



# Commodity Futures Trading Commission

## Office of Public Affairs

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### Fact Sheet and Q&A – Notice of Proposed Rulemaking to Amend Capital and Financial Reporting Requirements of Swap Dealers and Major Swap Participants

The Commodity Futures Trading Commission (“Commission” or “CFTC”) is proposing to amend Commission regulations 23.100, 23.101, 23.102, 23.103, 23.105, Appendices B and C to Subpart E of Part 23 (“Appendix B” and “Appendix C”), and the Commission’s Form 1-FR-FCM to address specific issues identified during the implementation of the final rule on capital and financial reporting requirements for swap dealers (“SDs”) and major swap participants (“MSPs”).<sup>1</sup>

Specifically, the proposal would: (i) codify the relief provided in CFTC Letters No. 21-15<sup>2</sup> and 21-18<sup>3</sup> with respect to the tangible net worth capital approach and financial reporting requirements for bank SDs, respectively; (ii) clarify other matters including the general applicability of reporting schedules, the process for the approval of subordinated debt, the reporting timeframe required for the notification of a substantial reduction in capital, certain required statements related to any material differences between audited and unaudited financial reports, and the format of required public disclosures of regulatory capital; and (iii) adopt changes to the Commission’s Form 1-FR-FCM to reflect changes previously adopted for FCM net capital requirements related to swaps.

#### Background

On July 24, 2020, the Commission adopted capital requirements for nonbank SDs and nonbank MSPs, as well as financial reporting requirements for bank SDs, bank MSPs, nonbank SDs, and nonbank MSPs.<sup>4</sup>

Following the adoption of the Final Rule and during the 14-month compliance period, the Commission’s Market Participants Division (“MPD”) worked with both the National Futures Association (“NFA”) and the U.S. Securities and Exchange Commission (“SEC”) to adopt several processes, procedures, and forms for the acceptance of financial reports and notifications in accordance with the Final Rule. In so doing, MPD received several compliance related questions, and as a result, issued eight staff letters.<sup>5</sup> The Commission is now proposing to codify two such staff letters, interpretative CFTC

<sup>1</sup> Capital Requirements of Swap Dealers and Major Swap Participants, 85 FR 57462 (Sept. 15, 2020) (the “Final Rule”).

<sup>2</sup> CFTC Letter No. 21-15, June 29, 2021, available at <https://www.cftc.gov/csl/21-15/download>.

<sup>3</sup> CFTC Letter No. 21-18, Aug. 31, 2021, available at <https://www.cftc.gov/csl/21-18/download>.

<sup>4</sup> “Nonbank SDs” and “nonbank MSPs” are the terms used to refer to SDs and MSPs, respectively, that are not subject to the capital requirements of a prudential regulator and therefore subject to the CFTC’s capital requirements, whereas “bank SDs” and “bank MSPs” are the terms used to refer to SDs and MSPs, respectively, that are subject to the capital requirements for a prudential regulator. The term “prudential regulator” is defined in section 1a(39) of the Commodity Exchange Act (“CEA” or the “Act”) to include the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Farm Credit Administration, and the Federal Housing Finance Agency, as applicable to the SD.

<sup>5</sup> CFTC Letter No. 21-15; CFTC Letter No. 21-18; CFTC Letter No. 21-20, Sept. 30, 2021, available at <https://www.cftc.gov/csl/21-20/download>; CFTC Letter No. 21-21, Sept. 30, 2021, available at [https://www.cftc.gov/csl/21-](https://www.cftc.gov/csl/21-21)

Letter No. 21-15 regarding capital and financial reporting requirements for nonbank SDs and nonbank MSPs electing the tangible net worth capital approach<sup>6</sup> and the time-limited no-action CFTC Letter No. 21-18 regarding financial reporting requirements for bank SDs.<sup>7</sup> The proposal also addresses several other recommended amendments that are technical in nature and the result of the Commission’s experience in implementing the rule. These recommended amendments are not intended to change the Commission’s capital approach adopted in the Final Rule and are expected to impose only minimal additional cost burdens. Based on its experience administering the Final Rule since its promulgation in 2020 and in consideration of relevant market participants’ feedback, the Commission proposed for comment the following specific amendments to its capital and financial reporting requirements for SDs and MSPs:

