

**COMMODITY FUTURES TRADING COMMISSION**

**17 CFR Parts 39 and 140**

**RIN 3038-AE65**

**Exemption from Derivatives Clearing Organization Registration**

**AGENCY:** Commodity Futures Trading Commission.

**ACTION:** Notice of proposed rulemaking.

**SUMMARY:** The Commodity Futures Trading Commission (Commission) is proposing amendments to its regulations to establish a regulatory framework within which the Commission may exempt a clearing organization that is organized outside of the United States (hereinafter referred to as “non-U.S. clearing organization”) from registration as a derivatives clearing organization (DCO) in connection with the clearing organization’s clearing of swaps. In addition, the Commission is proposing certain amendments to its delegation provisions in its regulations.

**DATES:** Comments must be received on or before [INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER].

**ADDRESSES:** You may submit comments, identified by “Exemption from Derivatives Clearing Organization Registration” and RIN number 3038-AE65, by any of the following methods:

- CFTC Comments Portal: <https://comments.cftc.gov>. Select the “Submit Comments” link for this rulemaking and follow the instructions on the Public Comment Form.

- Mail: Send to Christopher Kirkpatrick, Secretary of the Commission, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW, Washington, DC 20581.

- Hand Delivery/Courier: Follow the same instructions as for Mail, above.

Please submit your comments using only one of these methods. To avoid possible delays with mail or in-person deliveries, submissions through the CFTC Comments Portal are encouraged.

All comments must be submitted in English, or if not, accompanied by an English translation. Comments will be posted as received to <https://comments.cftc.gov>. You should submit only information that you wish to make available publicly. If you wish the Commission to consider information that you believe is 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 <https://comments.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 the public comment file and will be considered as required under the Administrative Procedure Act and other applicable laws, and may be accessible under the FOIA.

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<sup>1</sup> 17 CFR 145.9. Commission regulations referred to herein are found at 17 CFR chapter I (2018), and are accessible on the Commission's website at <https://www.cftc.gov/LawRegulation/CommodityExchangeAct/index.htm>.

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## **I. Background**

### **A. Project KISS**

The Commission is engaging in an agency-wide review of its rules, regulations, and practices to make them simpler, less burdensome, and less costly, and to make progress on G-20 regulatory reforms. This initiative is called Project KISS, which stands for “Keep It Simple, Stupid.”<sup>2</sup> The Commission is proposing to adopt regulations that would codify the policies and procedures that the Commission is currently following with respect to granting exemptions from DCO registration in order to make such policies and procedures transparent to all potential applicants.

### **B. Statutory and Regulatory Framework for Swaps Execution and Clearing**

The Commodity Exchange Act (CEA)<sup>3</sup> provides that a clearing organization may not “perform the functions of a [DCO]”<sup>4</sup> with respect to swaps unless the clearing organization is registered with the Commission.<sup>5</sup> However, the CEA also permits the Commission to conditionally or unconditionally exempt a clearing organization from

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<sup>2</sup> See Remarks of Acting Chairman J. Christopher Giancarlo before the 42nd Annual International Futures Industry Conference in Boca Raton, FL, Mar. 15, 2017, available at <https://www.cftc.gov/PressRoom/SpeechesTestimony/opagiancarlo-20>. On February 24, 2017, President Donald J. Trump issued Executive Order 13777: Enforcing the Regulatory Reform Agenda (EO 13777). EO 13777 directs federal agencies, among other things, to designate a Regulatory Reform Officer and establish a Regulatory Reform Task Force. Although the CFTC, as an independent federal agency, is not bound by EO 13777, the Commission is nevertheless engaging in an agency-wide review of its rules, regulations, and practices to make them simpler, less burdensome, and less costly. See Request for Information, 82 FR 23756 (May 24, 2017).

<sup>3</sup> 7 U.S.C. 1 *et seq.*

<sup>4</sup> The term “derivatives clearing organization” is statutorily defined to mean a clearing organization in general. However, for purposes of the discussion herein, the term “DCO” refers to a Commission-registered DCO, the term “exempt DCO” refers to a derivatives clearing organization that is exempt from registration, and the term “clearing organization” refers to a clearing organization that: (a) is neither registered nor exempt from registration with the Commission as a DCO; and (b) falls within the definition of “derivatives clearing organization” under Section 1a(15) of the CEA, 7 U.S.C. 1a(15), and “clearing organization or derivatives clearing organization” under Regulation 1.3, 17 CFR 1.3.

<sup>5</sup> Section 5b(a) of the CEA, 7 U.S.C. 7a-1(a).

registration for the clearing of swaps if the Commission determines that the clearing organization is subject to “comparable, comprehensive supervision and regulation” by appropriate government authorities in the clearing organization’s home country.<sup>6</sup>

To date, the Commission has exempted four non-U.S. clearing organizations from DCO registration. The Commission is proposing to adopt regulations that would codify the policies and procedures that the Commission is currently following with respect to granting exemptions from DCO registration and would make such policies and procedures transparent to all potential applicants.

### C. Statutory and Regulatory Requirements for Registration and Operation of DCOs

As previously noted, the CEA requires a clearing organization that clears swaps to be registered with the Commission as a DCO. However, in order to be registered and maintain registration as a DCO, a clearing organization must comply with the core principles for DCOs set forth in the CEA (DCO Core Principles)<sup>7</sup> and all applicable Commission regulations.<sup>8</sup>

The Commission may conditionally or unconditionally exempt a clearing organization from registration for the clearing of swaps if the Commission determines that the clearing organization is subject to “comparable, comprehensive supervision and regulation” by the clearing organization’s home country regulator(s). The Commission has construed “comparable, comprehensive supervision and regulation” to mean that the home country’s supervisory and regulatory framework should be consistent with, and

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<sup>6</sup> Section 5b(h) of the CEA, 7 U.S.C. 7a-1(h). Section 5b(h) also permits the Commission to exempt from DCO registration a securities clearing agency registered with the Securities and Exchange Commission; however, the Commission is not proposing to exempt securities clearing agencies at this time.

<sup>7</sup> 7 U.S.C. 7a-1(c)(2)(A).

<sup>8</sup> See 17 CFR parts 1-190 including, in particular, Part 39, which implements the DCO Core Principles.

achieve the same outcome as, the statutory and regulatory requirements applicable to registered DCOs. This outcomes-based approach reflects the Commission’s recognition that a foreign jurisdiction’s supervisory and regulatory scheme applicable to its clearing organizations may differ from the Commission’s in certain respects, but nevertheless may achieve the same underlying goals. This approach also supports the Commission’s effort to strike an appropriate balance by focusing on the risk implications to the United States, while promoting global harmonization.

