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Division of Clearing and Risk

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CFTC Letter No. 14-107
No-Action
August 18, 2014
DCR

Mr. R. Sridharan
Managing Director
The Clearing Corporation of India Ltd.
CCIL Bhavan
College Lane, Off. S K Bole Road
Dadar (West)
Mumbai, India

Re: No-Action Relief with Regard to Section 5b(a) of the Commodity Exchange Act and Commission Regulations Thereunder

Dear Mr. Sridharan:

This letter responds to your letter dated July 15, 2014 ("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 the Clearing Corporation of India Ltd. ("CCIL") for failure to register as a derivatives clearing organization ("DCO") pursuant to Section 5b(a) of the Commodity Exchange Act ("CEA")[1] should CCIL provide certain clearing services to U.S. persons.

Under this requested relief, CCIL would be permitted to clear Indian Rupee-denominated interest rate swaps ("INR IRS") and Indian Rupee-denominated forward-rate agreements (INR FRA") for the proprietary trades of clearing members[2] that are U.S. persons ("U.S. Clearing Members"). You request that such relief be effective until the date upon which the Commission, acting pursuant to its authority under Section 5b(h) of the CEA, exempts CCIL from the DCO registration requirement of the CEA.[3] You represent that CCIL intends to apply for an

[1] 7 U.S.C. § 7a-1(a).

[2] CCIL uses the term "clearing participant" throughout the Letter, which the Division understands to be equivalent to the term "clearing member," as defined in Commission Regulation 1.3(c), 17 C.F.R. § 1.3(c).

[3] Section 5b(h) of the CEA, 7 U.S.C. § 7a-1(h), permits the Commission to exempt a clearing organization from registration with the Commission as a DCO for the clearing of swaps to the extent that the Commission determines that such clearing organization is subject to comparable, comprehensive supervision by the Securities and Exchange Commission or the appropriate government authorities in the clearing organization's home country. At present, no clearing organization has been granted an exemption from DCO registration for the clearing of swaps.

exemption from registration as a DCO once the Commission addresses the process or specific criteria and conditions necessary to obtain exemptive relief.

Statement of Facts

Based on the representations made by CCIL in the Letter, the Division understands the relevant facts to be as follows:

CCIL was established in 2001 and, since February 2009, has been licensed and regulated by the Reserve Bank of India ("RBI") as a "Payment System," pursuant to India's Payment and Settlement Systems Act, 2007. In addition to its INR IRS and INR FRA clearing service, which was launched on March 28, 2014, CCIL also provides clearing services for Indian government securities, foreign exchange in the INR-USD currency pair, collateralized borrowing and loan obligations, and USD-INR foreign exchange forwards.

In July 2013, the RBI designated CCIL as a critical financial market infrastructure, considering CCIL's systemic importance to the financial markets regulated by the RBI. The RBI has also stated that CCIL is subject to regulation and supervision that is consistent with the CPSS-IOSCO Principles for Financial Market Infrastructures ("PFMIs"). In light of CCIL's supervision as a Payment System and that CCIL is subject to, on an ongoing basis, rules and regulations consistent with the PFMIs by the RBI, the RBI granted CCIL qualifying central counterparty[4] status, effective January 1, 2014.

Currently, CCIL offers its INR IRS and INR FRA clearing services to clearing members that are not U.S. persons. However, the Indian branches of certain U.S. banks have expressed interest in clearing such contracts at CCIL in order to benefit from a reduction in risk and capital requirements. These branches provide liquidity for, and represent a significant portion of the open interest in, the INR IRS and INR FRA markets.

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

The Division accepts, without independent analysis, CCIL's representation that the INR IRS and INR FRA contracts subject to its request are swaps under the CEA and Commission regulations.[5] The Division also accepts, without further inquiry, that certain of CCIL's prospective clearing members may be U.S. persons.

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[4] The Basel Committee on Banking Supervision generally provides that a qualifying central counterparty ("QCCP") is a central counterparty ("CCP") organized in a jurisdiction in which the relevant regulatory authority has established and applies to the CCP on an ongoing basis rules and regulations that are consistent with the PFMIs. Bank exposures arising from derivatives cleared at a CCP that has achieved QCCP status are afforded favorable capital treatment. *See* "Capital Requirements for Bank Exposures to Central Counterparties" (Apr. 2014), available at: www.bis.org/publ/bcbs282.pdf. *See also* Derivatives Clearing Organizations and International Standards, 78 Fed. Reg. 72,476, 72,478-79 (Dec. 2, 2013) (discussing the role of the PFMIs in international banking standards).

[5] The statutory definition of "swap" includes interest rate swaps. *See* Section 1a(47)(A) of the CEA, 7 U.S.C. § 1a(47)(A) ("[T]he term 'swap' means any agreement, contract, or transaction— . . . (iii) that provides on an executory basis for the exchange, on a fixed or contingent basis, of 1 or more payments based on the value or level

Section 5b(a) of the CEA provides that a clearing organization may not perform the functions of a DCO with respect to swaps unless it is registered with the Commission.[6] The Division, however, has recently granted no-action relief permitting similarly situated non-U.S. clearing organizations to clear certain swaps for U.S. persons prior to becoming registered with the Commission as a DCO or becoming exempted from registration, as applicable.[7] CCIL's request is generally consistent with the requests that prompted that relief. Granting the relief requested by CCIL pending consideration of its anticipated application for an exemption pursuant to Section 5b(h) of the CEA is appropriate in order to facilitate the centralized clearing of INR IRS and INR FRA. The Division notes, however, that the Commission has not established a regulatory framework for exempting a clearing organization from registration as a DCO pursuant to Section 5b(h) of the CEA. Accordingly, the Division's grant of no-action relief herein should not be interpreted to mean that the Commission will exempt CCIL from registration as a DCO.

