

COMMODITY FUTURES TRADING COMMISSION

17 CFR Part 1

Order Establishing a New *De Minimis* Threshold Phase-In Termination Date

AGENCY: Commodity Futures Trading Commission.

ACTION: Order.

SUMMARY: The Commodity Futures Trading Commission (“Commission” or “CFTC”) is issuing an order (“Order”), pursuant to the Commission regulation establishing the *de minimis* exception to the swap dealer definition, to establish December 31, 2019 as the new *de minimis* threshold phase-in termination date.

DATES: Issued by the Commission on October 26, 2017.

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SUPPLEMENTARY INFORMATION:

I. Background

The Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”)¹ directed the CFTC and the U.S. Securities and Exchange Commission to jointly

¹ Pub. L. 111-203, 124 Stat. 1376 (2010). The text of the Dodd-Frank Act can be accessed on the Commission’s website, at www.cftc.gov.

further define the term “swap dealer” and to include therein a *de minimis* exception.² The CFTC’s further definition of swap dealer is provided in § 1.3(ggg).³ The *de minimis* exception therein provides that a person shall not be deemed to be a swap dealer unless its swap dealing activity exceeds an aggregate gross notional amount threshold of \$3 billion (measured over the prior 12-month period), subject to a phase-in period during which the gross notional amount threshold is set at \$8 billion.⁴ Absent further action by the Commission, the phase-in period is scheduled to terminate on December 31, 2018, at which time the *de minimis* threshold would decrease to \$3 billion.⁵

When § 1.3(ggg) was adopted, establishing the \$3 billion *de minimis* exception, the Commission explained that there was little swap dealing data available that could be used to guide it in setting a threshold level. The Commission expected that the implementation of swap data reporting may enable reassessment of the *de minimis* exception.⁶ Accordingly, in § 1.3(ggg), the Commission directed CFTC staff to issue a report, after a specified period of time, on topics relating to the *de minimis* exception “as appropriate, based on the availability of data and information.”⁷ Paragraph 1.3(ggg) further provides that after giving due consideration to the report and any associated

² See Dodd-Frank Act, sections 712(d) and 721. The definition of “swap dealer” can be found in section 1a(49) of the Commodity Exchange Act and as further defined in § 1.3(ggg). 7 U.S.C. 1a(49) and 17 CFR 1.3(ggg). The Commodity Exchange Act is at 7 U.S.C. 1, *et seq.* (2014), and is accessible on the Commission’s website at www.cftc.gov.

³ 17 CFR 1.3(ggg).

⁴ See 17 CFR 1.3(ggg)(4). See also Further Definition of “Swap Dealer,” “Security-Based Swap Dealer,” “Major Swap Participant,” “Major Security-Based Swap Participant” and “Eligible Contract Participant”, 77 FR 30596 (May 23, 2012). This Order does not impact the *de minimis* threshold for swaps with “special entities” as defined in the Commodity Exchange Act, section 4s(h)(2)(C). 7 U.S.C. 6s(h)(2)(C).

⁵ Order Establishing De Minimis Threshold Phase-In Termination Date, 81 FR 71605, 71607 (Oct. 18, 2016).

⁶ See 77 FR at 30634, 30640.

⁷ See 17 CFR 1.3(ggg)(4)(ii)(B).

public comment, the Commission may by order establish a termination date for the phase-in period or propose through rulemaking modifications to the *de minimis* exception.⁸

Staff issued for public comment the Swap Dealer *De Minimis* Exception Preliminary Report on November 18, 2015 (“Preliminary Report”).⁹ After consideration of the public comments received, and further data analysis, staff issued the Swap Dealer *De Minimis* Exception Final Staff Report¹⁰ on August 15, 2016 (“Final Report,” and together with the Preliminary Report, the “Staff Reports”). The Staff Reports analyzed the available swap data in conjunction with relevant policy considerations to assess alternative *de minimis* threshold levels and other potential changes to the *de minimis* exception. The Staff Reports noted that the swap market data available, while much improved since § 1.3(ggg) was first adopted, was still somewhat limited in providing detailed information for assessing appropriate changes to the *de minimis* exception. For example, notional amounts could only be analyzed for the interest rate and credit default swap asset classes because, at the time, sufficient reliable notional data was not available for the other asset classes. As a further example, some of the data analyzed for the Staff Reports had significant quality issues. One of the “key issues” identified in the Final Report for Commission consideration was whether to delay reduction of the *de minimis*

⁸ See 17 CFR 1.3(ggg)(4)(ii)(C).