Further, the Commission has deemed a supervisory and regulatory framework that conforms to the Principles for Financial Market Infrastructures (PFMIs)<sup>9</sup> to be comparable to, and as comprehensive as, the supervisory and regulatory requirements applicable to registered DCOs.<sup>10</sup> Notably, the Commission was a key contributor to the joint efforts of the Committee on Payments and Market Infrastructures (CPMI)<sup>11</sup> and the Technical Committee of the International Organization of Securities Commissions (IOSCO) to develop the PFMI, which apply to clearing organizations.<sup>12</sup> In addition to

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<sup>9</sup> See CPMI-IOSCO, Principles for financial market infrastructures (Apr. 2012), available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD377-PFMI.pdf>. The PFMI define a “financial market infrastructure” as a “multilateral system among participating institutions, including the operator of the system, used for the purposes of clearing, settling, or recording payments, securities, derivatives, or other financial transactions.” See PFMI, ¶ 1.8. Additionally, the PFMI are “broadly designed to apply to all systemically important [financial market infrastructures].” See PFMI, ¶ 1.20.

<sup>10</sup> This conclusion is consistent with previous Commission determinations. See e.g., Regulation 50.52(b)(4)(i)(E), 17 CFR 50.52(b)(4)(i)(E) (permitting eligible affiliate counterparties that are located in certain jurisdictions to satisfy a condition to electing the exemption by clearing the swap through a DCO or a clearing organization that is subject to supervision by appropriate government authorities in the clearing organization’s home country and that has been assessed to be in compliance with the PFMI).

<sup>11</sup> CPMI was formerly the Committee on Payment and Settlement Systems; it was renamed effective September 1, 2014. See <http://www.bis.org/press/p140901.htm>.

<sup>12</sup> In order to promote effective and consistent global regulation of swaps, Section 752 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) directs the Commission to consult and coordinate with foreign regulatory authorities on the establishment of consistent international standards with respect to the regulation of swaps, among other things. Section 752 of the Dodd-Frank Act, Public Law 111-203, 124 Stat. 1376 (2010), codified at 15 U.S.C. 8325.

contributing to the development of the PFMI, the Commission serves as a member of the CPMI-IOSCO task force that monitors implementation of the PFMI. The PFMI are comparable to the DCO Core Principles and applicable Commission regulations in purpose and scope. Both address major elements critical to the safe and efficient operations of clearing organizations, such as risk management, adequacy of financial resources, default management, margin, settlement, and participation requirements.<sup>13</sup> In light of the foregoing, the Commission believes that a supervisory and regulatory framework that adheres to the framework under the PFMI achieves outcomes that are comparable to that of the supervisory and regulatory requirements applicable to registered DCOs. Accordingly, the Commission proposes to continue to use the PFMI framework as the benchmark for making a comparability determination with respect to a foreign jurisdiction's supervisory and regulatory scheme.

## **II. Proposed Amendments to Part 39**

### **A. Regulation 39.1 – Scope**

The Commission is proposing to amend Regulation 39.1 to state that the provisions of subpart A of Part 39 apply to any registered DCO or, as applicable, any entity applying to be registered as a DCO or applying to be exempt from DCO registration. Regulation 39.3, which is contained in subpart A and is not proposed to be amended, sets forth procedures for DCO registration. Proposed Regulation 39.6, which also would be contained in subpart A, would set forth the requirements for an exemption from DCO registration, as discussed below.

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<sup>13</sup> See, e.g., Derivatives Clearing Organizations and International Standards, 78 FR 72476 (Dec. 2, 2013) (adopting final rules).

## B. Regulation 39.2 – Definitions

In connection with the proposed exemption regulations, the Commission is proposing to add five definitions to Regulation 39.2, for purposes of Part 39 only.

The Commission proposes to define the term “exempt derivatives clearing organization” to mean a derivatives clearing organization that the Commission has exempted from registration under Section 5b(a) of the CEA, pursuant to Section 5b(h) of the CEA and Regulation 39.6.

The Commission proposes to define the term “good regulatory standing” to mean, with respect to a non-U.S. clearing organization that is authorized to act as a clearing organization in its home country, that either there has been no finding by the home country regulator of material non-observance of the PFMIIs or other relevant home country legal requirements, or there has been such a finding by the home country regulator, but it has been or is being resolved to the satisfaction of the home country regulator by means of corrective action taken by the clearing organization. The Commission believes that this is a workable definition from the standpoint of both the Commission and the home country regulator in that it establishes a basis for providing the Commission with a high degree of assurance as to the clearing organization’s observance of the PFMIIs, while only seeking from the home country regulator a representation that it can reasonably make.

The Commission proposes to define the term “home country” to mean, with respect to a non-U.S. clearing organization, the jurisdiction in which the clearing organization is organized.

The Commission proposes to define the term “home country regulator,” with respect to a non-U.S. clearing organization, as an appropriate government authority which licenses, regulates, supervises, or oversees the clearing organization’s clearing activities in the home country. The proposed definition is consistent with Section 5b(h) of the CEA, which provides, in relevant part, that the Commission may exempt a clearing organization from registration for the clearing of swaps if the Commission determines that the clearing organization is subject to comparable, comprehensive supervision and regulation by the appropriate government authorities in the home country of the clearing organization. Use of the term “an appropriate government authority” rather than “the appropriate government authority” is intended to recognize that in some foreign jurisdictions there may be more than one government authority that supervises and regulates a clearing organization.

The Commission proposes to define the term “Principles for Financial Market Infrastructures” as the PFMI published by CPMI-IOSCO in April 2012, as updated, revised, or otherwise amended.<sup>14</sup>

### C. Regulation 39.6 – Exemption Provisions

Proposed Regulation 39.6 would implement Section 5b(h) of the CEA by setting forth the regulatory framework within which the Commission may exempt a clearing organization from DCO registration in connection with the clearing of swaps. After Section 5b(h) was enacted in 2010, clearing organizations outside the United States began inquiring as to how they could go about obtaining an exemption. Because the

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<sup>14</sup> The Commission proposes to include this language to recognize that CPMI-IOSCO could offer further interpretation of or guidance on the PFMI. See, e.g., CPMI-IOSCO, Resilience of central counterparties: Further guidance on the PFMI (July 2017), available at <https://www.bis.org/cpmi/publ/d163.pdf>.

Commission had not yet developed a framework for granting exemptions, the Commission's Division of Clearing and Risk (DCR) began granting time-limited no-action relief to these clearing organizations which permit them to engage in swap clearing activity that would otherwise require registration as a DCO.<sup>15</sup> After careful consideration of the issues involved, DCR staff presented initial thoughts on granting exemptions at a May 2014 meeting of the Commission's Global Markets Advisory Committee. Finally, in November 2014, DCR sent a letter to those clearing organizations that had received no-action relief, advising them on how to petition the Commission for an exemption. In response to petitions submitted in accordance with the terms of the letter, the Commission issued orders of exemption from DCO registration to ASX Clear (Futures) Pty Limited (ASX), Korea Exchange, Inc. (KRX), Japan Securities Clearing Corporation (JSCC), and OTC Clearing Hong Kong Limited (OTC Clear).<sup>16</sup> Proposed Regulation 39.6 would codify the policies and procedures that the Commission is currently following with respect to granting exemptions from DCO registration and would make such policies and procedures transparent to all potential applicants for an exemption.

