
CFTC Proposes Order Further Extending Implementation of Certain Provisions of the Swap Regulatory Regime

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I. Introduction

In its May 10, 2012 Open Meeting, the Commodity Futures Trading Commission (CFTC or Commission) proposed a second amendment (Proposed Amendment) to the order delaying the effective date of swap regulation (July 2011 Order). The Proposed Amendment maintains much of the July 2011 Order, as amended last December (December 2011 Amendment), but includes some important changes, such as: (a) extending the expiry date; (b) accounting for the finalization of the swap entity definition rules; (c) including agricultural swaps in the exemption from the effective date; and (d) including exempt commercial markets (ECMs) and exempt boards of trade (EBOTs) in the exemption. Comments are due within 14 days of publication of the Proposed Amendment.

II. Previous Extensions

Under Section 754 of the Dodd-Frank Act (DFA), the provisions of Subtitle A of Title VII would have gone into effect on July 16, 2011. As the effective date approached, the Commission issued an order¹ in which it stated that, since the rulemakings defining the terms "swap," "swap dealer" (SD), "major swap participant" (MSP), and "eligible contract participant" (ECP) would not be completed by the effective date, and since several exemptions for transactions involving excluded and exempt commodities in the Commodity Exchange Act (CEA) would be removed as of that date, the Commission was extending to December 31, 2011 the implementation date of certain CEA provisions by: (a) exempting instruments and persons involved with swaps from those DFA provisions that specifically reference the further definition of entities and instruments under Sections 712(d) and 721(c);² and (b) exempting instruments, and persons involved with such instruments, in exempt or excluded (but not agricultural) commodities if they complied with Part 35 of the CEA.³ The July 2011 Order included a chart identifying the provisions that fell within one of these two categories, as well as those provisions that were not included in the exemption from the effective date. The July 2011 Order explicitly noted that the exemption did not: (a) limit the Commission's authority in regard to proscribing fraud; (b) apply to any CEA or DFA provisions that became effective before July 16, 2011; (c) affect any effective or compliance dates set by the Commission's DFA

rulemakings; (d) limit the Commission's authority to promulgate rules, orders, etc., prior to the effective date of the provisions of the DFA; or (e) affect the applicability of CEA provisions to futures, options on futures or the cash markets.

In December 2011, the Commission issued another order amending the July 2011 Order to extend the effective date through July 16, 2012.⁴ Noting that the Part 35 provisions would no longer be available after December 31, 2011, the December 2011 Amendment explicitly extended the effective date exemption to instruments and persons that would have fallen under old Part 35. This order also clarified that swaps on agricultural commodities could not be traded on ECMs or EBOTs, while providing an exemption until July 16, 2012 for instruments that were executed on grandfathered ECMs or EBOTs⁵ and cleared by registered derivatives clearing organizations (DCOs).

The Proposed Amendment is thus the third extension of the effective date. It substantially adopts the July 2011 Order and December 2011 Amendment, extending their relief through December 31, 2012. It also proposes some additional significant changes.

A. References to SDs, MSPs, and ECPs

Given that the Commission has recently finalized the entity definition rules for SDs, MSPs, and ECPs,⁶ the Proposed Amendment removes these terms from the original exemption, thereby only retaining the exemption for those provisions making reference to the term "swap." The exemption will expire on the earlier of December 31, 2012 or the effective date of the swap definition rule.

B. Agricultural Commodities

The Proposed Amendment removes the clearing prohibition for agricultural swaps, exempting all instruments and persons involved in an agricultural commodity from the CEA, provided that the instrument presently complies with Part 35 as it was prior to December 31, 2011, regardless of whether: (a) the instrument was part of a fungible class of agreements that are standardized as to their material and economic terms; and/or (b) the creditworthiness of any party having an obligation under the instrument would not be a material consideration in entering into or determining the terms of the instrument.

Further, in keeping with the recently finalized rule regarding agricultural swaps, the guidance in the Proposed Amendment confirms that agricultural swaps may only be entered into bilaterally and executed on a DCM or swap execution facility (SEF), and that they can be cleared like any other swap.⁷ This exemption expires on the earlier of December 31, 2012 or any other compliance date that the Commission may determine.

C. EBOTs and ECMs

The Proposed Amendment exempts from the effective date any instruments executed on EBOTs, ECMs or on markets that rely on Section 2(d)(2) of the CEA (as it was in effect prior to July 16, 2011).

The guidance notes that after the ECM/EBOT Grandfather Order expires in July, instruments still being traded on these markets will be able to rely on the Proposed Amendment. Relief will expire on the earlier of December 31, 2012 or the effective date of the later of the final SEF or DCM rules.⁸ If, however, any of these markets applies to become a DCM or SEF prior to the effective date of the final rules, the relief will last through the pendency of its application.

D. Tentative Schedule of Future Commission Rulemaking

Commissioner O'Malia has included, in Appendix 2 of the Proposed Amendment, a tentative schedule of future Commission rulemaking that reflects his understanding of the "earliest potential date for consideration" of anticipated rulemakings.

¹ "Effective Date for Swap Regulation," 76 *Fed. Reg.* 42508 (July 19, 2011).

² The exemption regarding the further definition of terms was to expire at the earlier of December 31, 2011 or the effective date of the entity and instrument definition rules.

³ The exemption from the effective date was to expire at the earlier of the repeal or December 31, 2011, and was available regardless of whether the instrument: (a) was executed on a multilateral transaction execution facility; (b) was cleared; (c) was not offered or entered into by eligible swap participants (ESPs) (though all parties had to be ECPs, as defined prior to the DFA); (d) was part of a fungible class of agreements standardized as to their material economic terms; and/or (e) for which no more than one party was entering into the instrument in conjunction with its line of business, but was not an ECP or ESP, and the instrument was not marketed to the public. The exemption required, however, that the instrument fall within the scope of certain pre-DFA CEA sections (Sections 2(d), 2(e), 2(g), 2(h), 5d or line of business).

⁴ "Amendment to the July 14, 2011 Order for Swap Regulation," 76 *Fed. Reg.* 80233 (December 23, 2011).

⁵ "Orders Regarding the Treatment of Petitions Seeking Grandfather Relief for Exempt Commercial Markets and Exempt Boards of Trade," 75 *Fed. Reg.* 56513 (September 16, 2010) (ECM/EBOT Grandfather Order).

⁶ See WilmerHale's alert regarding the final entity definition rules, available at www.wilmerhale.com/publications/whPubsDetail.aspx?publication=10138.

⁷ The guidance also confirms that entities cannot enter into or execute agricultural swaps on ECM or EBOTs, because these platforms are not self-regulated.

⁸ Since the DCM rules were also finalized on May 10, 2012, that would mean that the alternative expiry date would be the effective date of the SEF final rules, which could be considered as early as July 2012.

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