1. Codify CFTC Letter No. 21-15 by: (1) amending Commission regulation 23.100 to revise the definitions of “tangible net worth” and “predominantly engaged in non-financial activities” to provide that the tangible net worth capital approach may be utilized by nonbank SDs and nonbank MSPs; (2) amending Commission regulation 23.105 to provide that SDs may apply the test to determine whether they are predominantly engaged in non-financial activities at the parent or entity level and using generally accepted accounting principles (“GAAP”) as adopted in the United States or International Financial Reporting Standards (“IFRS”); and (3) amending Commission regulation 23.105(l) to state that an SD’s position and other related exposure reporting must be made at the same periodicity as financial reporting, which for SDs electing the tangible net worth capital approach is quarterly.
2. Codify CFTC Letter No. 21-18 by: (1) amending Commission regulation 23.105(p) to (a) permit non-U.S. domiciled bank SDs to file the applicable financial reporting within 90 days of the end of the financial reporting period; (b) accept balance sheet and regulatory capital schedules under FFIEC reports (Schedule RC and Schedule RC-R) for U.S. domiciled bank SDs in lieu of the current forms included at Appendix C; (c) accept the filing of such schedules at the same time as filed with prudential regulators; and (d) for Non-U.S. bank SDs, permit the filing of a balance sheet and statement of regulatory capital schedules in the format provided to the bank SDs’ home country regulator but subject to the requirement that they must be in English and converted to U.S. dollars and be filed no later than 90 days following the reporting period end date; and (2) amending Appendix C to eliminate the duplicative forms and retain only Schedule 1, which contains position information and is required of all SDs.
3. Amend Commission regulations 23.105(k) and (l) and the titles of Schedules 1-4 in Appendix B to provide that such supplemental schedules are intended to be provided by all nonbank SDs, and further amend Commission regulation 23.105(l) to provide that the supplemental schedules must be submitted on a monthly or quarterly basis, as applicable per the proposed codification of CFTC Letter No. 21-15 above.

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21/download; CFTC Letter No. 21-22, Sept. 30, 2021, available at <https://www.cftc.gov/csl/21-22/download>; CFTC Letter No. 21-23, Sept. 30, 2021, available at <https://www.cftc.gov/csl/21-23/download>; CFTC Letter No. 22-01, Jan. 5, 2022, available at <https://www.cftc.gov/csl/22-01/download>; CFTC Letter No. 22-02, Jan. 5, 2022, available at <https://www.cftc.gov/csl/22-02/download>.

<sup>6</sup> Nonbank SDs subject to the Commission’s capital requirements are permitted to elect one of three approaches to calculating their regulatory capital. *See* 17 CFR 23.101. One such option permits certain qualifying nonbank SDs to use a regulatory capital approach that is based on the firm’s tangible net worth. 17 CFR 23.101(a)(2). To qualify for the tangible net worth capital approach, a nonbank SD must be “predominantly engaged in non-financial activities.” The term “predominantly engaged in non-financial activities” is defined in Commission regulation 23.100, and provides that a nonbank SD, or its parent entity, does not receive more than 15% of its respective consolidated revenue from financial activities or hold financial assets in an amount that exceeds 15% of its respective total consolidated assets. 17 CFR 23.100.

<sup>7</sup> Bank SDs or bank MSPs are subject to the capital requirements and monitoring of a prudential regulator, and as a result, the Commission only adopted limited financial reporting for such registrants. The Commission finalized limited financial reporting requirements for bank SDs in recognition that prudential regulators have an obligation to impose capital requirements on bank SDs and have primary responsibility under the Act to monitor bank SD capital. *See* 7 U.S.C. 6s(e)(2)(i). There are no MSPs registered with the Commission, and only two firms have ever been provisionally-registered as MSPs. Therefore, no MSPs are subject to the capital requirements and monitoring of a prudential regulator. For brevity, this fact sheet only discusses proposals related to SDs, although the rules and any proposed amendments will continue to address MSPs, should they ever become registered.