## 1. Eligibility for Exemption

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<sup>15</sup> See, e.g., CFTC Letter No. 16-56 (May 31, 2016) (granting no-action relief to Shanghai Clearing House); CFTC Letter No. 14-107 (Aug. 18, 2014) (granting no-action relief to Clearing Corporation of India Ltd.); CFTC Letter No. 14-87 (June 26, 2014) (granting no-action relief to Korea Exchange, Inc.); CFTC Letter No. 14-68 (May 7, 2014) (granting no-action relief to OTC Clearing Hong Kong Limited and certain of its clearing members); CFTC Letter No. 14-07 (Feb. 6, 2014) (granting no-action relief to ASX Clear (Futures) Pty Limited); and CFTC Letter No. 12-56 (Dec. 17, 2012) (granting no-action relief to Japan Securities Clearing Corporation and certain of its clearing participants).

<sup>16</sup> See ASX Amended Order of Exemption from Registration (Jan. 28, 2016), available at <http://www.cftc.gov/idc/groups/public/@otherif/documents/ifdocs/asxclearamrdorderdcoexemption.pdf>; KRX Order of Exemption from Registration (Oct. 26, 2015), available at <http://www.cftc.gov/idc/groups/public/@otherif/documents/ifdocs/krxdcoexemptorder10-26-15.pdf>; JSCC Order of Exemption from Registration (Oct. 26, 2015), available at <http://www.cftc.gov/idc/groups/public/@otherif/documents/ifdocs/jsccdcoexemptorder10-26-15.pdf>; OTC Clear Order of Exemption from Registration (Dec. 21, 2015), available at <http://www.cftc.gov/idc/groups/public/@otherif/documents/ifdocs/otccleardcoexemptorder12-21-15.pdf>.

Proposed Regulation 39.6(a) would provide that the Commission may exempt, conditionally or unconditionally, a non-U.S. clearing organization from registration as a DCO for the clearing of swaps for certain U.S. persons,<sup>17</sup> and thereby exempt such clearing organization from compliance with the provisions of the CEA and Commission regulations applicable to DCOs, if the Commission determines that all of the eligibility requirements listed in proposed Regulation 39.6(a)(1) and (a)(2) are met, and the clearing organization satisfies the conditions set forth in Regulation 39.6(b).<sup>18</sup> Each of these requirements is described below.

Proposed Regulation 39.6(a)(1) would codify the statutory requirement that the Commission may only exempt a clearing organization from DCO registration for the clearing of swaps if the Commission determines that the clearing organization is subject to comparable, comprehensive supervision and regulation. Proposed Regulation 39.6(a)(1)(i) would require that, in order to be eligible for an exemption from DCO registration, a clearing organization must be organized in a jurisdiction in which a home country regulator applies to the clearing organization, on an ongoing basis, statutes, rules, regulations, policies, or a combination thereof that, taken together, are consistent with the

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<sup>17</sup> The Commission proposes to use the definition of “U.S. person” as set forth in the Commission’s Interpretive Guidance and Policy Statement Regarding Compliance With Certain Swap Regulations, 78 FR 45292, 45316–17 (July 26, 2013), as such definition may be amended or superseded by a definition of the term “U.S. person” that is adopted by the Commission and applicable to this proposed regulation.

<sup>18</sup> The eligibility requirements listed in proposed Regulation 39.6(a)(1) and (a)(2) and the conditions set forth in proposed Regulation 39.6(b) would be pre-conditions to the Commission’s issuance of any order exempting a clearing organization from the DCO registration requirements of the CEA and Commission regulations. Additional conditions that are unique to the facts and circumstances specific to a particular clearing organization could be imposed upon that clearing organization in the Commission’s order of exemption, as permitted by Section 5b(h) of the CEA.

PFMIs.<sup>19</sup> Under proposed Regulation 39.6(a)(1)(ii) and (iii), a clearing organization would be required to observe the PFMIs in all material respects and be in good regulatory standing in its home country. As previously noted, the Commission believes that operating within a regulatory framework consistent with the PFMIs would meet the CEA's requirement in Section 5b(h) that, in order to qualify for an exemption, a clearing organization must be subject to comparable, comprehensive supervision and regulation by the appropriate government authorities in its home country.<sup>20</sup>

Proposed Regulation 39.6(a)(2) would provide that, in order for a clearing organization to be eligible for an exemption from DCO registration, a memorandum of understanding (MOU) or similar arrangement satisfactory to the Commission must be in effect between the Commission and the clearing organization's home country regulator,<sup>21</sup> pursuant to which, among other things, the home country regulator agrees to provide to the Commission any information that the Commission deems necessary to evaluate the clearing organization's initial and continued eligibility for exemption or to review

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<sup>19</sup> The Commission notes that the regulatory framework of a particular jurisdiction may consist of one or multiple sources of authority. In particular, the inclusion of "policies" is intended to accommodate a jurisdiction in which a policy has the force of law, and a set of policies may, on its own, represent the jurisdiction's regulatory framework that is consistent with the PFMIs.

<sup>20</sup> In addition to the principles applicable to central counterparties and other FMIs, the PFMIs provide that central banks, market regulators, and other relevant authorities should observe five responsibilities. Consistent with this, the Commission expects that, in order to meet the standard of being subject to comparable, comprehensive supervision and regulation, a clearing organization's home country regulator will observe these responsibilities. In particular, Responsibility D Explanatory Note 4.4.1 provides that the home country regulator should adopt the PFMIs, and, "[w]hile the precise means through which the principles are applied may vary from jurisdiction to jurisdiction, all [CPMI] and IOSCO members are expected to apply the principles to the relevant FMIs in their jurisdictions to the fullest extent allowed by the legal framework in their jurisdiction." PFMIs, ¶ 4.4.1. Therefore, the Commission would not find a home country regulator's statement that it requires a clearing organization to observe the PFMIs to be sufficient to meet the above standard for exemption, if the home country regulator has not itself adopted a regulatory framework that is consistent with the PFMIs.

<sup>21</sup> In foreign jurisdictions where more than one regulator supervises and regulates a clearing organization, the Commission would expect to enter into an MOU or similar arrangement with more than one regulator.

compliance with any conditions of such exemption. The Commission has customarily entered into MOUs or similar arrangements in connection with the supervision of non-U.S. clearing organizations that are registered as DCOs. In the context of exempt DCOs, satisfactory MOUs or similar arrangements with the home country regulator would include provisions for information sharing and cooperation, as well as for notification upon the occurrence of certain events, but the Commission would not expect to conduct routine site visits to exempt DCOs.

## 2. Conditions of Exemption

Proposed Regulation 39.6(b) sets forth conditions to which an exempt DCO would be subject. These conditions are consistent with the conditions that the Commission has imposed on each of the clearing organizations to which it has previously issued orders of exemption.

