



U.S. COMMODITY FUTURES TRADING COMMISSION

Three Lafayette Centre
1155 21st Street, NW, Washington, DC 20581
Telephone: (202) 418-5977
Facsimile: (202) 418-5407
gbarnett@cftc.gov

CFTC Letter No. 13-80
No-Action
December 23, 2013
Division of Swap Dealer and Intermediary Oversight

Re: No-Action Relief from Certain Conditions of the Swap Dealer Exclusion for Registered Floor Traders

Ladies and Gentlemen:

This letter is in response to requests from multiple market participants registered as floor traders with the U.S. Commodity Futures Trading Commission (“**Commission**”) to the Division of Swap Dealer and Intermediary Oversight (“**DSIO**”) of the Commission for relief from the aggregation requirement of Commission Regulation (“**Regulation**”) 1.3(ggg)(4)(i) and certain conditions under Regulation 1.3(ggg)(6)(iv) that, if met, permit a floor trader to exclude swaps entered into either in its capacity as a floor trader as defined by section 1(a)(23) of the CEA or on or subject to the rules of a swap execution facility (“**SEF**”) from its aggregate gross notional amount of swap transactions in determining whether it may rely on the de minimis exception from SD registration set forth in Regulation 1.3(ggg)(4).¹

Applicable Regulatory Requirements

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010,² in relevant part, added § 1a(49) to the Commodity Exchange Act (the “**CEA**” or “**Act**”), which defined the term “swap dealer” for purposes of the CEA.³ Section 1a(49)(D) of the CEA states that “[t]he Commission shall exempt from designation as a swap dealer an entity that engages in a de minimis quantity of swap dealing in connection with transactions with or on behalf of its customers. The Commission shall promulgate regulations to establish factors with respect to the making of this determination to exempt.”⁴

On May 23, 2012, the Commission, jointly with the Securities and Exchange Commission (“**SEC**”), published final rules to further define “swap dealer,” “security-based swap dealer,” “major swap participant,” “major security-based swap participant,” and “eligible

¹ 17 CFR § 1.3(ggg)(4); *see* Further Definition of “Swap Dealer,” “Security-Based Swap Dealer,” “Major Swap Participant,” “Major Security-Based Swap Participant,” and “Eligible Contract Participant,” 77 FR 30596, 30744 (May 23, 2012) (hereinafter the “Entity Definition Rules”).

² Pub. L. No. 111-203, 124 Stat. 1376 (2010).

³ 7 U.S.C. § 1a(49).

⁴ 7 U.S.C. § 1a(49)(D).

contract participant”.⁵ Pursuant to the Entity Definition Rules, Regulation 1.3(ggg)(4)(i) provides that a person shall not be deemed an SD if the aggregate gross notional amount of the swap dealing activity of such person—or any other entity controlling, controlled by, or under common control with the person (an “**affiliate**”)—falls below certain thresholds.⁶

The Entity Definition Rules also provide that certain swaps are not to be considered in determining whether a person is an SD.⁷ In particular, Regulation 1.3(ggg)(6)(iv) provides that:

[i]n determining whether a person is a swap dealer, each swap that the person enters into in its capacity as a floor trader as defined by section 1a(23) of the Act or on or subject to the rules of a swap execution facility shall not be considered for the purpose of determining whether the person is a swap dealer if the person:

- (A) Is registered with the Commission as a floor trader pursuant to § 3.11 of this chapter;
- (B) Enters into swaps with proprietary funds for that trader’s own account solely on or subject to the rules of a designated contract market or swap execution facility and submits each such swap for clearing to a derivatives clearing organization;
- (C) Is not an affiliated person of a registered swap dealer;
- (D) Does not directly, or through an affiliated person, negotiate the terms of swap agreements, other than price and quantity or to participate in a request for quote process subject to the rules of a designated contract market or a swap execution facility;
- (E) Does not directly or through an affiliated person offer or provide swap clearing services to third parties;

⁵ See Entity Definition Rules, *supra* note 1.

⁶ *Id.* at 30744. Regulation 1.3(ggg)(4)(i) provides that:

a person that is not currently registered as a swap dealer shall be deemed not to be a swap dealer as a result of its swap dealing activity involving counterparties, so long as the swap positions connected with those dealing activities into which the person—or any other entity controlling, controlled by or under common control with the person—enters over the course of the immediately preceding 12 months (or following the effective date of final rules implementing Section 1a(47) of the Act, 7 U.S.C. 1a(47), if that period is less than 12 months) have an aggregate gross notional amount of no more than \$3 billion, subject to a phase in level of an aggregate gross notional amount of no more than \$8 billion.