⁹ Available at http://www.cftc.gov/idc/groups/public/@swaps/documents/file/dfreport_sddeminis_1115.pdf.

¹⁰ Available at http://www.cftc.gov/idc/groups/public/@swaps/documents/file/dfreport_sddeminis081516.pdf.

threshold to allow efforts to improve data quality to progress so that the Commission could better determine the appropriate *de minimis* threshold.¹¹

In October 2016, the Commission issued an order, pursuant to § 1.3(ggg)(4)(ii)(C)(I), establishing December 31, 2018 as the *de minimis* threshold phase-in termination date, thereby extending the original phase-in period by one year (“October 2016 Order”).¹² In the order, the Commission stated that the phase-in period extension provides additional time for further information to become available to more effectively reassess the *de minimis* exception.¹³ Given the twelve month lookback for calculating the swap dealing notional amount, a firm may need to start tracking its swap dealing activity on January 1, 2018 to determine whether its dealing activity would require it to register when the phase-in period ends on December 31, 2018.

II. New Phase-in Termination Date

As contemplated by the October 2016 Order, significant strides are being made in updating, improving, and reassessing the available swap data regarding the swap marketplace in a more granular manner. Though this data analysis is ongoing, the Commission believes that it will in the near future have more detailed data analysis to inform its consideration of possible modifications to the *de minimis* exception.¹⁴ However, any such modifications, if implemented, would not become effective until some point in 2018, when the Commission completes the proposal, public comment, and final rule amendment process pursuant to the Administrative Procedure Act.

¹¹ Final Report at 26.

¹² 81 FR 71605; 17 CFR 1.3(ggg)(4)(ii)(C)(I).

¹³ 81 FR at 71607.

¹⁴ The Commission also notes that the continuing efforts by the Division of Market Oversight to improve data quality have improved data analysis capabilities.

This timing creates some uncertainty for currently unregistered swap dealers that may be subject to registration if the \$3 billion *de minimis* threshold goes into effect on December 31, 2018. Such entities will not know what *de minimis* exception changes, if any, may become effective. Given this uncertainty, firms that might be subject to registration if the *de minimis* threshold decreases to \$3 billion would need to start managing, and perhaps altering, their swap dealing activity starting in January 2018 to remain below the \$3 billion threshold by December 31, 2018. Further, some firms might begin analyzing and adjusting their dealing activities prior to January 2018 if they do not want to be subject to registration. Such changes in behavior could lead to reduced competition, liquidity, and efficiency in the swap market, which may cause disruptions for the firms and their swap counterparties that might be unnecessary depending on the outcome of the continuing assessment of the *de minimis* exception.

Additionally, the Commission notes that a year's delay would provide additional time for the new Commissioners¹⁵ and the new Director of the Division of Swap Dealer and Intermediary Oversight, all of whom only joined the Commission in the last two months, to better familiarize themselves with the issues relevant to the *de minimis* exception and results of the swap data analysis currently underway.

Accordingly, the Commission believes that it is prudent to extend the phase-in period by one year. This extension will provide additional time for Commission staff to conduct data analysis regarding the *de minimis* exception, give market participants further clarity regarding when they will need to begin preparing for a change, if any, to the *de*

¹⁵ See Brian Quintenz Sworn In as a Commissioner of the U.S. Commodity Futures Trading Commission (Aug. 15, 2017), <http://www.cftc.gov/PressRoom/PressReleases/pr7602-17>; Rostin Behnam Sworn In as a Commissioner of the CFTC (Sep. 6, 2017), <http://www.cftc.gov/PressRoom/PressReleases/pr7610-17>. Additionally, there are currently two additional Commission vacancies that may be filled soon.

minimis exception, and provide additional time for new Commissioners and staff to become better apprised of issues relevant to this topic.

III. Conclusion and Order

For the reasons discussed above, and pursuant to its authority under § 1.3(ggg)(4)(ii)(C)(I), the Commission is establishing December 31, 2019 as the new termination date for the *de minimis* threshold phase-in period. The Commission notes that prior to the termination of the phase-in period, the Commission plans to take further action regarding the *de minimis* threshold.

