

**COMMODITY FUTURES TRADING COMMISSION****17 CFR Parts 23, 37, 38, and 39****RIN: 3038-AC98****REQUIREMENTS FOR PROCESSING, CLEARING, AND TRANSFER OF  
CUSTOMER POSITIONS****AGENCY:** Commodity Futures Trading Commission.**ACTION:** Notice of proposed rulemaking.

**SUMMARY:** The Commodity Futures Trading Commission (Commission) is proposing regulations to implement Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). Proposed regulations would establish the time frame for a swap dealer (SD), major swap participant (MSP), futures commission merchant (FCM), swap execution facility (SEF), and designated contract market (DCM) to submit contracts, agreements, or transactions to a derivatives clearing organization (DCO) for clearing. Proposed regulations also would facilitate compliance with DCO Core Principle C (Participant and Product Eligibility) in connection with standards for cleared products and the prompt and efficient processing of all contracts, agreements, and transactions submitted for clearing. The Commission is further proposing related regulations implementing SEF Core Principle 7 (Financial Integrity of Transactions) and DCM Core Principle 11 (Financial Integrity of Transactions), requiring coordination with DCOs in the development of rules and procedures to facilitate clearing. Additionally, the Commission is proposing a regulation to implement DCO Core Principle F (Treatment of Funds), requiring a DCO, upon customer request, to promptly transfer customer positions and related funds from one clearing member to another, without requiring the close-out and re-booking of the positions.

**DATES:** Submit comments on or before [INSERT DATE 30 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER].

**ADDRESSES:** You may submit comments, identified by RIN number 3038-AC98, by any of the following methods:

- Agency website, via its Comments Online process: <http://comments.cftc.gov>. Follow the instructions for submitting comments through the website.
- Mail: David A. Stawick, Secretary of the Commission, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW, Washington, DC 20581.
- Hand Delivery/Courier: Same as mail above.
- Federal eRulemaking Portal: <http://www.Regulations.gov>. Follow the instructions for submitting comments.

Please submit comments by only one method.

All comments must be submitted in English, or if not, accompanied by an English translation. Comments will be posted as received to <http://www.cftc.gov>. You should submit only information that you wish to make available publicly. If you wish the Commission to consider information that may be exempt from disclosure under the Freedom of Information Act (FOIA), a petition for confidential treatment of the exempt information may be submitted according to the procedures established in § 145.9 of the Commission's regulations.<sup>1</sup> The Commission reserves the right, but shall have no obligation, to review, pre-screen, filter, redact, refuse, or remove any or all of your submission from <http://www.cftc.gov> that it may deem to be inappropriate for publication, such as obscene language. All submissions that have been redacted or removed that contain comments on the merits of the rulemaking will be retained in

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<sup>1</sup> Commission regulations referred to herein are found at 17 CFR Ch. 1 (2010). They are accessible on the Commission's website at <http://www.cftc.gov>.

the public comment file and will be considered as required under the Administrative Procedure Act and other applicable laws, and may be accessible under FOIA.

**FOR FURTHER INFORMATION CONTACT:** John C. Lawton, Deputy Director, 202-418-5480, [jlawton@cftc.gov](mailto:jlawton@cftc.gov); Phyllis P. Dietz, Associate Director, 202-418-5449, [pdietz@cftc.gov](mailto:pdietz@cftc.gov); Sarah E. Josephson, Associate Director, 202-418-5684, [sjosephson@cftc.gov](mailto:sjosephson@cftc.gov), Division of Clearing and Intermediary Oversight; Riva Spear Adriance, Associate Director, 202-418-5494, [radriance@cftc.gov](mailto:radriance@cftc.gov); Nancy Markowitz, Assistant Deputy Director, 202-418-5453, [nmarkowitz@cftc.gov](mailto:nmarkowitz@cftc.gov); Nadia Zakir, Attorney-Advisor, 202-418-5720, [nzakir@cftc.gov](mailto:nzakir@cftc.gov); Mauricio Melara, Attorney-Advisor, 202-418-5719, [mmelara@cftc.gov](mailto:mmelara@cftc.gov); Division of Market Oversight, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21<sup>st</sup> Street, NW, Washington, DC 20581.

## **SUPPLEMENTARY INFORMATION:**

### **I. Background.**

#### **A. Title VII of the Dodd-Frank Act.**

On July 21, 2010, President Obama signed the Dodd-Frank Act.<sup>2</sup> Title VII of the Dodd-Frank Act<sup>3</sup> amended the Commodity Exchange Act (CEA)<sup>4</sup> to establish a comprehensive regulatory framework to reduce risk, increase transparency, and promote market integrity within the financial system by, among other things: (1) providing for the registration and comprehensive regulation of SDs and MSPs; (2) imposing clearing and trade execution requirements on standardized derivative products; (3) creating rigorous recordkeeping and real-time reporting

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<sup>2</sup> See Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 124 Stat. 1376 (2010). The text of the Dodd-Frank Act may be accessed at <http://www.cftc.gov/LawRegulation/OTCDERIVATIVES/index.htm>.

<sup>3</sup> Pursuant to section 701 of the Dodd-Frank Act, Title VII may be cited as the “Wall Street Transparency and Accountability Act of 2010.”

<sup>4</sup> 7 U.S.C. 1 et seq.

regimes; and (4) enhancing the Commission's rulemaking and enforcement authorities with respect to all registered entities and intermediaries subject to the Commission's oversight.

In this notice of proposed rulemaking, the Commission proposes to adopt regulations to establish the time frame for an SD, MSP, FCM, SEF, or DCM to process and submit contracts, agreements, or transactions to a DCO for clearing; to establish certain product standards and a time frame for a DCO to clear such contracts, agreements, and transactions; and to facilitate a DCO's transfer of open positions from a carrying clearing member to another clearing member without unwinding and re-booking the position. These supplement proposed regulations that were previously published for public comment.<sup>5</sup>

#### B. Existing Swap Clearing Practices.

##### 1. Time frame for clearing.

Currently, a significant number of swaps are not cleared and, for those that are cleared, there may be a delay in the substitution of a DCO as the counterparty to the transaction through a novation of the original contract, agreement, or transaction.<sup>6</sup> In many instances, this delay can be up to a week. For example, some clearinghouses accept bilateral trades for clearing on a batched basis once a week. This time lag potentially presents credit risk to the swap counterparties and the DCO because the value of a position may change significantly between the time of execution and the time of novation, thereby allowing financial exposure to accumulate in the absence of daily mark-to-market. Among the purposes of clearing are the

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<sup>5</sup> See 76 FR 6715, Feb. 8, 2011 (proposed rules for SD and MSP documentation); 76 FR 3698, Jan. 20, 2011, (proposed rules for DCO Core Principles C and F); 76 FR 1214, Jan. 7, 2011 (proposed rules for SEF Core Principle 7; 75 FR 81519, Dec. 28, 2010, (proposed rules for SD and MSP confirmation, portfolio reconciliation, and portfolio compression); 75 FR 80572, Dec. 22, 2010 (proposed rules for DCM Core Principle 11).

<sup>6</sup> A clearinghouse becomes the counterparty to trades with market participants through novation, an open offer system, or an analogous legally binding arrangement. Through novation, the original contract between the buyer and seller is extinguished and replaced by two new contracts, one between the clearinghouse and the buyer and the other between the clearinghouse and the seller. In an open offer system, a clearinghouse is automatically and immediately interposed in a transaction at the moment the buyer and seller agree on the terms.

reduction of risk and the enhancement of financial certainty, and this delay diminishes these benefits of clearing swaps that Congress sought to promote in the Dodd-Frank Act. Delay in clearing is also inconsistent with other proposed regulations concerning product eligibility and financial integrity of transactions insofar as the delay constrains liquidity and increases risk.