Under proposed Regulation 39.6(b)(1)(i), a U.S. person that is a clearing member of an exempt DCO would be permitted to clear swaps for itself and those persons identified in the definition of “proprietary account” set forth in Regulation 1.3. This provision is intended to permit a U.S. clearing member to clear for affiliates (including a parent or subsidiary) that are either U.S. or non-U.S. persons. The Commission recognizes that in some foreign jurisdictions, affiliates are considered to be “customers” and their positions are held in customer accounts. Clearing for affiliates under these circumstances would be permissible even if the affiliate positions are not held in an account that is an analogue to a proprietary account under the Commission’s regulations.

Similarly, proposed Regulation 39.6(b)(1)(ii) would provide that a non-U.S. person that is a clearing member of an exempt DCO may clear swaps for any affiliated

U.S. person identified in the definition of “proprietary account” in Regulation 1.3. This complements the standard in paragraph (b)(1)(i) by clarifying that an exempt DCO may clear for affiliated entities when one or more of those entities is a U.S. person, even if the clearing member itself is not a U.S. person.

Proposed Regulation 39.6(b)(1)(iii) would provide that a futures commission merchant (FCM) may be a clearing member of an exempt DCO, or maintain an account with an affiliated broker that is a clearing member, for the purpose of clearing swaps for the FCM itself and those persons identified in the definition of “proprietary account” in Regulation 1.3. Again, this provision is intended to permit what would be considered clearing of “proprietary” positions under the Commission’s regulations, even if the positions would qualify as “customer” positions under the laws and regulations of an exempt DCO’s home country. This provision would clarify that an exempt DCO may clear positions for FCMs if the positions are not “customer” positions under the Commission’s regulations.

The effect of proposed Regulation 39.6(b)(1) is to prohibit the clearing of FCM customer positions at an exempt DCO. Section 4d(f)(1) of the CEA makes it unlawful for any person to accept money, securities, or property (i.e., funds) from a swaps customer to margin a swap cleared through a DCO unless the person is registered as an FCM.<sup>22</sup> Any swaps customer funds held by a DCO are also subject to the segregation requirements of Section 4d(f)(2) of the CEA, and in order for a swaps customer to receive protection under this regime, particularly in an insolvency context, its funds must be

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<sup>22</sup> 7 U.S.C 6d(f)(1). This provision establishes a customer protection regime for swaps customers that is broadly similar to the regime for futures customers and options on futures customers under Sections 4d(a) and (b) of the CEA. 7 U.S.C. 6d(a) and (b).

carried by an FCM and deposited with a registered DCO.<sup>23</sup> Absent that chain of registration, the swaps customer's funds may not be treated as customer property under the U.S. Bankruptcy Code<sup>24</sup> and the Commission's regulations. Because of this, it has been the Commission's policy to allow exempt DCOs to clear only proprietary positions of U.S. persons and FCMs. The proposed regulations would codify this approach.

Proposed Regulation 39.6(b)(2) would codify the "open access" requirements of Section 2(h)(1)(B) of the CEA with respect to swaps cleared by an exempt DCO to which one or more of the counterparties is a U.S. person.<sup>25</sup> Paragraph (b)(2)(i) would require an exempt DCO to maintain rules providing that all such swaps with the same terms and conditions (as defined by product specifications established under the exempt DCO's rules) submitted to the exempt DCO for clearing are economically equivalent and may be offset with each other, to the extent that offsetting is permitted by the exempt DCO's rules. Paragraph (b)(2)(ii) would require an exempt DCO to maintain rules providing for non-discriminatory clearing of such a swap executed either bilaterally or on or subject to the rules of an unaffiliated electronic matching platform or trade execution facility, e.g., a swap execution facility.

Proposed Regulation 39.6(b)(3) would provide that an exempt DCO must consent to jurisdiction in the United States and designate an agent in the United States, for notice or service of process, pleadings, or other documents issued by or on behalf of the

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<sup>23</sup> See Section 761(2) of the Bankruptcy Code, 11 U.S.C. 761(2) (defining a "clearing organization" as a derivatives clearing organization registered under the CEA), and Regulation 190.01(f), 17 CFR 190.01(f) (stating that for purposes of the part 190 bankruptcy rules, "clearing organization" has the same meaning as that set forth in Section 761(2) of the Bankruptcy Code).

<sup>24</sup> 11 U.S.C. 761-767.

<sup>25</sup> 7 U.S.C. 2(h)(1)(B).

Commission or the U.S. Department of Justice in connection with any actions or proceedings against, or any investigations relating to, the exempt DCO or any U.S. person or FCM that is a clearing member or that clears swaps through an affiliated clearing member. The name of the designated agent would be submitted as part of the clearing organization's application for exemption. If an exempt DCO appoints another agent to accept such notice or service of process, the exempt DCO would be required to promptly inform the Commission of this change. This is consistent with requirements currently imposed in the registration orders of DCOs that are organized outside of the United States as well as in each of the orders of exemption that the Commission has issued.

Proposed Regulation 39.6(b)(4) is a general provision that would require an exempt DCO to comply, and demonstrate compliance as requested by the Commission, with any condition of the exempt DCO's order of exemption.

Proposed Regulation 39.6(b)(5) would require an exempt DCO to make all documents, books, records, reports, and other information related to its operation as an exempt DCO (books and records) open to inspection and copying by any Commission representative, and to promptly make its books and records available and provide them directly to Commission representatives, upon the request of a Commission representative. This condition of exemption is consistent with Section 5b(h) of the CEA, which states that the Commission may exempt a DCO from registration with conditions that may include "requiring that the [DCO] be available for inspection by the Commission and

make available all information requested by the Commission.”<sup>26</sup> The Commission notes that it does not anticipate conducting routine site visits to exempt DCOs. However, the Commission may request an exempt DCO to provide books and records related to its operation as an exempt DCO in order for the Commission to ensure that, among other things, the exempt DCO continues to meet the eligibility requirements for an exemption as well as the conditions of its exemption.<sup>27</sup>

Proposed Regulation 39.6(b)(6) would require that the exempt DCO provide an annual certification that it continues to observe the PFMI in all material respects, within 60 days following the end of its fiscal year. Proposed Regulation 39.6(b)(7) would require that the Commission receive an annual written representation from a home country regulator that the exempt DCO is in good regulatory standing, within 60 days following the end of the exempt DCO’s fiscal year. These requirements would help the Commission to assess an exempt DCO’s continued eligibility for an exemption.

### 3. Reporting Requirements

Proposed Regulation 39.6(c) and (d) would require an exempt DCO to meet certain reporting requirements, which are consistent with the reporting requirements exempt DCOs currently meet.

#### a. General Reporting Requirements

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<sup>26</sup> See also Regulation 1.31, 17 CFR 1.31 (requiring, among other things, that books and records of DCOs and other registered entities be made available for inspection by Commission representatives).

<sup>27</sup> Although an MOU or similar arrangement would provide for information sharing whereby the home country regulator agrees to provide to the Commission any information that the Commission deems necessary to evaluate the clearing organization’s initial and continued eligibility for exemption or to review compliance with any conditions of such exemption, the Commission would retain the authority to access books and records directly from an exempt DCO.