4. Amend Commission regulation 23.101(a) to provide that subordinated debt qualifying for net capital is subject to a determination of that qualification by either the Commission or NFA. Further, amend Commission regulation 23.105(c) to provide references that incorporate the immediate notifications required for SDs that are also FCMs and to provide that the period of time required for an SD's notification of a substantial reduction of capital should be made within two business days.
5. Amend references within the Final Rule to provide clarity on applicable market and credit risk charges both for SDs using internal models electing the Bank-Based Capital Approach in Commission regulation 23.102 and for SDs not electing the Bank-Based Capital Approach and not electing to use internal models in Commission regulation 23.103.
6. Amend Commission regulation 23.105(d) to provide that SDs that are also registered with the SEC as either broker dealers ("BDs") or security-based swap dealers ("SBSDs") must file financial reports required to be filed with the SEC, and SDs also registered as FCMs must file Form 1-FR-FCM (or such other form as is permissible by FCM requirements). Further, amend Commission regulation 23.105(e) to establish that if no material differences exist between a required audited financial report and an unaudited financial report that an affirmative statement to that effect is required. Additionally, amend Commission regulation 23.105(e) to establish that SDs that are also FCMs must file the audited reports that are required of FCMs (or permitted to be filed by FCMs), including a supplemental accountants report on material inadequacies concurrently with the audited financial report.
7. Amend Commission regulation 23.105(i) to provide that the applicable public disclosure of SD unaudited statement of financial condition information in Commission regulation 23.105(i)(1)(i) includes footnote disclosures and that the amounts of regulatory capital and required minimum regulatory capital to be publicly disclosed in both Commission regulations 23.205(i)(1) and (2) need not be included as a schedule or in any particular format.
8. Amend Form 1-FR-FCM to conform with the changes adopted in the Final Rule to FCM net capital requirements, including adding reporting lines for the market and credit risk charges for swaps and for 2% of the risk margin amount in required net capital for FCMs which are also SDs.

## Objective

The Commission is seeking to amend the capital and financial reporting requirements of SDs and MSPs to address challenges identified in the implementation of those requirements.

The Commission believes that the proposal supports the Final Rule's objective of imposing capital and financial reporting requirements for SDs and MSPs as directed by the Congressional mandate.<sup>8</sup>

## Proposed Rulemaking Q & A

### 1. Who would be affected by the proposed changes?

SDs electing the tangible net worth capital approach and non-U.S. bank SDs would be primarily impacted. Other SDs may be impacted by the further clarifications, but such impact is not expected to be substantial in relation to the general capital and financial reporting requirements for SDs.

### 2. What policy considerations motivated the proposed changes?

The Commission believes that the capital and financial reporting requirements for SDs contained in the Commission's regulations should be clear, and thus proposes to codify two important staff implementation letters being relied upon

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<sup>8</sup> Section 4s(e) of the Commodity Exchange Act ("CEA" or the "Act"), 7 U.S.C § 6s(e), which is contained in Section 731 of the Dodd-Frank Act, requires the Commission to adopt minimum capital and margin requirements for SDs and MSPs that are not subject to a prudential regulator. Section 731 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Public Law 111-203, 124 Stat. 1376 (2010) (the "Dodd-Frank Act"). The text of the Dodd-Frank Act is available at <http://www.cftc.gov/LawRegulation/OTCDERIVATIVES/index.htm>.

by certain SDs. The Commission further believes that adding specificity or detail to various existing requirements, (such as timeframes for notices, the approval process for subordinated debt qualifying as capital, etc.) will enhance SDs' ability to clearly demonstrate compliance with capital and financial reporting requirements.

**3. Why is the Commission proposing the amendments at this time?**

The Commission intends these clarifying amendments to address outstanding issues identified during the implementation of the Final Rule, two years past the implementation date of the Final Rule, which the Commission believes is a sufficient time for registrants to have identified significant problems or difficulties with the Final Rule.