⁷ See Entity Definition Rules, 77 FR at 30746; *see also* Regulation 1.3(ggg)(6), 17 CFR § 1.3(ggg)(6).

- (F) Does not directly or through an affiliated person enter into swaps that would qualify as hedging physical positions pursuant to paragraph (ggg)(6)(iii) of this section or hedging or mitigating commercial risk pursuant to paragraph (kkk) of this section (except for any such swap executed opposite a counterparty for which the transaction would qualify as a bona fide hedging transaction);
- (G) Does not participate in any market making program offered by a designated contract market or swap execution facility; and
- (H) Notwithstanding the fact such person is not registered as a swap dealer, such person complies with §§ 23.201, 23.202, 23.203, and 23.600 of this chapter with respect to each such swap as if it were a swap dealer.⁸

The definition of the term “floor trader” includes a person entering into swaps on a “contract market.”⁹ The exclusion from the de minimis calculation for SD registration provided by Regulation 1.3(ggg)(6)(iv) for certain swaps entered into by persons registered as floor traders also encompasses swaps that a registered floor trader enters into on or subject to the rules of a SEF, in addition to on or subject to the rules of a designated contract market (“**DCM**”), so long as the swap meets the conditions stated in the exclusion.¹⁰

On August 13, 2012, the Commission, jointly with the SEC, issued final rules further defining the products terms “swap,” “security-based swap,” “security-based swap agreement,” and “mixed swap.”¹¹ The effective date of these joint final rules was October 12, 2012. All swaps a person enters into in connection with its swap dealing activities on or after October 12, 2012, are relevant in determining whether the person meets the SD definition and therefore must register with the Commission as a SD.

Summary of Request for Relief

The floor traders requesting relief argue that absent further relief, Regulation 1.3(ggg)(6)(iv) may not serve its intended purpose, which is to avoid subjecting floor traders to potentially duplicative SD regulations as a result of the swaps they enter into in their capacity as floor traders by allowing them to exclude those swaps from their SD de minimis calculation. Specifically, the floor traders raise the following issues:

⁸ *Id.* at 30746; 17 CFR § 1.3(ggg)(6)(iv).

⁹ *See* CEA § 1a(23).

¹⁰ *See* Entity Definition Rules, 77 FR at 30614, n. 236.

¹¹ Further Definition of “Swap,” “Security-Based Swap,” and “Security-Based Swap Agreement”; Mixed Swaps; Security-Based Swap Agreement Recordkeeping, 77 FR 48208 (Aug. 13, 2012).

- (1) Regulation 1.3(ggg)(6)(iv) states that “each swap that the [floor trader] enters into . . . on or subject to the rules of a [SEF or DCM] shall not be considered for the purpose of determining whether the [floor trader] is a swap dealer” but does not expressly indicate that an affiliate of the floor trader should not consider such swaps in its own SD de minimis calculation for purposes of determining whether it is an SD pursuant to the aggregation requirements of Regulation 1.3(ggg)(4)(i);
- (2) Regulation 1.3(ggg)(6)(iv) does not expressly state that floor traders should not consider the swaps of an affiliate for purposes of determining whether it is an SD pursuant to the aggregation requirements of Regulation 1.3(ggg)(4)(i);
- (3) Regulation 1.3(ggg)(6)(i) states that a person’s swaps with majority-owned affiliates shall not be considered in determining whether a person is an SD, but Regulation 1.3(ggg)(6)(iv)(B) prohibits a floor trader seeking to comply with Regulation 1.3(ggg)(6)(iv) from entering into swaps that are not executed “solely on or subject to the rules of a [DCM or SEF]” and submitted for clearing to a DCO, thus effectively such floor traders are not permitted to hedge risks through inter-affiliate swaps to the same extent as other market participants;
- (4) Regulation 1.3(ggg)(6)(iv)(G) prohibits a floor trader from participating in “any market making program offered by a designated contract market or swap execution facility,” but does not limit this condition to swap market making programs, thereby preventing floor traders seeking to comply with Regulation 1.3(ggg)(6)(iv) from participating in non-swaps-based market making programs offered by a SEF or DCM; and
- (5) Regulation 1.3(ggg)(6)(iv)(G) does not distinguish between market making programs in which a person is contractually obligated to make two-way markets in a particular product and other common programs sponsored by SEFs and DCMs that merely offer discounts based on transaction volume or fee rebates or equity in exchange for providing liquidity (i.e., “maker/taker” programs).