The Commission recognizes that there may be instances when a delay in acceptance of a transaction by a DCO is unavoidable. For instance, when new products are first listed for clearing, existing legacy transactions may have to be moved into clearing incrementally. However, this process, sometimes referred to as backloading or migration, should be accomplished as quickly as possible.

The swap market infrastructure established by the Dodd-Frank Act provides for the trading of swaps on a SEF or DCM. The Dodd-Frank Act also establishes certain parameters for the bilateral execution of swaps among entities registered as SDs or MSPs and their counterparties. Swaps traded on a SEF or DCM, as well as swaps executed bilaterally, that are subject to mandatory clearing (and have not been electively excepted from mandatory clearing by an end user under section 2(h)(7) of the CEA), must be cleared by a registered DCO. For swaps executed bilaterally that are not required to be cleared, if the parties to the transaction agree to clear, they may submit the swap to a registered DCO for clearing.

Through this proposed rulemaking, the Commission seeks to expand access to, and to strengthen the financial integrity of, the swap markets subject to Commission oversight by requiring, and establishing uniform standards for, prompt processing, submission, and acceptance of swaps eligible for clearing by DCOs. This requires setting an appropriate time frame for the processing and submission of swaps for clearing, as well as a time frame for the clearing of swaps by the DCO.

## 2. Transfer of swaps positions and related funds.

Currently, in the futures industry, a request by a customer to transfer its open positions and related funds from its carrying FCM to another FCM is accomplished within a reasonable period of time (typically within two business days). However, under current practice for some cleared swaps, a customer's request to transfer all or a portion of its swap positions and related funds may be subject to a more significant delay. (A party to a cleared swap may wish to transfer its positions from its current clearing member to another clearing member because there is concern about the carrying clearing member's financial strength or for competitive reasons relating to customer service or pricing). In these instances, a party must either enter into an offsetting position without terminating its original position, thereby creating economically unnecessary trades, or "unwind" the position with the clearinghouse.

In proposing a new regulation to implement DCO Core Principle F (Treatment of Funds), the Commission seeks to ensure that DCOs do not impose economic or operational obstacles to the prompt transfer of customer positions and related funds from one clearing member to another, upon the request of a customer. The Commission's purpose in this regard is to formalize and apply to swaps clearing, the futures clearinghouse practice of transferring customer positions and related funds without close-out and re-booking of the positions.

## **II. Proposed regulations.**

### A. Proposed § 23.506 – SD and MSP Submission of Swaps for Processing and Clearing.

#### 1. Proposed regulations.

Section 731 of the Dodd-Frank Act amends the CEA by adding a new section 4s, which sets forth a number of requirements for SDs and MSPs. Specifically, section 4s(i) of the CEA establishes swap documentation standards for SDs and MSPs and requires them to "conform

with such standards as may be prescribed by the Commission by rule or regulation that relate to timely and accurate confirmation, processing, netting, documentation, and valuation of all swaps.” Accordingly, the Commission is proposing regulations on swap processing and clearing discussed below, pursuant to the authority granted under sections 4s(h)(1)(D), 4s(h)(3)(D), 4s(i), and 8a(5) of the CEA.<sup>7</sup> These proposed regulations for SDs and MSPs are intended to complement the proposed regulations for DCOs, which require timely acceptance of swaps for clearing.<sup>8</sup>

In order to ensure compliance with any mandatory clearing requirement issued pursuant to section 2(h)(1) of the CEA and to promote the mitigation of counterparty credit risk through the use of central clearing, the Commission is proposing § 23.506(a)(1), which would require that SDs and MSPs have the ability to route swaps that are not executed on a SEF or DCM to a DCO in a manner that is acceptable to the DCO for the purposes of risk management. Under § 23.506(a)(2), SDs and MSPs would also be required to coordinate with DCOs to facilitate prompt and efficient processing in accordance with proposed regulations related to the timing of clearing by DCOs.

Proposed § 23.506(a) does not prescribe the manner by which SDs or MSPs route their swaps to DCOs and provide for prompt and efficient processing. Indeed, in many instances, it is likely that DCOs will enable SDs and MSPs to submit their swaps to clearing via third-party platforms and other service providers. In this manner, privately negotiated swaps may be submitted to DCOs with minimal burden on market participants.

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<sup>7</sup> 7 U.S.C. 6s(h)(1)(D); 7 U.S.C. 6s(h)(3)(D); 7 U.S.C. 6s(i); and 7 U.S.C. 12a(5). Section 8a(5) of the CEA authorizes the Commission to promulgate such regulations as, in the judgment of the Commission, are reasonably necessary to effectuate any of the provisions or to accomplish any of the purposes of the CEA.

<sup>8</sup> See discussion in section II.B. of this notice.

Proposed § 23.506(b) would set forth timing requirements for submitting swaps to DCOs in those instances where the swap is subject to a clearing mandate and in those instances when a swap is not subject to a mandate. Under § 23.506(b)(1), an SD or MSP would be required to submit a swap that is not executed on a SEF or DCM, but is subject to a clearing mandate under section 2(h)(1) of the CEA (and has not been electively excepted from mandatory clearing by an end user under section 2(h)(7) of the CEA) as soon as technologically practicable following execution of the swap, but no later than the close of business on the day of execution.

For those swaps that are not subject to a clearing mandate, but both counterparties to the swap have elected to clear the swap, under proposed § 23.506(b)(2), the SD or MSP would be required to submit the swap for clearing not later than the next business day after execution of the swap or the agreement to clear, if later than execution. This time frame reflects the possibility that, unlike a trade that takes place on a DCM, in the case of a bilateral swap, the parties may need time to agree to terms that would conform with a DCO's template for swaps it will accept for clearing. As noted previously, any delay between execution and novation to a clearinghouse potentially presents credit risk to the swap counterparties and the DCO because the value of the position could change significantly between the time of execution and the time of novation, thereby allowing financial exposure to accumulate in the absence of daily mark-to-market. The proposed regulation would serve to limit this delay as much as reasonably possible.

Proposed § 23.506 is consistent with regulations previously proposed for SDs and MSPs, including proposed § 23.501, which requires confirmation of all swaps.<sup>9</sup> In fact, by providing for confirmation upon acceptance for clearing pursuant to proposed § 39.12(b)(7)(v), SDs and MSPs would be able to satisfy proposed § 23.501.

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<sup>9</sup> See 76 FR at 81531.

Proposed § 23.506 is consistent with the Commission’s proposed regulations requiring reporting of swap transaction data to a registered swap data repository.<sup>10</sup> Under these proposed regulations, SDs and MSPs are required to report certain information about a swap that is not executed on a SEF or DCM to a registered swap data repository “promptly following verification of the primary economic terms by the counterparties with each other at or immediately following execution of the swap, but in no event later than: 30 minutes after execution of the swap if verification of primary economic terms occurs electronically; or 24 hours after execution of a swap if verification of primary economic terms does not occur electronically.”<sup>11</sup> One of the “primary economic terms” required to be reported under such proposed regulations is an indication of whether or not the swap will be cleared by a DCO.<sup>12</sup>

The proposed regulation also is consistent with the Commission’s proposed regulations requiring real-time public reporting of swap transaction and pricing data.<sup>13</sup> Under these proposed regulations, SDs and MSPs are required to report certain information about a swap that is not executed on a SEF or DCM to a registered swap data repository that accepts and publicly disseminates swap transaction and pricing data, as soon as technologically practicable following execution of such swap.<sup>14</sup> The information required to be reported under the proposed regulations includes an indication of whether or not a swap is cleared by a DCO.<sup>15</sup>

## 2. Solicitation of comments.

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<sup>10</sup> See 75 FR 76574, Dec. 8, 2010 (proposed rules for swap data recordkeeping and reporting requirements).

