



## U.S. COMMODITY FUTURES TRADING COMMISSION

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Division of Clearing and Risk

Ananda Radhakrishnan  
Director

CFTC Letter No. 13-43  
No-Action  
July 11, 2013  
Division of Clearing and Risk

Mr. Christophe Hémon  
LCH.Clearnet SA  
CEO  
18 rue du Quatre Septembre  
Paris, France 750002

Re: No-Action Relief with Regard to Sections 5b(a) and 2(h)(1)(A) of the Commodity Exchange Act and Implementing Regulations Thereunder

Dear Mr. Hémon:

This is in response to your letter dated July 2, 2013 (“Letter”), to the Division of Clearing and Risk (“Division”) of the Commodity Futures Trading Commission (“Commission”). In the Letter, you request that the Division confirm that it will not recommend that the Commission take enforcement action against (1) Banque Centrale de Compensation, doing business as LCH.Clearnet SA (“LCH.C SA”) for failure to register as a derivatives clearing organization (“DCO”) pursuant to Section 5b(a) of the Commodity Exchange Act (“CEA”),<sup>1</sup> or (2) clearing members of LCH.C SA that are U.S. persons (each, a “U.S. CDS Clearing Member”) for failure to clear certain credit default swaps (“CDS”) on a broad-based index of reference entities (“Index CDS”) through a registered DCO pursuant to Section 2(h)(1)(A) of the CEA and the implementing regulations thereunder as applicable.<sup>2</sup>

Under this proposed relief, LCH.C SA would be permitted to clear Index CDS transactions based on certain iTraxx Europe indices. In addition, U.S. CDS Clearing Members would be permitted to clear proprietary positions in such Index CDS through a DCO that is not registered with the Commission. You have requested that such relief be effective until the earlier of December 31, 2013, or the date upon which the Commission

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<sup>1</sup> 7 U.S.C. 7a-1(a).

<sup>2</sup> 7 U.S.C. 2(h)(1)(A); 17 C.F.R. Part 50.

approves LCH.C SA's pending application for registration as a DCO with respect to its Index CDS clearing business.<sup>3</sup>

### Statement of Facts

Based upon the representations made by LCH.C SA to the Division, including the representations made in the Letter and in LCH.C SA's DCO application, we understand the relevant facts to be as follows:

LCH.C SA is a French subsidiary of LCH.Clearnet Group Limited, a holding company incorporated in the United Kingdom, and operates as a clearing house subject to French law. Its principal office is in Paris, and it operates branches in Amsterdam and Brussels and a representative office in Portugal. Under French law, LCH.C SA is regulated both as a credit institution by the Prudential Control Authority (Autorité de Contrôle Prudentiel) ("ACP") and as a clearing house by the Financial Markets Authority (Autorité des Marchés Financiers) ("AMF"). The ACP and AMF also regulate LCH.C SA as an investment service provider. In addition, LCH.C SA is subject to regulation as a securities settlement system operator by the Banque de France and the AMF.

LCH.C SA launched its clearing services for Index CDS on March 29, 2010, and it has proposed to expand these services to additional members and customers.<sup>4</sup> In connection with this proposed expansion of its business, LCH.C SA filed an initial application for DCO registration on April 25, 2012 and amended its application on November 2, 2012 and May 16, 2013.

Index CDS contracts currently accepted for clearing by LCH.C SA include Index CDS on the following iTraxx Europe indices:

- the benchmark iTraxx Europe Main index;
- the iTraxx Europe HiVol index; and
- the iTraxx Europe Crossover Index.

LCH.C SA accepts for clearing 3-, 5-, 7-, and 10-year maturity CDS on the iTraxx indices listed above, from series 5 and above. The Commission recently adopted regulations to establish a clearing requirement under Section 2(h)(1)(A) of the CEA with respect to

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<sup>3</sup> By letter dated June 21, 2013, LCH.C SA requested that the review period for its DCO application be extended until December 31, 2013.

<sup>4</sup> LCH.C SA has proposed to extend its Index CDS clearing business to U.S. proprietary and U.S. customer clearing. The scope of the relief provided herein *does not* extend to customer clearing by U.S. CDS Clearing Members or U.S. customer clearing by any LCH.C SA clearing member. The term "customer" is defined in § 1.3(k) of the Commission's regulations, 17 C.F.R. § 1.3(k). *See* Adaptation of Regulations to Incorporate Swaps, 77 Fed. Reg. 66,288, 66,316 (Nov. 2, 2012).

certain classes of interest rate swaps and CDS.<sup>5</sup> Certain Index CDS products accepted for clearing by LCH.C SA are among those covered by the clearing determination.

#### Discussion of Request for No-Action Relief and Applicable Legal Requirements

The Division accepts, without independent analysis, LCH.C SA's representation that the Index CDS contracts subject to its request are swaps under the CEA and Commission regulations. It also accepts, without further inquiry, that certain of LCH.C SA's prospective clearing members may be U.S. persons.