IV. Related Matters

A. Paperwork Reduction Act

The Paperwork Reduction Act (“PRA”)¹⁶ imposes certain requirements on Federal agencies in connection with their conducting or sponsoring any collection of information as defined by the PRA. This Order does not impose any new recordkeeping or information collection requirements, or other collections of information that require approval of the Office of Management and Budget under the PRA.

B. Cost-Benefit Considerations

Section 15(a) of the Commodity Exchange Act (“CEA”) requires the Commission to consider the costs and benefits of its actions before promulgating a regulation under the CEA or issuing certain orders.¹⁷ Section 15(a) further specifies that the costs and benefits shall be evaluated in light of five broad areas of market and public concern: (i) protection of market participants and the public; (ii) efficiency, competitiveness, and

¹⁶ 44 U.S.C. 3501 *et seq.*

¹⁷ 7 U.S.C. 19(a).

financial integrity of futures markets; (iii) price discovery; (iv) sound risk management practices; and (v) other public interest considerations. In this section, the Commission considers the costs and benefits resulting from its determinations with respect to the Section 15(a) factors.

1. Background

As discussed above, § 1.3(ggg)(4)(i) provides an exception from the swap dealer definition for persons who engage in a *de minimis* amount of swap dealing activity. Currently, under § 1.3(ggg)(4)(i), a person shall not be deemed to be a swap dealer unless its swap dealing activity exceeds an aggregate gross notional amount threshold of \$3 billion (measured over the prior 12-month period), subject to a phase-in period during which the gross notional amount threshold is set at \$8 billion.¹⁸ The phase-in period would have terminated on December 31, 2018, and the *de minimis* threshold would have decreased to \$3 billion, absent this Order.¹⁹ This would have required firms to start tracking their swap activity beginning January 1, 2018 to determine whether their dealing activity over the course of that year would require them to register as swap dealers.

The \$3 billion threshold, which, absent this Order, would be effective on December 31, 2018, sets the baseline for the Commission's consideration of the costs and benefits of this Order.²⁰ Accordingly, the Commission considers the costs and benefits that will result from extending the phase-in period.

¹⁸ 17 CFR 1.3(ggg)(4)(i). *See generally* 77 FR at 30626-35. *See also* note 4, *supra*.

¹⁹ *See* 81 FR 71605.

²⁰ *See* 77 FR at 30702-14 (discussing the cost-benefit considerations with regard to the final swap dealer definition); 81 FR at 71607.

2. General Cost and Benefit Considerations

There are several policy objectives underlying swap dealer regulation and the *de minimis* exception to the swap dealer definition. The primary policy objectives of swap dealer regulation include the reduction of systemic risk, increased counterparty protections, and market efficiency, orderliness, and transparency.²¹ Registered swap dealers are subject to a broad range of requirements, including, *inter alia*, registration, internal and external business conduct standards, reporting, recordkeeping, risk management, posting and collecting margin, and chief compliance officer designation and responsibilities. As noted in the § 1.3(ggg) adopting release, generally, the lower the *de minimis* threshold, the greater the number of entities that are subject to these requirements, which could decrease systemic risk, increase counterparty protections, and promote swap market efficiency, orderliness, and transparency.²²

The Commission also considers policy objectives furthered by a *de minimis* exception, which include regulatory certainty, allowing limited ancillary dealing, encouraging new participants to enter the swap dealing market, and regulatory efficiency.²³ Generally, the higher the *de minimis* threshold, the greater the number of entities that are able to engage in dealing activity without being required to register, which could increase competition and liquidity in the swap market.²⁴ In addition, because competitive markets may be more efficient, a higher *de minimis* threshold might improve swap market efficiency. Further, the Commission notes that it has been

²¹ 77 FR at 30628-30, 30707-08.

²² *Id.* at 30628-30, 30703, 30707-08.

²³ *Id.* at 30628-30, 30707-08.

²⁴ Alternatively, the Commission notes that a lower *de minimis* threshold may lead to potential changes in market behavior, including, for example, product innovation.

suggested that a higher threshold could allow the Commission to expend its resources on entities with larger swap dealing activities warranting more oversight. An alternative view is that the *de minimis* threshold should be set based on policy independent of consideration of the Commission's resources.