<sup>11</sup> Proposed § 45.3(a)(1)(iii)(A), 75 FR at 76600.

<sup>12</sup> Proposed § 45.1(q)(20), 75 FR at 76598.

<sup>13</sup> See 75 FR 76140, Dec. 7, 2010 (proposed rules for real-time public reporting of swap transaction data).

<sup>14</sup> Proposed § 43.3(a)(3), 75 FR at 76172.

<sup>15</sup> Proposed § 43.4 and Appendix A to part 43, 75 FR at 76174 and 76177.

The Commission solicits comment on all aspects of the proposed § 23.506. It further requests responses to the following specific questions: Should the regulations specify how an SD or MSP must ensure that it has the capacity to route swaps to a DCO? Are there any systemic obstacles to the DCO, SD, and MSP coordination required under the proposed regulation?

Are the proposed time frames in § 23.506(b) appropriate? Are they operationally feasible? What is the operational feasibility of same-day clearing for swaps executed bilaterally that are required to be cleared and those that will not be required to be cleared? The Commission further requests comment on the use of the phrase “as soon as technologically practicable.”

B. Proposed § 39.12 – Acceptance and Clearing of Swaps by a DCO.

1. Recently proposed product eligibility standards under Core Principle C.

Core Principle C requires each DCO to establish “appropriate standards for determining the eligibility of agreements, contracts, or transactions submitted to the [DCO] for clearing.”<sup>16</sup> The Commission has previously proposed § 39.12(b) to implement this provision,<sup>17</sup> pursuant to its rulemaking authority under sections 5b(c)(2)(A) and 8a(5) of the CEA.<sup>18</sup>

As previously published for public notice and comment, proposed § 39.12(b)(1) would require a DCO to establish appropriate requirements for determining the eligibility of agreements, contracts, or transactions submitted to the DCO for clearing, taking into account the DCO’s ability to manage the risks associated with such agreements, contracts, or transactions.<sup>19</sup> Proposed § 39.12(b)(2) would codify the requirements of section 2(h)(1)(B) of the CEA

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<sup>16</sup> Section 5b(c)(2)(C)(i)(II) of the CEA; 7 U.S.C. 7a-1(c)(2)(C)(i)(II).

<sup>17</sup> See 76 FR 3698.

<sup>18</sup> 7 U.S.C. 7a-1(c)(2)(A); and 7.U.S.C. 12a(5).

<sup>19</sup> See 76 FR at 3720.

regarding a DCO's offset of economically equivalent swaps.<sup>20</sup> Proposed § 39.12(b)(3) would require a DCO to select contract unit sizes that maximize liquidity, open access, and risk management.<sup>21</sup> Finally, proposed § 39.12(b)(4) would require each DCO that clears swaps to have rules stating that upon acceptance of a swap by the DCO for clearing, (i) the original swap is extinguished, (ii) it is replaced by equal and opposite swaps between clearing members and the DCO, (iii) all terms of the cleared swaps must conform to templates established under DCO rules, and (iv) if a swap is cleared by a clearing member on behalf of a customer, all terms of the swap, as carried in the customer account on the books of the clearing member, must conform to the terms of the cleared swap established under the DCO's rules.<sup>22</sup>

## 2. Re-proposed and newly proposed regulations.

To refine and supplement the previously proposed regulations implementing Core Principle C, the Commission is (1) re-proposing § 39.12(b)(2) to clarify the role of a DCO in establishing the terms and conditions for swaps that it accepts for clearing;<sup>23</sup> (2) proposing a new § 39.12(b)(4) that would prohibit a DCO from refusing to clear a product where neither party to the original contract, agreement, or transaction is a clearing member; (3) re-proposing § 39.12(b)(3) (renumbered as § 39.12(b)(5)) to clarify a DCO's role and objectives in selecting contract units for clearing purposes that are smaller than the contract units in which trades submitted for clearing were executed; and (4) proposing a new § 39.12(b)(7) that would clarify

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<sup>20</sup> *Id.* Section 2(h)(1)(B) of the CEA, 7 U.S.C. 2(h)(1)(B), requires a DCO to adopt rules providing that all swaps with the same terms and conditions submitted to the DCO for clearing are economically equivalent within the DCO and may be offset with each other within the DCO. Section 2(h)(1)(B) further requires a DCO to provide for non-discriminatory clearing of a swap executed bilaterally or on or subject to the rules of an unaffiliated SEF or DCM.

<sup>21</sup> *See* 76 FR at 3720.

<sup>22</sup> *Id.*

<sup>23</sup> To provide additional clarity regarding open access to clearing, the Commission is proposing to renumber the second sentence of proposed § 39.12(b)(2) as § 39.12(b)(3) and to insert a new paragraph (b)(4). Accordingly, proposed paragraphs (b)(3) and (b)(4) would be renumbered as paragraphs (b)(5) and (b)(6), respectively.

the timing of the actions described in previously proposed §§ 39.12(b)(4)(i) and (ii) (renumbered as paragraph (b)(6)), i.e., requirements that upon acceptance of a swap by the DCO for clearing, (i) the original swap is extinguished and (ii) it is replaced by equal and opposite swaps between clearing members and the DCO.

(a) Section 39.12(b)(2).

As previously proposed, § 39.12(b)(2) required a DCO to “adopt rules providing that all swaps with the same terms and conditions submitted to the derivatives clearing organization for clearing are economically equivalent within the derivatives clearing organization and may be offset with each other within the derivatives clearing organization.”<sup>24</sup> It also required that a DCO provide for non-discriminatory clearing of a swap executed bilaterally or on or subject to the rules of an unaffiliated SEF or DCM.<sup>25</sup>

The Commission is proposing to revise the first provision of § 39.12(b)(2) to clarify that a DCO must adopt rules to establish templates for the terms and conditions of swaps that it will clear. Accordingly, the proposed provision now reads: “A derivatives clearing organization shall adopt rules providing that all swaps with the same terms and conditions, as defined by templates established under derivatives clearing organization rules, submitted to the derivatives clearing organization for clearing are economically equivalent within the derivatives clearing organization and may be offset with each other within the derivatives clearing organization.”

As noted above, the second provision of previously proposed § 39.12(b)(2) would be unchanged, and would be renumbered as § 39.12(b)(3).

(b) Section 39.12(b)(4).

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<sup>24</sup> See 76 FR at 3720.

<sup>25</sup> Id.

Some clearinghouses have indicated that they intend to require that, for a transaction to be eligible for clearing, one of the executing parties must be a clearing member. This has the effect of preventing trades between two parties who are not clearing members from being cleared. Such a restriction of open access serves no apparent risk management purpose and operates to keep certain trades out of the clearing process and to constrain liquidity for cleared trades. Moreover, such restrictions also may raise competitive issues under Core Principle N (Antitrust Considerations).<sup>26</sup>

Accordingly, the Commission is proposing new § 39.12(b)(4) to prohibit a DCO from refusing to clear a product where neither party to the original contract, agreement, or transaction is a clearing member. The Commission notes that parties that are not clearing members would still have to submit their bilateral trades for clearing through a clearing member of the DCO.