On October 12, 2012, the Commission's regulatory definition of the term "swap," which includes Index CDS, became effective.<sup>6</sup> Section 5b(a) of the CEA provides that a derivatives clearing organization may not perform the functions of a DCO with respect to swaps unless it is registered with the Commission.<sup>7</sup> Section 2(h)(1)(A) of the CEA states that swaps that are required to be cleared must be submitted to a registered DCO or a DCO that is exempt from registration.<sup>8</sup>

LCH.C SA's request for relief is consistent with recent requests for Division no-action letters permitting similarly-situated non-U.S. clearing organizations to clear swaps for U.S. persons prior to becoming registered with the Commission as a DCO.<sup>9</sup> Granting the relief requested by LCH.C SA during the pendency of its DCO registration application is appropriate in order to promote competition and enhance choice in clearing services for Index CDS, particularly iTraxx products.

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<sup>5</sup> See Clearing Requirement Determination Under Section 2(h) of the CEA, 77 Fed. Reg. 74,284 (Dec.13, 2012) (adopting Part 50 of the Commission's regulations).

<sup>6</sup> See Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping, 77 Fed. Reg. 48,207 (Aug. 13, 2012).

<sup>7</sup> Section 5b(a) of the CEA, 7 U.S.C. 7a-1(a), states: "Except as provided in paragraph (2), it shall be unlawful for a derivatives clearing organization, directly or indirectly, to make use of the mails or any means or instrumentality of interstate commerce to perform the functions of a derivatives clearing organization with respect to . . . (B) a swap. (2) EXCEPTION. – Paragraph (1) shall not apply to a derivatives clearing organization that is registered with the Commission."

<sup>8</sup> Section 5b(h) of the CEA, 7 U.S.C. 7a-1(h), permits the Commission to exempt a DCO from registration for the clearing of swaps to the extent that the Commission determines that such DCO is subject to comparable, comprehensive supervision by the Securities and Exchange Commission or the appropriate government authorities in the home country of the DCO. At the present time, no DCO has sought or been granted an exemption from registration for the clearing of swaps.

<sup>9</sup> See CFTC No-Action Letter No. 12-56 (Dec. 17, 2012) (granting no action relief to Japan Securities Clearing Corporation and certain of its clearing members); and CFTC No-Action Letter No. 12-63 (Dec. 21, 2012) (granting no-action relief to Singapore Exchange Derivatives Clearing Limited and certain of its clearing members).

Grant of No-Action Relief

Based on the facts presented and the representations you have made, the Division will not recommend that the Commission take enforcement action against (i) LCH.C SA for failure to register as a DCO pursuant to the requirements of Section 5b(a) of the CEA, or (ii) U.S. CDS Clearing Members for failure to clear Index CDS through a registered or exempt DCO pursuant to the requirements of Section 2(h)(1)(A) of the CEA and the implementing regulations thereunder as applicable, subject to the following conditions:

- (1) Product Scope. This relief is limited to Index CDS currently accepted for clearing by LCH.C SA;
- (2) Participant Scope. The relief applies to LCH.C SA and to its prospective U.S. CDS Clearing Members in connection with their proprietary<sup>10</sup> Index CDS clearing business (LCH.C SA will not accept, and no LCH.C SA clearing member will offer for clearing through LCH.C SA, Index CDS on behalf of a U.S. customer); and
- (3) Limited Duration. The no-action relief shall expire at the earlier of: (i) December 31, 2013 or (ii) the date upon which LCH.C SA becomes registered as a DCO with respect to its Index CDS clearing business.<sup>11</sup>

The position taken herein concerns enforcement action only and does not represent a legal conclusion with respect to the applicability of any provision of the CEA or the Commission's regulations. In addition, the Division's position does not necessarily reflect the views of the Commission or any other division or office of the Commission. Because this position is based upon the representations contained in the Letter and in LCH.C SA's DCO application, it should be noted that any different, changed, or omitted material facts or circumstances may require a different conclusion or render this letter void. Finally, as with all no-action letters, the Division retains the authority to condition further, modify, suspend, terminate, or otherwise restrict the terms of the no-action relief provided herein, in its discretion.

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<sup>10</sup> The term "proprietary account" is defined in § 1.3(y) of the Commission's regulations, 17 C.F.R. § 1.3(y). The relief granted herein to U.S. CDS Clearing Members includes transactions of a parent or affiliate of a U.S. CDS Clearing Member.

<sup>11</sup> Should the Commission deny LCH.C SA's application for DCO registration, the Division will provide LCH.C SA and its U.S. CDS Clearing Members with guidance and, as appropriate, no-action relief to facilitate the orderly disposition of open positions.

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Should you have any questions, please do not hesitate to contact me at (202) 418-5188, or Heidi Rauh, Special Counsel, at (312) 596-0644.

Sincerely,

Ananda Radhakrishnan  
Director