in October 2012 would be required to register with the Commission. *See* CFTC Staff Frequently Asked Questions on Timing of Swap Dealer Registration Rules (Sept. 10, 2012).

exclude such foreign exchange swaps from the definition of the term “swap” with an effective date of November 15, 2012, then the entity may disregard all such excluded foreign exchange swaps for purposes of such aggregate gross notional amount calculation. However, if in the month of November 2012 the entity enters into interest rate swaps in connection with its swap dealing activities with an aggregate gross notional amount of \$5 billion, then (because it has entered into interest rate swaps in connection with its swap dealing activities with an aggregate gross notional amount of more than the \$8 billion de minimis threshold by December 31, 2012), its foreign exchange swaps must be considered for purposes of determining the date by which it must register as a swap dealer, and therefore the entity must apply to be registered as a swap dealer by no later than December 31, 2012.

Also, the Division will not recommend enforcement action to the Commission against an entity for failure to include, in its calculation of its substantial position in swaps or substantial counterparty exposure for purposes of Commission Regulation §1.3(hhh), any foreign exchange swap or foreign exchange forward that is covered by an exemption by the Secretary under section 1a(47)(E)(i) of the CEA that is effective prior to December 31, 2012.

In addition, the Division believes that time-limited no-action relief is warranted in order to alleviate uncertainty with respect to operators of collective investment vehicles that trade foreign exchange swaps and forwards and persons who provide advice concerning foreign exchange swaps and forwards, and would have to register with the Commission as commodity pool operators or commodity trading advisors solely as a result of these respective activities, in the event that, shortly after October 12, 2012, the Secretary issues a determination to exempt foreign exchange swaps and foreign exchange forwards from the definition of the term “swap.” Accordingly, the Division will not recommend enforcement action to the Commission against a person who operates a collective investment vehicle that trades foreign exchange swaps and forwards or a person who provides advice concerning foreign exchange swaps and forwards, and would have to apply to be registered with the Commission as a commodity pool operator or commodity trading advisor solely as a result of these respective activities, for failure to apply to be registered with the Commission, if the Secretary issues a final determination to exempt foreign exchange swaps and forwards from the term “swap” that becomes effective before December 31, 2012.

This letter, and the positions taken herein, represent the view of the Division only, and do not necessarily represent the position or view of the Commission or of any other office or division of the Commission. The relief issued by this letter does not excuse the affected persons from compliance with any other applicable requirements contained in the CEA or in the Commission’s regulations issued thereunder. Further, this letter, and the relief contained herein, is based upon the information made available to the Division. Any different or changed material facts or circumstances might render this letter void.

Should you have any questions, please do not hesitate to contact Frank Fisanich, Chief Counsel, at 202-418-5949, or Ward Griffin, Associate Chief Counsel, at 202-418-5425.

Very truly yours,

Gary Barnett
Director

cc: Regina Thoele, Compliance
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