(c) Section 39.12(b)(5).

The Commission previously proposed § 39.12(b)(3), now proposed to be renumbered at § 39.12(b)(5), which would require a DCO to “select contract unit sizes that maximize liquidity, open access, and risk management.”<sup>27</sup> To the extent appropriate to further these objectives, a DCO would be further required to select contract units for clearing purposes that are smaller than the contract units in which trades submitted for clearing were executed.<sup>28</sup> The purpose of this provision is to require the DCO to split a cleared swap into smaller units in order to promote liquidity by permitting more parties to trade the product, to facilitate open access by permitting

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<sup>26</sup> See Section 5b(c)(2)(N) of the CEA, which provides that “Unless necessary or appropriate to achieve the purposes of this Act, a derivatives clearing organization shall not—

- (i) adopt any rule or take any action that results in any unreasonable restraint of trade; or
- (ii) impose any material anticompetitive burden.”

<sup>27</sup> See 76 FR at 3720.

<sup>28</sup> *Id.*

more clearing members to clear the product, and to aid risk management by enabling a DCO, in the event of a default, to have more potential counterparties to take on positions during a liquidation.

The Commission is now proposing to expand its description of the actions to be undertaken by the DCO and the objectives to be served. Accordingly, the Commission proposes that the introductory sentence of § 39.12(b)(5) read as follows: “A derivatives clearing organization shall select contract unit sizes and other terms and conditions that maximize liquidity, facilitate transparency in pricing, promote open access, and allow for effective risk management.” This would clarify that, in establishing product templates under its rules, the DCO is required to select other terms and conditions in addition to unit size, such as termination or maturity period, settlement features, and cash flow conventions, to facilitate price transparency in addition to liquidity, open access, and risk management.

(d) Section 39.12(b)(7).

Proposed § 39.12(b)(7)(i) would establish general standards for the adoption of rules that establish a time frame for clearing. The DCO would have to coordinate with each SEF and DCM that lists for trading a product that is cleared by the DCO, in developing rules and procedures to facilitate prompt and efficient processing of all contracts, agreements, and transactions submitted to the DCO for clearing.

For prompt and efficient clearing to occur, the rules, procedures, and operational systems of the trading platform and the clearinghouse must mesh. Vertically integrated trading and clearing systems currently process high volumes of transactions quickly and efficiently. The Commission believes that trading platforms and DCOs under separate control should be able to coordinate with one another to achieve similar results. The Commission also recognizes that

there may be issues of connectivity between and among trading platforms and clearinghouses. The Commission requests comment on how best to facilitate the development of infrastructure, systems, and procedures to address these issues.

Proposed paragraph (ii) would require a DCO to have rules that provide that the DCO will accept for clearing, immediately upon execution, all contracts, agreements, and transactions that are listed for clearing by the DCO and (A) that are entered into on or subject to the rules of a SEF or DCM; (B) for which the executing parties have clearing arrangements in place with clearing members of the DCO; and (C) for which the executing parties identify the DCO as the intended clearinghouse.

Rules, procedures, and operational systems along these lines currently work well for many exchange-traded futures. Similar requirements could be applied across multiple exchanges and clearinghouses for swaps. The parties would need to have clearing arrangements in place with clearing members in advance of execution. In cases where more than one DCO offered clearing services, the parties also would need to specify in advance where the trade should be sent for clearing.

Proposed paragraph (iii), which governs swaps subject to mandatory clearing, would require a DCO to have rules that provide that the DCO will accept for clearing, upon submission, all contracts, agreements, and transactions that are listed for clearing by the DCO and (A) that are not executed on or subject to the rules of a SEF or DCM; (B) that are subject to mandatory clearing pursuant to section 2(h) of the CEA; (C) that are submitted by the parties to the DCO, in accordance with § 23.506 of the Commission's regulations; (D) for which the executing parties have clearing arrangements in place with clearing members of the DCO; and (E) for which the executing parties identify the DCO as the intended clearinghouse.

Proposed paragraph (iv) would provide for a longer time frame for clearing swaps not executed on or subject to the rules of a SEF or DCM and not subject to mandatory clearing. It would require a DCO to have rules that provide that the DCO will process for clearing, no later than the close of business on the day of submission to the DCO, all swaps that are listed for clearing by the DCO and (A) that are not executed on a SEF or a DCM; (B) that are not subject to mandatory clearing pursuant to section 2(h) of the CEA; (C) that are submitted by the parties to the DCO in accordance with proposed § 23.506; (D) for which the executing parties have clearing arrangements in place with clearing members of the DCO; and (E) for which the executing parties identify the DCO as the intended clearinghouse.

Because the execution of bilateral trades might not be automated and because the parties to a trade might not decide that they want to clear the trade until some time after execution, immediate clearing might not be feasible. However, a DCO should provide sufficient clarity about its participant and product eligibility requirements to enable swap counterparties to determine whether a bilateral trade would be acceptable to be cleared within one day of submission.

Proposed § 39.12(b)(7)(v) would require that DCOs accepting a swap for clearing provide the counterparties with a definitive written record of the terms of their agreement, which will serve as a confirmation of the swap. This requirement would facilitate the timely processing and confirmation of swaps not executed on a SEF or DCM by allowing parties to confirm their transaction by submitting it to a DCO for clearing. Swaps executed on a SEF or DCM are confirmed upon execution.<sup>29</sup> In other regulations proposed by the Commission, a swap confirmation is defined as the consummation (electronically or otherwise) of legally binding

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<sup>29</sup> See 76 FR at 1240.

documentation (electronic or otherwise) that memorializes the agreement of the counterparties to all of the terms of a swap.<sup>30</sup> By providing for confirmation upon acceptance for clearing, SDs and MSPs would be able to satisfy proposed § 23.501, which requires timely confirmation of all swaps.

(e) Proposed §§ 37.702 and 38.601 – reciprocal requirements for SEFs and DCMs.

In connection with proposing that a DCO coordinate the development of rules and procedures with each SEF and DCM that lists for trading a product that is cleared by the DCO, the Commission is re-proposing certain amendments to parts 37 and 38 of the Commission’s regulations to include reciprocal coordination obligations for SEFs and DCMs.

The Commission previously proposed §§ 37.700 to 703 to implement SEF Core Principle 7 (Financial Integrity of Transactions), pursuant to its rulemaking authority under sections 5h(h) and 8a(5) of the CEA.<sup>31</sup> Core Principle 7 requires a SEF to “establish and enforce rules and procedures for ensuring the financial integrity of swaps entered on or through the facilities of the swap execution facility, including the clearing and settlement of the swaps pursuant to section 2(h)(1) [of the CEA].”<sup>32</sup> As previously proposed, § 37.702(b) would require a SEF to provide for the financial integrity of its transactions cleared by a DCO by ensuring that the SEF has the capacity to route transactions to the DCO in a manner acceptable to the DCO for purposes of risk management.<sup>33</sup> In this notice, the Commission proposes to renumber previously proposed § 37.702(b) as paragraph (b)(1) and add a new paragraph (b)(2) to require the SEF to additionally

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<sup>30</sup> See 75 FR 76140; and 75 FR 76574.

<sup>31</sup> See 76 FR 1214; 7 U.S.C. 7b-3(h); and 7.U.S.C. 12a(5).

<sup>32</sup> Section 5h(f)(7) of the CEA, 7 U.S.C. 7b-3(f)(7).