Proposed Regulation 39.6(c)(1) sets forth general reporting requirements pursuant to which an exempt DCO must provide certain information directly to the Commission: (1) on a periodic basis (daily or quarterly); and (2) after the occurrence of a specified event, each in accordance with the submission requirements of Regulation 39.19(b).<sup>28</sup> Such information may be used by the Commission, among other things, for the purposes of the Commission evaluating the continued eligibility of the exempt DCO for exemption, reviewing the exempt DCO's compliance with any conditions of its exemption, or conducting oversight of U.S. persons and their affiliates, and the swaps that they clear through the exempt DCO.

Proposed Regulation 39.6(c)(2)(i) would require an exempt DCO to compile a report as of the end of each trading day, and submit it to the Commission by 10:00 a.m. U.S. Central time on the following business day, containing with respect to swaps: (A) initial margin requirements and initial margin on deposit for each U.S. person; and (B) daily variation margin, separately listing the mark-to-market amount collected from or paid to each U.S. person. However, if a clearing member margins on a portfolio basis its own positions and the positions of its affiliates, and either the clearing member or any of its affiliates is a U.S. person, the exempt DCO would be required to report initial margin requirements and initial margin on deposit for all such positions on a combined basis for each such clearing member and to separately list the mark-to-market amount collected from or paid to each such clearing member, on a combined basis. These requirements are

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<sup>28</sup> Regulation 39.19(b), 17 CFR 39.19(b), requires that a DCO submit reports electronically and in a format and manner specified by the Commission, defines the term "business day," and establishes the relevant time zone for any stated time, unless otherwise specified by the Commission. The Commission has specified that U.S. Central time will apply with respect to the daily reports that must be filed by exempt DCOs pursuant to proposed Regulation 39.6(c)(2)(i).

similar to certain reporting requirements in Regulation 39.19(c)(1) that apply to registered DCOs.<sup>29</sup> These reports would provide the Commission with information regarding the cash flows associated with U.S. persons clearing swaps through exempt DCOs in order to analyze the risks presented by such U.S. persons and to assess the extent to which U.S. business is being cleared by each exempt DCO.

Proposed Regulation 39.6(c)(2)(ii) would require an exempt DCO to compile a report as of the last day of each fiscal quarter, and submit the report to the Commission no later than 17 business days after the end of the fiscal quarter, containing: (A) the aggregate clearing volume of U.S. persons during the fiscal quarter, and (B) the average open interest of U.S. persons during the fiscal quarter. If a clearing member is a U.S. person, this data would include the transactions and positions of the clearing member and all affiliates for which the clearing member clears; if a clearing member is not a U.S. person, the data would only have to include the transactions and positions of affiliates that are U.S. persons. Paragraph (C) of proposed Regulation 39.6(c)(2)(ii) would require that an exempt DCO's quarterly report to the Commission contain a list of U.S. persons and FCMs<sup>30</sup> that are either clearing members or affiliates of any clearing member, with

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<sup>29</sup> Specifically, Regulation 39.19(c)(1) requires registered DCOs to submit daily reports to the Commission, by 10:00 a.m. on the following business day, which contain, among other things, initial margin requirements, initial margin on deposit, and daily variation margin for each clearing member. See Regulation 39.19(c)(1)(i)(A) and (c)(1)(i)(B), 17 CFR 39.19(c)(1)(i)(A) and (c)(1)(i)(B). These provisions require such information to be provided for each clearing member by house origin and by each customer origin. This distinction would not apply to an exempt DCO, which will only be permitted to clear transactions that the Commission would treat as "proprietary." See discussion of proprietary and customer clearing supra section II.C.2.

<sup>30</sup> Such FCMs may or may not be U.S. persons. The Commission is not proposing to require that exempt DCOs provide daily information regarding initial margin requirements, initial margin on deposit, and daily variation margin, or quarterly aggregate clearing volume or average open interest, with respect to swaps, for FCMs that are not U.S. persons (unless reporting would otherwise be required because such FCMs are affiliates of U.S. persons). However, the Commission has a supervisory interest in receiving information

respect to the clearing of swaps, as of the last day of the fiscal quarter. This information would enable the Commission, in conducting risk surveillance of U.S. persons and swaps markets more broadly, to better understand and evaluate the nature and extent of the cleared swaps activity of U.S. persons.

Paragraphs (c)(2)(iii) through (c)(2)(viii) of proposed Regulation 39.6 each would require an exempt DCO to provide information to the Commission upon the occurrence of certain specified events. Several of the proposed required notifications are intended to provide the Commission with information relevant to the exempt DCO's continued eligibility for an exemption or its compliance with the conditions of its exemption. Proposed Regulation 39.6(c)(2)(iii) would require an exempt DCO to provide prompt notice to the Commission regarding any change in its home country regulatory regime that is material to the exempt DCO's continuing observance of the PFMI's, any requirements set forth in proposed Regulation 39.6, or the order of exemption issued by the Commission. In this regard, the Commission requests comment on whether an exempt DCO should make the determination of whether a change to the home country regulatory regime constitutes a "material" change to the exempt DCO's continuing observance of the PFMI's, any requirements set forth in proposed Regulation 39.6, or the Commission's order of exemption. Alternatively, the Commission requests comment on whether the Commission should require an exempt DCO to provide prompt notice of any change in its home country regulatory regime thereby allowing the Commission to determine whether a change is "material" to the exempt DCO's continuing observance of the PFMI's, any requirements set forth in proposed Regulation 39.6, or the Commission's

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regarding which of its registered FCMs are clearing members or affiliates of clearing members, with respect to the clearing of swaps on an exempt DCO.

order of exemption. Proposed Regulation 39.6(c)(2)(iv) would require an exempt DCO to provide to the Commission, to the extent that it is available to the exempt DCO, any assessment of the exempt DCO's observance (or the home country regulator's observance) of any of the PFMIs by a home country regulator or other national authority, or an international financial institution or international organization.<sup>31</sup> Proposed Regulation 39.6(c)(2)(v) would require an exempt DCO to provide to the Commission, to the extent that it is available to the exempt DCO, any examination report, examination findings, or notification of the commencement of any enforcement or disciplinary action by a home country regulator. Proposed Regulation 39.6(c)(2)(vi) would require an exempt DCO to provide immediate notice to the Commission of any change with respect to its licensure, registration, or other authorization to act as a clearing organization in its home country.

Two of the event-specific required notifications would assist the Commission in its oversight of U.S. persons and FCMs clearing swaps. Proposed Regulation 39.6(c)(2)(vii) would require an exempt DCO to provide immediate notice to the Commission in the event of a default (as defined by the exempt DCO in its rules) by a U.S. person or FCM clearing swaps, including the name of the U.S. person or FCM, a list of the positions held by the U.S. person or FCM, and the amount of the U.S. person's or FCM's financial obligation. Proposed Regulation 39.6(c)(2)(viii) would require an exempt DCO to provide notice of any action that it has taken against a U.S. person or FCM, no later than two business days after the exempt DCO takes such action against a

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<sup>31</sup> Such an international organization may include the International Monetary Fund or World Bank. See PFMIs, ¶ 1.33.