Grant of No-Action Relief

Based on the facts presented and CCIL's representations to the Division, the Division will not recommend that the Commission take enforcement action against CCIL for failure to register as a DCO pursuant to the requirements of Section 5b(a) of the CEA, subject to the following conditions:

(1) Product Scope. The relief is limited to the INR IRS and INR FRA contracts accepted for clearing by CCIL.

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of 1 or more interest or other rates . . . including any agreement, contract, or transaction commonly known as— (I) an interest rate swap . . . ."). The statutory definition of "swap," as further defined in the implementing regulations, includes forward rate agreements. *See* Regulation 1.3(xxx)(2)(i), 17 C.F.R. § 1.3(xxx)(2)(i) ("The term swap includes, without limiting the meaning set forth in section 1a(47) of the Commodity Exchange Act . . . (E) [a] forward rate agreement.).

[6] 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."

[7] *See* CFTC Letter 14-87 (June 26, 2014) (granting no-action relief to Korea Exchange, Inc.); CFTC Letter 14-68 (May 7, 2014) (granting no-action relief to OTC Clearing Hong Kong Limited and certain of its clearing members); CFTC Letter 14-27 (Mar. 20, 2014) (extending previous grant of no-action relief to Eurex Clearing AG and certain of its clearing members); CFTC Letter 14-07 (Feb. 6, 2014) (granting no-action relief to ASX Clear (Futures) Pty Limited); CFTC Letter 13-73 (Dec. 19, 2013) (extending previous grant of no-action relief to Japan Securities Clearing Corporation and certain of its clearing members); CFTC Letter 13-44 (July 11, 2013) (granting no-action relief to Eurex Clearing AG and certain of its clearing members); CFTC Letter 13-43 (July 11, 2013) (granting no-action relief to LCH.Clearnet SA and certain of its clearing members); CFTC Letter 12-63 (Dec. 21, 2012) (granting no-action relief to Singapore Exchange Derivatives Clearing Limited and certain of its clearing members); and CFTC Letter 12-56 (Dec. 17, 2012) (granting no-action relief to Japan Securities Clearing Corporation and certain of its clearing members).

(2) Participant Scope. The relief applies to CCIL's clearing of proprietary trades[8] of U.S. Clearing Members.

(3) Reporting. If a clearing member clears through CCIL a swap (referred to as the "alpha" swap) that has been reported to a Commission-registered swap data repository ("SDR") pursuant to Part 45 of the Commission's regulations,[9] then CCIL must report to an SDR, pursuant to Part 45, data regarding the two swaps resulting from the novation of the alpha swap that had been submitted to CCIL for clearing (referred to as "beta" and "gamma" swaps).[10]

(4) Limited Duration. The no-action relief shall expire at the earlier of: (i) December 31, 2014,[11] or (ii) the date upon which the Commission either registers CCIL as a DCO under Section 5b(a) of the CEA or exempts CCIL from registration as a DCO under Section 5b(h) of the CEA.

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 on the representations contained in the Letter, 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,

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[8] *See* 17 C.F.R. § 1.3(y) (definition of "proprietary account").

[9] *See* Swap Data Recordkeeping and Reporting Requirements, 77 Fed. Reg. 2136 (Jan. 13, 2012) (adopting Part 45).

[10] Pursuant to Regulation 39.12(b)(6), 17 C.F.R. § 39.12(b)(6), during the clearing process, a swap submitted for clearing to a registered DCO (the alpha swap) is extinguished or terminated, and two new swaps (the beta and gamma swaps) are created. The registered DCO must then report the beta and gamma swaps to an SDR under Part 45 and associate the unique swap identifier of the alpha swap with the beta and gamma swaps in order for the Commission to confirm that such alpha swap was cleared. *See* Statement of the Commission concerning CME Rule 1001 (March 6, 2013), page 6, available at: http://www.cftc.gov/ucm/groups/public/@newsroom/documents/file/statementofthecommission.pdf; s*ee also* 17 C.F.R. § 45.4(a) ("[R]eporting counterparties and [DCOs] required to report swap continuation data must do so in a manner sufficient to ensure that all data in the [SDR] concerning the swap remains current and accurate, and includes all changes to the primary economic terms of the swap occurring during the existence of the swap."); 77 Fed. Reg. at 2153 ("[T]he final rule requires registered entities and reporting counterparties to report continuation data in a manner sufficient to ensure that the information in the SDR concerning the swap is current and accurate, and includes all changes to any of the primary economic terms of the swap.").

In order to avoid duplicative reporting for such transactions, CCIL should have rules that prohibit the Part 45 reporting of the beta and gamma swaps by the original counterparties to the alpha swap. These rules should make it clear to market participants that CCIL is reporting the beta and gamma swaps as if it were a registered DCO under the Part 45 rules.

[11] CCIL requested that the relief expire on the date on which the Commission exempts CCIL from the DCO registration requirement under Section 5b(h) of the CEA. To maintain consistency with the relief granted to other similarly situated non-U.S. clearing organizations, the relief expires on December 31, 2014.

modify, suspend, terminate, or otherwise restrict the terms of the no-action relief provided herein, in its discretion.

Should you have any questions, please do not hesitate to contact me at (202) 418-5188 or Shawn Durrani, Attorney-Advisor, at (202) 418-5048.

Sincerely,

Ananda Radhakrishnan
Director