<sup>33</sup> See 76 FR at 1248. Section 37.702(b), as originally proposed, referred to “ongoing” risk management. In renumbering and re-proposing this provision herein, the Commission is deleting the term “ongoing” because it is superfluous and could create confusion when read in conjunction with other Commission regulations that refer to “risk management.” See, e.g., proposed § 39.13 relating to risk management for DCOs, 76 FR at 3720.

provide for the financial integrity of cleared transactions by coordinating with each DCO to which it submits transactions for clearing, in the development of rules and procedures to facilitate prompt and efficient transaction processing in accordance with the requirements of § 39.12(b)(7) of the Commission's regulations.

Similarly, the Commission previously proposed §§ 38.600 to 607 to implement DCM Core Principle 11 (Financial Integrity of Transactions) pursuant to its rulemaking authority under sections 5(d)(1) and 8a(5) of the CEA.<sup>34</sup> Core Principle 11 requires a DCM to “establish and enforce –(A) rules and procedures for ensuring the financial integrity of transactions entered into on or through the facilities of the contract market (including the clearance and settlement of the transactions with a derivatives clearing organization); and (B) rules to ensure—(i) the financial integrity of any—(I) futures commission merchant; and (II) introducing broker; and (ii) the protection of customer funds.”<sup>35</sup> As previously proposed, § 38.601 would require that transactions executed on or through a DCM, other than transactions in security futures products, must be cleared through a registered DCO in accordance with the provisions of part 39 of the Commission's regulations.<sup>36</sup> In this notice, the Commission proposes to renumber this provision as paragraph (a) of proposed § 38.601 and add a new paragraph (b) to specifically require the DCM to coordinate with each DCO to which it submits transactions for clearing, in the development of DCO rules and procedures to facilitate prompt and efficient transaction processing in accordance with the requirements of § 39.12(b)(7) of the Commission's regulations.

### 3. Solicitation of comments.

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<sup>34</sup> See 75 FR 80572; 7 U.S.C. 7(d)(1); and 7 U.S.C. 12a(5).

<sup>35</sup> Section 5(d)(11) of the CEA, 7 U.S.C. 7(d)(11).

<sup>36</sup> See 75 FR at 80618.

The Commission solicits comment on all aspects of the proposed regulations. It further requests responses to the following specific questions: Are there any systemic or legal obstacles to the DCO, SEF, and DCM coordination required under the proposed regulation? Are the proposed time frames appropriate? Are they operationally feasible? More specifically, for futures traded on a DCM, rules and procedures are in place under which bunched orders are accepted for clearing immediately upon execution, with allocation to individual customer accounts occurring before the end of the day. Are similar procedures operationally feasible for swaps executed as block trades? What amount of time is necessary for asset managers to allocate block trades to the individual entities on whose behalf they manage money, prior to the allocated trades being sent to clearing (i.e. end of day, two hours, etc.)? Should the submission of block trades to a DCO be treated differently than other trades executed on or subject to the rules of a SEF or DCM? What is the operational feasibility of same-day clearing for bilateral swaps that are not required to be cleared?

C. Proposed § 39.15 – Transfer of Customer Positions and Related Funds.

1. Recently proposed treatment of funds standards under Core Principle F.

Core Principle F, as amended by the Dodd-Frank Act,<sup>37</sup> requires a DCO to:

(a) establish standards and procedures that are designed to protect and ensure the safety of its clearing members' funds and assets; (b) hold such funds and assets in a manner by which to minimize the risk of loss or of delay in the DCO's access to the assets and funds; and (c) only invest such funds and assets in instruments with minimal credit, market, and liquidity risks.<sup>38</sup>

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<sup>37</sup> Section 5b(c)(2)(F) of the CEA; 7 U.S.C. 7a-1(c)(2)(F) (Core Principle F).

<sup>38</sup> Prior to amendment by the Dodd-Frank Act, Core Principle F provided that "[t]he applicant shall have standards and procedures designed to protect and ensure the safety of member and participant funds."

The Commission has proposed § 39.15 to establish standards for compliance with Core Principle F.<sup>39</sup>

2. Newly-proposed regulations.

To supplement the previously proposed regulations implementing Core Principle F, the Commission is proposing a new § 39.15(d) to require a DCO to facilitate the prompt transfer of customer positions from one clearing member of the DCO to another clearing member of the DCO.<sup>40</sup>

Efficient and complete portability of customer positions and the funds related to those positions is important in both pre-default and post-default scenarios. A DCO should therefore structure its portability arrangements in a way that facilitates the prompt and efficient transfer of all or a portion of a customer's positions and funds from one clearing member to one or more other clearing members. A DCO's rules and procedures should require clearing members to facilitate the transfer of customer positions and funds upon the customer's request, subject to any notice or other contractual requirements.

Proposed § 39.15(d) would require a DCO to have rules providing that, upon the request of a customer and subject to the consent of the receiving clearing member, the DCO will promptly transfer all or a portion of such customer's portfolio of positions and related funds from the carrying clearing member of the DCO to another clearing member of the DCO, without requiring the close-out and re-booking of the positions prior to the requested transfer. The term "promptly," as used in this provision is intended to mean as soon as possible and within a reasonable period of time. Based on current futures industry standards, this time frame is

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<sup>39</sup> See 76 FR at 3723.

<sup>40</sup> In connection with the proposed addition of new paragraph (d), the Commission also proposes to renumber previously proposed paragraph (d) as paragraph (e).

typically no more than two business days. The requirement that a DCO not require close-out and re-booking of positions eliminates a source of unnecessary delay and market disruption, and conforms with current futures industry practice.<sup>41</sup> The Commission is unaware of any reason that the transfer of cleared swaps positions cannot be accomplished by means of the same process that has been used for futures positions.

### 3. Solicitation of comments.

The Commission requests comment on whether the use of the term “promptly” provides adequate guidance or whether another descriptive term or phrase, such as “within a reasonable period of time” or “as soon as practicable” would better convey the intended meaning. The Commission is not proposing that a specific time frame be included in § 39.15(d) because as technology evolves, it is likely that the transfer of customer positions and related funds can be accomplished more quickly and with greater operational efficiency. The Commission requests comment on the proposed time frame and possible alternative standards that could be applied.

As noted above, the Commission believes<sup>41</sup> that the transfer of cleared customer swap positions can be processed in the same manner as futures positions. The Commission requests comment on whether there are distinctions between futures and cleared swaps positions that would require a different type of processing such that the cleared swaps positions would have to be closed out and re-booked prior to transfer from the carrying clearing member to another clearing member.

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<sup>41</sup> See, e.g., National Futures Association Rule 2-27 “Transfer of Customer Accounts” (requiring that in response to a customer’s request to transfer its account, the carrying member must confirm the account balances and positions to the receiving member and then effect the requested transfer); and Chicago Mercantile Exchange Rule 853 “Transfer of Trades” (permitting existing trades to be transferred either on the books of a clearing member or from one clearing member to another clearing member provided 1. the transfer merely constitutes a change from one account to another account where the underlying beneficial ownership in the accounts remains the same; or 2. an error has been made in the clearing of a trade and the error is discovered and the transfer is completed within two business days after the trade date).

The proposed regulation places an obligation on the DCO to promptly transfer customer positions and related funds, and the Commission requests comment on whether the regulation also should require that a DCO adopt rules that would require its clearing members to facilitate prompt transfer of customer accounts.

### **III. Related Matters.**

#### **A. Regulatory Flexibility Act.**

##### **1. Swap dealers and major swap participants.**

The Regulatory Flexibility Act (RFA) requires that agencies consider whether the regulations they propose will have a significant economic impact on a substantial number of small entities.<sup>42</sup> The Commission previously has established certain definitions of “small entities” to be used in evaluating the impact of its regulations on small entities in accordance with the RFA.<sup>43</sup> The proposed regulations would affect SDs and MSPs.