U.S. person or FCM. In particular, these provisions would require such reporting with respect to a default of, or an action taken against, an FCM, which may or may not be a U.S. person, in furtherance of the Commission's supervisory responsibilities with respect to registered FCMs. Proposed paragraphs (c)(2)(vii) and (c)(2)(viii) of Regulation 39.6 are similar to paragraphs (c)(4)(vii) and (c)(4)(xi) of Regulation 39.19, which apply to registered DCOs, respectively.

#### b. Swap Data Reporting Requirements

Proposed Regulation 39.6(d) would require that if a clearing member clears through an exempt DCO a swap that has been reported to a registered swap data repository (SDR) pursuant to part 45 of the Commission's regulations, the exempt DCO must report to an SDR data regarding the two swaps resulting from the novation of the original swap that had been submitted to the exempt DCO for clearing. In addition, an exempt DCO would be required to report the termination of the original swap accepted for clearing by the exempt DCO to the SDR to which the original swap was reported. Further, in order to avoid duplicative reporting for such transactions, an exempt DCO would be required to have rules that prohibit the part 45 reporting of the two new swaps by the counterparties to the original swap.<sup>32</sup>

#### 4. Application Procedures

Proposed Regulation 39.6(e) would describe the relevant application procedures for a clearing organization that seeks to be exempt from DCO registration, which are consistent with the application procedures the Commission has been using to evaluate

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<sup>32</sup> While the Commission recognizes that the counterparties to the original swap would otherwise be required to report the two new swaps under part 45 of the Commission's regulations, because an exempt DCO would be required to implement rules to the contrary at the direction of the Commission, such counterparties would be expected to comply with the rules of the exempt DCO in this case.

petitions for exemption. Specifically, under proposed Regulation 39.6(e)(1), a clearing organization would be required to file an application for exemption with the Secretary of the Commission in the format and manner specified by the Commission. After reviewing the application, the Commission could: (1) grant the exemption without conditions; (2) grant the exemption with conditions; or (3) deny the application for exemption.<sup>33</sup> This provision mirrors language in Regulation 39.3(a)(1), which addresses the application procedures for registration as a DCO.

Proposed Regulation 39.6(e)(2) would require an applicant to submit a complete application, including all applicable information and documentation as detailed in proposed Regulation 39.6(e)(2) and discussed below. It would provide that the Commission will not commence processing an application unless the application is complete. Proposed Regulation 39.6(e)(2) would further provide that an applicant may file with its completed application additional information that may be necessary or helpful to the Commission in processing the application. This provision is similar to certain provisions of Regulation 39.3(a)(2), which sets forth requirements with respect to applications for registration as a DCO.

Under proposed Regulation 39.6(e)(2)(i), an applicant would be required to submit a cover letter providing general information identifying the applicant, its regulatory licenses or registrations, and relevant contact information. Proposed Regulation 39.6(e)(2)(ii)–(viii) would require an applicant for exemption to submit documents that would establish the applicant’s eligibility for exemption under proposed

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<sup>33</sup> As noted above, proposed Regulation 39.6(b) sets forth the pre-conditions that would apply to any exemption from registration as a DCO.

Regulation 39.6(a), and would contain representations that the applicant would comply with the conditions of exemption, the general reporting requirements, and the swap data reporting requirements set forth in proposed Regulation 39.6(b), (c), and (d), respectively, and the terms and conditions of its order of exemption as issued by the Commission.

Additionally, proposed Regulation 39.6(e)(2)(v) would require an applicant to submit to the Commission copies of its most recent disclosures necessary to observe the PFMI, including the financial market infrastructure (FMI) disclosure template set forth in Annex A to the Disclosure Framework and Assessment Methodology (Disclosure Framework) for the PFMI.<sup>34</sup> The FMI disclosure template requires a clearing organization to provide a general description of itself and the markets it serves, a description of its general organization, an overview of the relevant legal and regulatory framework, a description of how it processes a transaction, and a summary narrative detailing its approach to observing each of the PFMI. The Commission expects that the FMI disclosure template provided to the Commission would have been reviewed and updated within the previous two years.<sup>35</sup> The FMI disclosure template is generally required by home country regulators that enforce the PFMI and is necessary to achieve status as a qualified central counterparty (QCCP).<sup>36</sup>

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<sup>34</sup> See CPMI-IOSCO, Principles for financial market infrastructures: Disclosure framework and Assessment methodology (Dec. 2012), at 82 *et seq.*, available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD396.pdf>.

<sup>35</sup> PFMI Explanatory Note 3.23.7 provides that the Principle 23, Key Consideration 5 standard that responses to the Disclosure Framework should be completed “regularly” means that an FMI should review its responses “[a]t a minimum . . . every two years to ensure continued accuracy and usefulness.” PFMI, ¶ 3.23.7.

<sup>36</sup> A QCCP is defined as an entity that (i) is licensed to operate as a central counterparty (CCP) and is permitted by the appropriate regulator to operate as such, and (ii) is prudentially supervised in a jurisdiction where the relevant regulator has established and publicly indicated that it applies to the CCP, on an ongoing basis, domestic rules and regulations that are consistent with the PFMI. The failure of a CCP to achieve

Proposed Regulation 39.6(e)(3) would provide that, at any time during the Commission's review of an application for exemption from registration as a DCO, the Commission may request that the applicant submit supplemental information in order for the Commission to process the application, and would require that the applicant file such supplemental information in the format and manner specified by the Commission. A similar provision is contained in Regulation 39.3(a)(3), which applies to applications for DCO registration.

Proposed Regulation 39.6(e)(4) would state that an applicant for exemption from registration as a DCO must promptly amend its application if it discovers a material omission or error, or if there is a material change in the information provided to the Commission in the application or other information provided in connection with the application. This provision is virtually identical to Regulation 39.3(a)(4), which addresses amendments to applications for DCO registration.

Proposed Regulation 39.6(e)(5) would identify those sections of an application for exemption from registration that will be made public, including the cover letter required in proposed Regulation 39.6(e)(2)(i); documents demonstrating that the applicant is organized in a jurisdiction in which its home country regulator applies to the applicant statutes, rules, regulations, and/or policies that are consistent with the PFMI; disclosures necessary to observe the PFMI;<sup>37</sup> rules that meet the requirements of proposed

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QCCP status could result in significant costs to its bank customers due to certain financial incentives for banks, including their subsidiaries and affiliates, to clear financial derivatives through QCCPs. See Basel Committee on Banking Supervision, Capital Requirements for Bank Exposures to Central Counterparties (Apr. 10, 2014), available at <https://www.bis.org/publ/bcbs282.htm>.

<sup>37</sup> The Disclosure Framework contemplates that central counterparties will make public disclosures pursuant to the Disclosure Framework. See CPMI-IOSCO, Principles for financial market infrastructures:

Regulation 39.6(b)(2) and (d), as applicable; and any other part of the application not covered by a request for confidential treatment, subject to Regulation 145.9. This provision is similar to Regulation 39.3(a)(5), which identifies those portions of an application for registration as a DCO that are made public.