Extending the phase-in period by one year will delay realization of the policy benefits associated with the \$3 billion *de minimis* threshold, but will also extend the policy benefits associated with a higher *de minimis* threshold. The additional time to adjust to the \$3 billion *de minimis* threshold also would potentially increase regulatory certainty for some market participants. Given that the *de minimis* exception is subject to a 12-month look-back, extending the phase-in period to December 31, 2019 would allow entities that would potentially have to register as swap dealers additional time to adjust their activities and prepare for the compliance obligations related to swap dealer registration.

3. Section 15(a)

Section 15(a) of the CEA requires the Commission to consider the effects of its actions in light of the following five factors. This Order will delay the potential costs and benefits discussed below by one year.

(i) Protection of Market Participants and the Public

Providing regulatory protections for swap counterparties who may be less experienced or knowledgeable about the swap products offered by swap dealers (particularly end-users who use swaps for hedging or investment purposes) is a fundamental policy goal advanced by the regulation of swap dealers. The Commission recognizes that the \$3 billion *de minimis* threshold may result in more entities being

required to register as swap dealers compared to an \$8 billion threshold, thereby extending counterparty protections to a greater number of market participants. Further, swap dealer regulation is intended to reduce systemic risk in the swap market because registered swap dealers are subject to a broad range of requirements, including, *inter alia*, requirements applicable to internal and external business conduct standards, reporting and recordkeeping, risk management, posting and collecting margin, and chief compliance officer designation and responsibilities. Pursuant to the Dodd-Frank Act, the Commission has proposed or adopted regulations for swap dealers – including margin and risk management requirements – designed to mitigate the potential systemic risk inherent in the swap market. Therefore, the Commission recognizes that a lower *de minimis* threshold may result in more entities being required to register as swap dealers, thereby potentially further reducing systemic risk.

(ii) Efficiency, Competitiveness, and Financial Integrity of Markets

Other goals of swap dealer regulation are swap market transparency, orderliness, and efficiency. These benefits are achieved through regulations requiring, for example, swap dealers to keep trading records and report trades, provide counterparty disclosures about swap risks and pricing, and undertake portfolio reconciliation and compression exercises. Accordingly, the Commission notes that a lower *de minimis* threshold may have a positive effect on the efficiency and integrity of the markets.

However, the Commission also recognizes that the efficiency and competitiveness of the swap market may be negatively impacted if the *de minimis* threshold is set too low by potentially increasing barriers to entry that may stifle competition and reduce swap market efficiency. For example, if entities choose to reduce or cease their swap dealing

activities so that they would not need to register if the *de minimis* threshold decreases to \$3 billion, the number or availability of market makers for swaps may be reduced, which could lead to increased costs for potential counterparties and end-users through having to pay higher spreads when undertaking swap transactions or foregoing the benefits of engaging in certain swap transactions that they would otherwise have undertaken.

(iii) Price Discovery

The Commission preliminarily believes that a \$3 billion *de minimis* threshold may discourage participation of new swap dealers and ancillary dealing. If there are fewer entities engaged in dealing, there may be a negative effect on price discovery.

(iv) Sound Risk Management

The Commission notes that a \$3 billion *de minimis* threshold could lead to better risk management practices because a greater number of entities would be required by regulation to: (i) develop and implement detailed risk management programs; (ii) adhere to business conduct standards that reduce operational and other risks; and (iii) satisfy margin requirements for uncleared swaps.

(v) Other Public Interest Considerations

The Commission has not identified any other public purpose considerations for this Order.

C. *Antitrust Considerations*

Section 15(b) of the CEA requires the Commission to take into consideration the public interest to be protected by the antitrust laws and endeavor to take the least anticompetitive means of achieving the objectives of the CEA, in issuing any order or

adopting any Commission rule or regulation. The Commission does not anticipate that the Order discussed herein will result in anti-competitive behavior.

V. Order

In light of the foregoing, IT IS ORDERED, pursuant to the Commission's authority under § 1.3(ggg)(4)(ii)(C)(1), that the *de minimis* threshold phase-in termination date shall be December 31, 2019.

The Commission retains the authority to condition further, modify, suspend, terminate, or otherwise restrict any of the terms of the Order provided herein, in its discretion.

Issued in Washington, DC, on October 26, 2017, by the Commission.

Christopher J. Kirkpatrick,

Secretary of the Commission.

Appendix to Order Establishing a New *De Minimis* Threshold Phase-In Termination Date – Commission Voting Summary

On this matter, Chairman Giancarlo and Commissioner Quintenz voted in the affirmative. Commissioner Behnam voted in the negative.