SDs and MSPs are new categories of registrants. Accordingly, the Commission has not previously addressed the question of whether such persons are, in fact, small entities for purposes of the RFA. The Commission previously has determined, however, that futures commission merchants (FCMs) should not be considered to be small entities for purposes of the RFA.<sup>44</sup> The Commission’s determination was based, in part, upon the obligation of FCMs to meet the minimum financial requirements established by the Commission to enhance the protection of customers’ segregated funds and protect the financial condition of FCMs generally.<sup>45</sup> Like FCMs, SDs will be subject to minimum capital and margin requirements and are expected to

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<sup>42</sup> 5 U.S.C. 601 et seq.

<sup>43</sup> 47 FR 18618, Apr. 30, 1982.

<sup>44</sup> Id. at 18619.

<sup>45</sup> Id.

comprise the largest global financial firms. The Commission is required to exempt from SD registration any entities that engage in a de minimis level of swaps dealing in connection with transactions with or on behalf of customers. The Commission anticipates that this exemption would tend to exclude small entities from registration. Accordingly, for purposes of the RFA for this rulemaking, the Commission is hereby proposing that SDs not be considered “small entities” for essentially the same reasons that FCMs have previously been determined not to be small entities and in light of the exemption from the definition of SD for those engaging in a de minimis level of swap dealing.

The Commission also has previously determined that large traders are not “small entities” for RFA purposes.<sup>46</sup> In that determination, the Commission considered that a large trading position was indicative of the size of the business. MSPs, by statutory definition, maintain substantial positions in swaps or maintain outstanding swap positions that create substantial counterparty exposure that could have serious adverse effects on the financial stability of the United States banking system or financial markets. Accordingly, for purposes of the RFA for this rulemaking, the Commission is hereby proposing that MSPs not be considered “small entities” for essentially the same reasons that large traders have previously been determined not to be small entities.

Moreover, the Commission is carrying out Congressional mandates by proposing this regulation. Specifically, the Commission is proposing these regulations to comply with the Dodd-Frank Act, the aim of which is to reduce systemic risk presented by SDs and MSPs through comprehensive regulation. The Commission does not believe that there are regulatory alternatives to those being proposed that would be consistent with the statutory mandate.

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<sup>46</sup> Id. at 18620.

Accordingly, the Chairman, on behalf of the Commission, hereby certifies pursuant to 5 U.S.C. 605(b) that the proposed regulations will not have a significant economic impact on a substantial number of small entities.

The Commission invites the public to comment on whether SDs and MSPs should be considered small entities for purposes of the RFA.

## 2. Swap execution facilities.

As noted above, the RFA requires that agencies consider whether the regulations they propose will have a significant economic impact on a substantial number of small entities. The Commission previously has established certain definitions of “small entities” to be used in evaluating the impact of its regulations on small entities in accordance with the RFA.

The regulations adopted herein will affect SEFs. While SEFs are new entities to be regulated by the Commission pursuant to the Dodd-Frank Act, in a recent rulemaking proposal,<sup>47</sup> the Commission proposed that SEFs should not be considered as small entities for the purpose of the RFA. The Dodd-Frank Act defines a SEF to mean “a trading system or platform in which multiple participants have the ability to execute or trade swaps by accepting bids and offers made by multiple participants in the facility or system, through any means of interstate commerce, including any trading facility, that – (A) facilitates the execution of swaps between persons; and (B) is not a designated contract market.”<sup>48</sup>

In such rulemaking, the Commission proposed that SEFs not be considered to be “small entities” for essentially the same reasons that DCMs and DCOs have previously been determined not to be small entities. These reasons include the fact that the Commission designates a DCM

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<sup>47</sup> 75 FR 63745-46 (Oct. 18, 2010).

<sup>48</sup> See section 1a(50) of the CEA. In addition, the Commission proposed regulations regarding the types of entities that must register as SEFs. See 76 FR 1214. The Commission does not believe that such proposals would alter its determination that a SEF is not a “small entity” for purposes of the RFA.

or registers a DCO only when it meets specific criteria including the expenditure of sufficient resources to establish and maintain adequate self-regulatory programs. Likewise, the Commission will register an entity as a SEF only after it has met specific criteria including the expenditure of sufficient resources to establish and maintain an adequate self-regulatory program.<sup>49</sup> Once registered, a SEF will be required to comply with the additional requirements set forth in the final form of the proposed Part 37 rulemaking.<sup>50</sup> Under such rulemaking, the Commission proposed that SEFs should also not be considered small entities based on, among other things, the central role SEFs will play in the national regulatory scheme overseeing the trading of swaps.<sup>51</sup> Not only will SEFs play a vital role in the national economy, but they will be subject to Commission oversight with statutory duties to enforce the regulations adopted by their own governing bodies.

Accordingly, the Commission does not expect the regulations, as proposed herein, to have a significant economic impact on a substantial number of small entities. Therefore, the Chairman, on behalf of the Commission, hereby certifies, pursuant to 5 U.S.C. 605(b), that the proposed regulations will not have a significant economic impact on a substantial number of small entities.

The Commission invites the public to comment on whether SEFs should be considered small entities for purposes of the RFA.

### 3. Designated contract markets and derivatives clearing organizations.

The regulations proposed by the Commission will affect DCMs and DCOs (some of which will be designated as systemically important DCOs). As noted above, the Commission

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<sup>49</sup> See 76 FR 1214.

<sup>50</sup> *Id.*

<sup>51</sup> *Id.* at 1235.

has previously established certain definitions of “small entities” to be used by the Commission in evaluating the impact of its regulations on small entities in accordance with the RFA. The Commission has previously determined that DCMs and DCOs are not small entities for the purpose of the RFA.<sup>52</sup> Accordingly, the Chairman, on behalf of the Commission, hereby certifies pursuant to 5 U.S.C. 605(b) that the proposed regulations will not have a significant economic impact on a substantial number of small entities.

B. Paperwork Reduction Act.

The Paperwork Reduction Act (PRA)<sup>53</sup> imposes certain requirements on Federal agencies in connection with their conducting or sponsoring any collection of information as defined by the PRA. Under the PRA, an agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid control number from the Office of Management and Budget (OMB). The Commission believes that these proposed regulations will not impose any new information collection requirements that require approval of OMB under the PRA.

C. Cost-Benefit Analysis.

Section 15(a) of the CEA requires the Commission to consider the costs and benefits of its actions before issuing a rulemaking under the CEA. By its terms, Section 15(a) does not require the Commission to quantify the costs and benefits of a regulation or to determine whether the benefits of the rulemaking outweigh its costs; rather, it requires that the Commission “consider” the costs and benefits of its action.

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<sup>52</sup> See 47 FR 18618, 18621, Apr. 30, 1982 (DCM determination); 66 FR 45605, 45609, Aug. 29, 2001 (DCO determination).

<sup>53</sup> 44 U.S.C. 3501 et seq.

Section 15(a) further specifies that the costs and benefits shall be evaluated in light of five broad areas of market and public concern: (1) protection of market participants and the public; (2) efficiency, competitiveness, and financial integrity of futures markets; (3) price discovery; (4) sound risk management practices; and (5) other public interest considerations. The Commission may in its discretion give greater weight to any one of the five enumerated areas and could in its discretion determine that, notwithstanding its costs, a particular regulation is necessary or appropriate to protect the public interest or to effectuate any of the provisions or to accomplish any of the purposes of the CEA.