#### 5. Modification of an Exemption

Proposed Regulation 39.6(f) would provide that the Commission may modify the terms and conditions of an order of exemption, either at the request of the exempt DCO or on the Commission's own initiative, based on changes to or omissions in material facts or circumstances pursuant to which the order of exemption was issued, or for any reason in the Commission's discretion. This is a further expression of the Commission's discretionary authority under Section 5b(h) of the CEA to exempt a clearing organization from registration "conditionally or unconditionally," and it reflects the Commission's authority to act with flexibility in responding to changed circumstances affecting an exempt DCO.

#### 6. Termination of Exemption upon Request by an Exempt DCO

Proposed Regulation 39.6(g) would set forth the framework under which an exempt DCO may petition the Commission to terminate its exemption and the applicable procedures. Specifically, pursuant to proposed Regulation 39.6(g)(1), an exempt DCO may request that the Commission terminate its exemption if the exempt DCO: (i) no longer qualifies for an exemption as a result of changed circumstances; (ii) intends to cease clearing swaps for U.S. persons; or (iii) submits a completed Form DCO in order to become a registered DCO in conjunction with its petition. Proposed Regulation

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Disclosure framework and Assessment methodology (Dec. 2012), at 1, available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD396.pdf>.

39.6(g)(2) would provide that the petition for termination must include an explanation for the request and describe the exempt DCO's plans for liquidation or transfer of the positions and related collateral of U.S. persons, if applicable. Pursuant to proposed Regulation 39.6(g)(3), the Commission would issue an order of termination within a reasonable time appropriate to the circumstances or in conjunction with the issuance of an order of registration, if applicable.

#### D. Regulation 39.9 – Scope

The Commission is proposing to revise Regulation 39.9 to make it clear that the provisions of subpart B apply to any DCO, as defined under Section 1a(15) of the CEA and Regulation 1.3, that is registered with the Commission as a DCO pursuant to Section 5b of the CEA, but do not apply to any exempt DCO. This revision would clarify that the subpart B regulations that address compliance with the DCO Core Principles applicable to registered DCOs do not impose any obligations upon exempt DCOs.

### **III. Proposed Amendments to Part 140 – Delegations of Authority**

The proposed amendments to Regulation 140.94(c)(4) would delegate to the Director of DCR all functions reserved to the Commission under proposed Regulation 39.6 except for the following: (i) granting an exemption under paragraph (a); (ii) prescribing any conditions to an exemption under paragraph (b); (iii) modifying an exemption under paragraph (f); and (iv) terminating an exemption under paragraph (g)(3). Such delegation would expedite consideration of exemption requests by permitting DCR to more efficiently carry out tasks associated with the processing of an exemption application. Certain technical amendments have also been proposed to

Regulation 140.94 in order to adjust the paragraph numbering to accommodate the proposed amendments to Regulation 140.94(c)(4).

#### **IV. Request for Comments**

The Commission generally requests comments on all aspects of the proposed rules. Additionally, the Commission requests comments on the following specific issues:

- Exempt DCOs are permitted to clear only proprietary positions of U.S. persons and FCMs. The proposed regulations would codify this approach. Should the Commission consider permitting an exempt DCO to clear swaps for FCM customers?
- Should the Commission impose any additional conditions on an exempt DCO or modify any of the existing conditions?
- Should any of the conditions imposed on an exempt DCO lead to an automatic termination of the exemption if the condition is not met?

#### **V. Consideration of Costs and Benefits**

##### **A. Introduction**

Section 15(a) of the CEA requires the Commission to consider the costs and benefits of its actions before promulgating a regulation under the CEA or issuing certain orders.<sup>38</sup> 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

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<sup>38</sup> 7 U.S.C. 19(a).

public interest considerations. The Commission considers the costs and benefits resulting from its discretionary determinations with respect to the Section 15(a) factors.

## B. Proposed Regulation 39.6

### 1. Summary

Section 5b(a) of the CEA requires a clearing organization that clears swaps to be registered with the Commission as a DCO. Section 5b(h) of the CEA, however, permits the Commission to exempt a clearing organization from DCO registration for the clearing of swaps to the extent that the Commission determines that such clearing organization is subject to comparable, comprehensive supervision by appropriate government authorities in the clearing organization's home country. Pursuant to this authority, the Commission has exempted four non-U.S. clearing organizations from DCO registration to clear proprietary swap positions of U.S. persons and FCMs. The proposed regulation would codify the policies and procedures that the Commission is currently following with respect to granting exemptions from DCO registration. Accordingly, the baseline for this consideration of costs and benefits is the current status, where the Commission has implemented a set of conditions and procedures for granting exemptions from DCO registration, but has not codified those conditions and procedures under Commission regulations.

Specifically, the proposed regulation would set forth the process by which a non-U.S. clearing organization could obtain an exemption from DCO registration for the clearing of swaps provided that it meets the specified eligibility standards and can meet the conditions of an exemption. The eligibility standards require, among other things, that a clearing organization applying for exemption must be organized in a jurisdiction in

which a home country regulator applies to the clearing organization, on an ongoing basis, statutes, rules, regulations, policies, or a combination thereof that, taken together, are consistent with the PFMI, and the clearing organization must observe the PFMI in all material respects. The conditions of exemption describe, among other things, the circumstances in which an exempt DCO would be permitted to clear swaps for U.S. persons. An exempt DCO is and would be permitted to clear only “proprietary” positions as defined in Regulation 1.3, and it is not and would not be permitted to clear “customer” positions subject to Section 4d(f) of the CEA.

## 2. Benefits

Proposed Regulation 39.6 would provide several benefits. First, an exempt DCO may clear proprietary swap positions for U.S. persons without having to prepare and submit an application for DCO registration, which involves the submission of extensive documentation to the Commission. Similarly, an exempt DCO is not required to comply with Commission regulations applicable to registered DCOs, except as required under Regulation 39.6 or the exempt DCO’s order of exemption. Thus, the significantly reduced application and ongoing compliance requirements for exempt DCOs may encourage clearing organizations to seek an exemption from registration. This mitigation of registration-related requirements may also benefit market participants and the public more generally. That is, non-U.S. clearing organizations that are exempt from registration may incur lower compliance costs, which may, in turn, result in lower costs to their clearing members. In addition, U.S. persons (as clearing members or affiliates of clearing members) would likely have access to more clearing organizations in order to clear their proprietary swaps. Access to more clearing organizations may also encourage

voluntary clearing of swaps that are not required to be cleared, as certain swaps may not be cleared by any registered DCOs. This may, in turn, serve to diversify the potential risk of cleared swaps, because any such risk would become less concentrated if a larger number of registered and exempt DCOs were clearing swaps for U.S. persons, and the volume of those swaps could become more evenly distributed among those registered and exempt DCOs.