Accordingly, the floor traders request: (i) relief for their affiliates from considering the swaps of a floor trader that is in compliance with Regulation 1.3(ggg)(6)(iv) in determining whether such affiliates are required to register as SDs; (ii) relief for floor traders in compliance with Regulation 1.3(ggg)(6)(iv) from considering the swaps of an affiliate in determining whether such floor traders are required to register as SDs; (iii) relief for floor traders in compliance with Regulation 1.3(ggg)(6)(iv) from condition (B) of 1.3(ggg)(6)(iv) with respect to swaps with their majority-owned affiliates that are not executed on or subject to the rules of a DCM or SEF or not submitted for clearing to a DCO; (iv) relief from the market making prohibition in Regulation 1.3(ggg)(6)(iv)(G) with respect to participation in market making programs for products other than swaps; and (v) relief from the market making prohibition in Regulation 1.3(ggg)(6)(iv)(G) with respect to participation in programs that solely offer discounts based on transaction volume or fee rebates or equity in exchange for providing liquidity.

DSIO No-Action Position

With respect to issue (1) above, DSIO confirms that, pursuant to Regulation 1.3(ggg)(4)(i), for purposes of determining whether they are SDs, affiliates of registered floor traders should not consider in their own SD de minimis calculations any swaps entered into by such floor traders in compliance with Regulation 1.3(ggg)(6)(iv). Regulation 1.3(ggg)(4) requires affiliates to aggregate their swap dealing activities for purposes of determining whether they should register as SDs. Because Regulation 1.3(ggg)(6)(iv) indicates that swaps entered into pursuant to its terms “shall not be considered for the purpose of determining whether the person is a swap dealer,” affiliates should also not consider those swaps for purposes of determining whether they should register as SDs.

With respect to issues (2), (3), (4) and (5) above, DSIO believes that no-action relief is appropriate. Accordingly, DSIO will not recommend that the Commission take an enforcement action against any person for:

- (a) Failure to register as an SD solely by virtue of not aggregating with its own swaps the swaps of any affiliate, provided that such person is in compliance with Regulation 1.3(ggg)(6)(iv);
- (b) Failure to meet the requirements of condition (B) of Regulation 1.3(ggg)(6)(iv) solely because such person enters into a swap with a majority-owned affiliate that is not executed on or subject to the rules of a DCM or SEF, or failure to meet the requirements of condition (B) of Regulation 1.3(ggg)(6)(iv) solely because such person enters into a swap with a majority-owned affiliate that is not submitted for clearing to a DCO;
- (c) Failure to meet the requirements of condition (G) of Regulation 1.3(ggg)(6)(iv) solely because such person participates in one or more market making programs offered by a DCM that do not apply or relate to swaps; or
- (d) Failure to meet the requirements of condition (G) of Regulation 1.3(ggg)(6)(iv) solely because such person participates in one or more programs offered by a DCM or SEF that solely offers discounts based on the person’s transaction volume or fee rebates or equity in exchange for providing liquidity.

This letter, and the positions taken herein, represent the views of DSIO 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 persons relying on it from compliance with any other applicable requirements contained in the Act or in the Regulations issued thereunder. This letter does not create or confer any rights for or obligations on any person or persons subject to compliance with the CEA that bind the Commission or any of its other offices or divisions. Further, this letter, and the relief contained herein, is based upon the representations made to DSIO. Any different, changed or omitted material facts or circumstances might render this no-action relief void.

Floor Traders

Page 6

Should you have any questions, please do not hesitate to contact me at (202) 418-5977; Frank Fisanich, Chief Counsel, at (202) 418-5949; Ward Griffin, Associate Chief Counsel, at (202) 418-5425.

Very truly yours,

Gary Barnett
Director
Division of Swap Dealer and Intermediary Oversight

cc: Regina Thoele, Compliance
National Futures Association, Chicago

Jamila A. Piracci, OTC Derivatives
National Futures Association, New York