Summary of proposed requirements. The proposed regulations would establish the time frame for SDs, MSPs, FCMs, DCMs, and SEFs to submit contracts, agreements, or transactions to a DCO for clearing. The proposed regulations would implement new section 4s(i) of the CEA by establishing standards for SDs and MSPs related to the timely processing and clearing of swaps. The proposed regulations also would implement SEF Core Principle 7 (Financial Integrity of Transactions) and DCM Core Principle 11 (Financial Integrity of Transactions), requiring coordination with DCOs in the development of rules and procedures to facilitate clearing. Additionally, the proposed regulations would facilitate compliance with DCO Core Principle C (Participant and Product Eligibility) in connection with the prompt and efficient processing of all contracts, agreements, and transactions submitted for clearing. Finally, the proposed regulations would implement DCO Core Principle F (Treatment of Funds), requiring a DCO, upon customer request, to promptly transfer customer positions and related funds from one clearing member to another, without requiring the close-out and re-booking of the positions.

Costs. The Commission has determined that the costs borne by SDs, MSPs, FCMs, SEFs, DCMs, and DCOs to implement the new timing requirements for processing and clearing

positions and for transferring customer positions and related funds, may be limited and far outweighed by the accrual of benefits to the financial system as a result of the regulations' implementation. Indeed, as discussed in Section I.B.2., the timely transfer of futures positions and funds is currently practiced; thus, the additional costs of similar processes for swaps may not be too significant. Rather, timely transfers of positions and funds between clearing members would reduce economic and operational obstacles. Moreover, the Commission has determined that the costs of implementing new timing requirements for clearing would not be significantly burdensome to a DCO given that immediate processing and clearing of futures contracts is the current industry standard. Furthermore, the clearing delays in the swaps market (as discussed in Sections I.B.1, above) creates a credit risk because the value of position may change between execution and novation, thereby allowing financial exposure to accumulate in the absence of daily mark-to-market, and additionally can have negative effects on liquidity and the market's price discovery function.

Benefits. The Commission has determined that the benefits of the proposed regulations are considerable. Through this proposed rulemaking, market access will be expanded by requiring and establishing uniform standards for, prompt processing and clearing of swaps eligible for clearing by DCOs. Other benefits of timely clearing include the promotion of centralized trading and clearing; increased financial and legal certainty; and the timely notice of information so that parties and market participants can gauge risk exposure, liquidity, and market integrity. Timely clearing increases liquidity, enhances price discovery for traders, and reduces risk to markets by informing market participants of margin concerns and whether safeguards should be triggered. Significantly, the Commission notes that these regulations would aid market participants in fully complying with Dodd-Frank's overarching mandate to promote

clearing of swaps. The proposed new regulation regarding a DCO's timely transfer of swaps positions and related funds would benefit market participants by eliminating economic or operational obstacles to customer transfers between clearing members. In addition, the standardization of swaps clearing and procedures for customer account transfer will be more akin to valuable practices used in the futures market. The Commission believes it is prudent to employ similar practices in the swaps markets.

### **List of Subjects**

#### **17 CFR Part 23**

Antitrust, Commodity futures, Conduct standards, Conflicts of interests, Major swap participants, Reporting and recordkeeping, Swap dealers, Swaps.

#### **17 CFR Part 37**

Swaps, Swap execution facilities, Registration application, Registered entities, Reporting and recordkeeping requirements.

#### **17 CFR Part 38**

Block transaction, Commodity futures, Designated contract markets, Reporting and Recordkeeping requirements, Transactions off the centralized market.

#### **17 CFR Part 39**

Commodity futures, Participant and product eligibility, Risk management, Swaps.

In light of the foregoing, the Commission hereby proposes to amend parts 23, 37, 38, and 39 of Title 17 of the Code of Federal Regulations as follows:

### **PART 23 – SWAP DEALERS AND MAJOR SWAP PARTICIPANTS**

1. The authority citation for part 23 is revised to read as follows:

**AUTHORITY:** 7 U.S.C. 1a, 2, 6, 6a, 6b, 6b-1, 6c, 6p, 6r, 6s, 6t, 9, 9a, 12, 12a, 13b, 13c, 16a, 18, 19, 21.

2. Revise the table of contents for part 23, subpart I to read as follows:

**Subpart I – Swap Documentation**

Sec.

23.500 Definitions.

23.501 Swap confirmation.

23.502 Portfolio reconciliation.

23.503 Portfolio compression.

23.504 Swap trading relationship documentation.

23.505 End user exception documentation.

23.506 Swap processing and clearing.

3. Add § 23.506 to part 23, subpart I, to read as follows:

**§ 23.506 Swap processing and clearing.**

(a) Swap processing. (1) Each swap dealer and major swap participant shall ensure that it has the capacity to route swap transactions not executed on a swap execution facility or designated contract market to a derivatives clearing organization in a manner acceptable to the derivatives clearing organization for the purposes of risk management; and

(2) Each swap dealer and major swap participant shall coordinate with each derivatives clearing organization to which the swap dealer, major swap participant, or its clearing member, submits transactions for clearing, to facilitate prompt and efficient swap transaction processing in accordance with the requirements of § 39.12(b)(7) of this chapter.

(b) Swap clearing. With respect to each swap that is not executed on a swap execution facility or a designated contract market, each swap dealer and major swap participant shall:

(1) If such swap is subject to a mandatory clearing requirement pursuant to section 2(h)(1) of the Act and an exception pursuant to 2(h)(7) is not applicable, submit such swap for clearing to a derivatives clearing organization as soon as technologically practicable after execution of the swap, but no later than the close of business on the day of execution; or

(2) If such swap is not subject to a mandatory clearing requirement pursuant to section 2(h)(1) of the Act but is accepted for clearing by any derivatives clearing organization and the swap dealer or major swap participant and its counterparty agree that such swap will be submitted for clearing, submit such swap for clearing not later than the next business day after execution of the swap, or the agreement to clear, if later than execution.

## **PART 37 – SWAP EXECUTION FACILITIES**

4. Revise the authority citation for part 37 to read as follows:

**AUTHORITY:** 7 U.S.C. 1a, 2, 5, 6, 6c, 7, 7a-2, 7b-3 and 12a, as amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 124 Stat. 1376.

### **Subpart H – Financial Integrity of Transactions**

5. Add § 37.702 to read as follows:

#### **§ 37.702 General financial integrity.**

A swap execution facility must provide for the financial integrity of its transactions:

(a) [Reserved.]

(b) For transactions cleared by a derivatives clearing organization:

(1) By ensuring that the swap execution facility has the capacity to route transactions to the derivative clearing organization in a manner acceptable to the derivatives clearing organization for purposes of risk management; and

(2) By coordinating with each derivatives clearing organization to which it submits transactions for clearing, in the development of rules and procedures to facilitate prompt and efficient transaction processing in accordance with the requirements of § 39.12(b)(7) of this chapter.

(c) [Reserved.]

(d) [Reserved.]

## **PART 38 – DESIGNATED CONTRACT MARKETS**

6. Revise the authority citation for part 38 to read as follows:

**AUTHORITY:** 7 U.S.C. 1a, 2, 6, 6a, 6c, 6d, 6e, 6f, 6g, 6i, 6j, 6k, 6l, 6m, 6n, 7, 7a-2, 7b, 7b-1, 7b-3, 8, 9, 15, and 21, as amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 124 Stat. 1376.

