

Staff Overview of the Proposed Rulemaking Further Defining “Swap Dealer”



May 19, 2011

Status of Rulemaking

- The Commission (jointly with the SEC) approved a Notice of Proposed Rulemaking Further Defining “Swap Dealer” (along with MSP and ECP) in December 2010.
- The initial comment period closed February 22, 2011. The comment period has been extended to June 3, 2011.
- We have met with numerous market participants and received nearly 200 comments.



Definition of “Swap Dealer”

The proposed rules closely follow the text of the Dodd-Frank Act in defining the term “swap dealer” as any person who:

- holds itself out as a dealer in swaps,
- makes a market in swaps,
- regularly enters into swaps with counterparties as an ordinary course of business for its own account, or
- engages in activity causing itself to be commonly known in the trade as a dealer or market maker in swaps.



Distinguishing Characteristics of Swap Dealers

The Commission's rule proposal states that swap dealers:

- tend to accommodate demand for swaps from other parties;
- are generally available to enter into swaps to facilitate other parties' interest in entering into swaps;
- tend not to request that other parties propose the terms of swaps; rather, they tend to enter into swaps on their own standard terms or on terms they arrange in response to other parties' interest; and
- tend to be able to arrange customized terms for swaps upon request, or to create new types of swaps at their own initiative.



De Minimis Exemption from the Definition of Swap Dealer

The Dodd-Frank Act provides an exemption for a person who “engages in a de minimis quantity of swap dealing in connection with transactions with or on behalf of its customers.”

The proposed rule exempts a person that meets all of the following conditions over the prior 12 months:

- Aggregate effective notional amount, measured on a gross basis, of swaps that the person enters into in connection with dealing activities must not exceed \$100 million.
- Aggregate effective notional amount of such swaps with “special entities” must not exceed \$25 million.
- Swaps as a dealer with no more than 15 counterparties, other than security based swap dealers.
- No more than 20 swaps as a dealer.



Exclusion for Swaps in Connection with Originating a Loan

- The Dodd-Frank Act provides an exclusion for an insured depository institution “to the extent it offers to enter into a swap with a customer in connection with originating a loan with that customer.”
- The exclusion in the proposed rule would apply only to swaps that are connected to the financial terms of the loan itself.



Identification of Swap Dealers by Functional Role

- The Commission's rule proposal states that swap dealers may be identified by the functional role they fulfill in the swap markets.
- Swap dealers tend to accommodate demand and to be available to enter into swaps to facilitate other parties' interest in swaps.
- The rule proposal also states that persons that fulfill the function of swap dealers exist in most parts of the swap markets.



Proposed Indicators of Being Commonly Known in the Trade as a Swap Dealer

The Commission's rule proposal states that indicators that a person is holding itself out as a swap dealer or is commonly known in the trade as a swap dealer include:

- contacting potential counterparties to solicit interest in swaps,
- developing new types of swaps and informing potential counterparties of their availability,
- membership in a swap association in a category reserved for dealers,
- providing marketing materials (such as a web site) that describe the types of swaps one is willing to enter into with other parties, and
- generally expressing a willingness to offer or provide a range of financial products that would include swaps.



Process of Designation as a Swap Dealer

- The proposed rule provides that a person that meets the definition must register as a swap dealer.
- The proposed rule is intended to allow each market participant to assess its activities to determine whether it functions as a swap dealer.
- The proposed rule also permits persons to make an application to be designated as a swap dealer with respect to only specified categories of swaps or activities without being considered a swap dealer for other categories of swaps or activities.



Interaction with Agricultural Swaps

- The Commission's rule proposal states that it may consider particular terms and conditions for the interpretation of the swap dealer definition when applied to dealing in swaps in agricultural commodities.
- The Commission requested and has received comments on the application of the swap dealer definition to dealers, including potentially agricultural cooperatives, that limit their dealing activity primarily to swaps in agricultural commodities.