### **Subpart L – Financial Integrity of Transactions**

7. Add § 38.601 to read as follows:

#### **§ 38.601 Mandatory clearing.**

(a) Transactions executed on or through the designated contract market, other than transactions in security futures products, must be cleared through a Commission-registered derivatives clearing organization, in accordance with the provisions of part 39 of this chapter.

(b) A designated contract market must coordinate with each derivatives clearing organization to which it submits transactions for clearing, in the development of rules and

procedures to facilitate prompt and efficient transaction processing in accordance with the requirements of § 39.12(b)(7) of this chapter.

## **PART 39 – DERIVATIVES CLEARING ORGANIZATIONS**

8. Revise the authority citation for part 39 to read as follows:

**AUTHORITY:** 7 USC 1a, 2, 5, 6, 6d, 7a-1, 7a-2, and 7b as amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 124 Stat. 1376.

### **Subpart B – Compliance with Core Principles**

9. Add § 39.12 to read as follows:

#### **§ 39.12 Participant and product eligibility.**

(a) [Reserved.]

(b)(1) [Reserved.]

(2) A derivatives clearing organization shall adopt rules providing that all swaps with the same terms and conditions, as defined by templates established under derivatives clearing organization rules, submitted to the derivatives clearing organization for clearing are economically equivalent within the derivatives clearing organization and may be offset with each other within the derivatives clearing organization.

(3) A derivatives clearing organization shall provide for non-discriminatory clearing of a swap executed bilaterally or on or subject to the rules of an unaffiliated swap execution facility or designated contract market.

(4) A derivatives clearing organization shall not require that one of the original executing parties must be a clearing member in order for a contract, agreement, or transaction to be eligible for clearing.

(5) A derivatives clearing organization shall select contract unit sizes and other terms and conditions that maximize liquidity, facilitate transparency in pricing, promote open access, and allow for effective risk management. To the extent appropriate to further these objectives, a derivatives clearing organization shall select contract units for clearing purposes that are smaller than the contract units in which trades submitted for clearing were executed.

(6) A derivatives clearing organization that clears swaps shall have rules providing that, upon acceptance of a swap by the derivatives clearing organization for clearing:

(i) The original swap is extinguished;

(ii) The original swap is replaced by equal and opposite swaps between clearing members and the derivatives clearing organization;

(iii) All terms of the cleared swaps must conform to templates established under derivatives clearing organization rules; and

(iv) If a swap is cleared by a clearing member on behalf of a customer, all terms of the swap, as carried in the customer account on the books of the clearing member, must conform to the terms of the cleared swap established under the derivatives clearing organization's rules.

(7) Time frame for clearing. (i) General. Each derivatives clearing organization shall coordinate with each swap execution facility and designated contract market that lists for trading a product that is cleared by the derivatives clearing organization, in developing rules and procedures to facilitate prompt and efficient processing of all contracts, agreements, and transactions submitted to the derivatives clearing organization for clearing.

(ii) Transactions executed on or subject to the rules of a swap execution facility or designated contract market. A derivatives clearing organization shall have rules that provide that the derivatives clearing organization will accept for clearing, immediately upon execution, all

contracts, agreements, and transactions that are listed for clearing by the derivatives clearing organization and

(A) That are entered into on a swap execution facility or designated contract market;

(B) For which the executing parties have clearing arrangements in place with clearing members of the derivatives clearing organization; and

(C) For which the executing parties identify the derivatives clearing organization as the intended clearinghouse.

(iii) Swaps not executed on or subject to the rules of a swap execution facility or a designated contract market and subject to mandatory clearing. A derivatives clearing organization shall have rules that provide that the derivatives clearing organization will accept for clearing, upon submission to the derivatives clearing organization, all swaps that are listed for clearing by the derivatives clearing organization and

(A) That are not executed on a swap execution facility or a designated contract market;

(B) That are subject to mandatory clearing pursuant to section 2(h) of the Act;

(C) That are submitted by the parties to the derivatives clearing organization, in accordance with § 23.506 of this chapter;

(D) For which the executing parties have clearing arrangements in place with clearing members of the derivatives clearing organization; and

(E) For which the executing parties identify the derivatives clearing organization as the intended clearinghouse.

(iv) Swaps not executed on or subject to the rules of a swap execution facility or a designated contract market and not subject to mandatory clearing. A derivatives clearing organization shall have rules that provide that the derivatives clearing organization will accept

for clearing, no later than the close of business on the day of submission to the derivatives clearing organization, all swaps that are listed for clearing by the derivatives clearing organization and

(A) That are not executed on a swap execution facility or a designated contract market;

(B) That are not subject to mandatory clearing pursuant to section 2(h) of the Act;

(C) That are submitted by the parties to the derivatives clearing organization, in accordance with § 23.506 of this chapter;

(D) For which the executing parties have clearing arrangements in place with clearing members of the derivatives clearing organization; and

(E) For which the executing parties identify the derivatives clearing organization as the intended clearinghouse.

(v) All swaps not executed on a swap execution facility or a designated contract market and submitted for clearing. A derivatives clearing organization shall have rules that provide that all swaps submitted to the derivatives clearing organization for clearing shall include written documentation that memorializes all of the terms of the transaction and legally supersedes any previous agreement. The confirmation of all terms of the transaction shall take place at the same time as the swap is accepted for clearing.

10. Add § 39.15 to read as follows:

**§ 39.15 Treatment of funds.**

(a)-(c) [Reserved.]

(d) Transfer of customer positions. A derivatives clearing organization shall have rules providing that, upon the request of a customer and subject to the consent of the receiving clearing member, the derivatives clearing organization will promptly transfer all or a portion of

such customer's portfolio of positions and related funds from the carrying clearing member of the derivatives clearing organization to another clearing member of the derivatives clearing organization, without requiring the close-out and re-booking of the positions prior to the requested transfer.

(e) Permitted investments. Funds and assets belonging to clearing members and their customers that are invested by a derivatives clearing organization shall be held in instruments with minimal credit, market, and liquidity risks. Any investment of customer funds or assets by a derivatives clearing organization shall comply with § 1.25 of this part, as if all such funds and assets comprise customer funds subject to segregation pursuant to section 4d(a) of the Act and Commission regulations thereunder.

Issued in Washington, DC, on February 24, 2011, by the Commission.

  
David A. Stawick,

Secretary of the Commission.

Appendices to Requirements for Processing, Clearing and Transfer of Customer Positions--  
Commission Voting Summary and Statements of Commissioners

NOTE: The following appendices will not appear in the Code of Federal Regulations

Appendix 1—Commission Voting Summary

On this matter, Chairman Gensler and Commissioners Dunn, Sommers, Chilton and O'Malia voted in the affirmative; no Commissioner voted in the negative.

Appendix 2—Statement of Chairman Gary Gensler

I support the proposed rulemaking regarding straight-through processing because it furthers the goal of expanding access to and strengthening the financial integrity of the swap markets. These proposed regulations would require and establish uniform standards for prompt processing, submission and acceptance for clearing of swaps eligible for clearing. Such uniform standards, similar to the practices in the futures markets, lower risk because they allow market participants to get the prompt benefit of clearing rather than having to first enter into a bilateral transaction that would subsequently be moved into a clearinghouse.

In addition, I support the requirement for prompt and efficient transfer of customer positions from a carrying clearing member of a clearinghouse to another clearing member of the clearinghouse, upon a customer's request. This would promote efficiency and avoid unnecessary delay and market disruption. Furthermore, users of derivatives could get the benefit of greater competition amongst clearing members.