Finally, the proposed regulation may also promote competition among registered and exempt DCOs by encouraging more clearing organizations to seek an exemption, and it would permit exempt DCOs to clear the same types of swap transactions for the proprietary accounts of U.S. persons that may be cleared by registered DCOs.

The Commission requests comment on the potential benefits of proposed Regulation 39.6, including, where possible, quantitative data. More specifically, the Commission requests comment on the potential benefits to clearing organizations that are eligible to become exempt DCOs and thereby clear swaps for U.S. persons and their affiliates, and the potential benefits to other market participants or the financial system as a whole. The Commission further requests comment on any alternative proposals that might achieve the objectives of the proposed regulation, and the benefits associated with any such alternatives.

### 3. Costs

A clearing organization seeking an exemption incurs some costs in preparing an application for exemption. If a clearing organization were not able to seek an exemption, however, it would be required to register with the Commission and to submit a Form

DCO.<sup>39</sup> While the Form DCO and the FMI disclosure template set forth in Annex A to the Disclosure Framework require certain similar types of information to be provided to the Commission, the Form DCO would require the clearing organization to provide additional documentation that is not required pursuant to the Disclosure Framework. Moreover, a clearing organization is likely to have already prepared the FMI disclosure template in order to comply with the requirements of its home country regulator, which must be consistent with the PFMIIs, and to achieve QCCP status.<sup>40</sup> Therefore, the costs involved in applying for an exemption are less than the costs involved in applying for registration, and the proposed regulation would not change this. Based on the Commission's Paperwork Reduction Act estimates, the cost burden to submit Form DCO is approximately \$100,000 per entity,<sup>41</sup> while that for submitting an application for exemption is approximately \$10,500 per entity.<sup>42</sup> Thus, there is an estimated cost savings associated with submitting an application for exemption rather than Form DCO of approximately \$89,500 per entity, and the proposed regulation would codify the procedures for submitting an application for exemption. The Commission seeks comment about whether these cost estimates are reasonable.

Other potential administrative costs associated with maintaining an exemption from DCO registration are minimal. For example, an exempt DCO would be required to

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<sup>39</sup> For purposes of this analysis, it is assumed that any clearing organization that is not granted an exemption will be required to register as a DCO if it clears swaps for any U.S. person. This assumption, however, is not intended to be a legal conclusion that, with respect to the particular facts and circumstances of any particular clearing organization, the CEA would require registration with the Commission as a DCO.

<sup>40</sup> See supra section II.C.4 for more detail.

<sup>41</sup> See Derivatives Clearing Organization General Provisions and Core Principles, 76 FR 69334, 69410 (Nov. 8, 2011).

<sup>42</sup> See infra section VI.B for more detail.

make its books and records relating to its operation as an exempt DCO available for inspection by Commission staff upon request. This condition of exemption is consistent with Section 5b(h) of the CEA, which states that the Commission may exempt a DCO from registration with conditions that may include “requiring that the [DCO] be available for inspection by the Commission and make available all information requested by the Commission.” In addition, this requirement is imposed on registered DCOs; as a result, an exempt DCO would be held to this requirement even if it were to choose to register as a DCO. The Commission notes that there would be no costs imposed on an exempt DCO in connection with this condition unless and until the Commission requests to inspect its books and records. Furthermore, an exempt DCO’s home country regulator is and would be required to provide to the Commission an annual written representation that the exempt DCO is in good regulatory standing. The Commission believes that the costs associated with this requirement are minimal, as home country regulators typically provide a standard letter and are required to provide it only once a year.

Lastly, exempt DCOs would be held to certain reporting requirements, the costs of which are limited to providing them to the Commission on either a regular or event-specific basis. The Commission has previously considered the costs of regular and event-specific reporting requirements when adopting Regulation 39.19(c) for registered DCOs.<sup>43</sup> The reporting requirements for exempt DCOs are substantially less extensive than those specified in Regulation 39.19(c). The Commission believes the costs of the exempt DCO reporting requirements are not significant but welcomes comment on such costs, particularly from existing exempt DCOs.

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<sup>43</sup> Derivatives Clearing Organization General Provisions and Core Principles, 76 FR at 69426.

An exempt DCO may incur costs related to establishing and maintaining connections to an SDR in order to report the swap data that would be required by proposed Regulation 39.6(d). In connection with the analysis required by the Paperwork Reduction Act, the Commission has estimated an initial cost of \$85,478 per exempt DCO to establish an SDR connection, and an annual cost of \$93,750 to maintain this connection.

As discussed in section VI.B below, an exempt DCO would likely realize some administrative cost savings with respect to its ongoing compliance obligations with the Commission. The Commission acknowledges that it is difficult to differentiate the ongoing costs of complying with a home country's regulatory requirements from those of complying with the CEA and Commission regulations given that there may be costs common to both. Furthermore, the Commission lacks reliable data upon which to base many of these cost estimates, which it acknowledges could vary greatly among clearing organizations. Thus, the Commission seeks comment about such costs.

### C. Section 15(a) Factors

#### 1. Protection of Market Participants and the Public

The proposed amendments to Part 39 would protect market participants and the public by requiring, among other things, that an exempt DCO: (i) may only clear swaps for U.S. persons for their proprietary accounts, and not for "swaps customers" within the meaning of the CEA and Commission regulations; (ii) must be organized in a jurisdiction in which it is subject to supervision and regulation by a government authority that applies to the clearing organization statutes, rules, regulations, policies, or a combination thereof that, taken together, are consistent with the PFMI; (iii) must submit to the Commission

the FMI disclosure template set forth in Annex A to the Disclosure Framework required to observe the PFMI standards, and must provide information to the Commission, upon request, that the Commission deems necessary to evaluate its continued eligibility for exemption or to review its compliance with any conditions of exemption; and (iv) must be licensed, registered, or otherwise authorized to act as a clearing organization in its home country, and its home country regulator must not have made any findings of material non-observance of the PFMI standards or other relevant home country legal requirements that have not resulted in corrective action. Furthermore, the proposed amendments to Part 39 would provide additional market safeguards through requiring an MOU or other similar arrangement with the home country regulator that would enable the Commission to obtain any information that the Commission deems necessary to evaluate the initial and continued eligibility of the DCO for exemption from registration or to review its compliance with any conditions of such exemption.

These requirements would protect market participants and the public by ensuring that U.S. “swaps customers” would remain subject to the customer protection regime established in the CEA and Commission regulations, and that exempt DCOs would be subject to the internationally recognized PFMI standards.

## 2. Efficiency, Competitiveness, and Financial Integrity

Proposed Regulation 39.6 would promote efficiency in the design of an exempt DCO’s settlement and clearing arrangements, operating structure and procedures, scope of products cleared, and use of technology because it would permit an exempt DCO to clear proprietary transactions for U.S. persons through observance of the PFMI standards, subject to supervision and regulation by a home country regulator. Moreover, the use of a single

set of standards to determine eligibility, namely the internationally recognized PFMI, would promote operational efficiency because it would (i) permit a non-U.S. clearing organization to obtain an exemption from registration that would mitigate duplicative compliance requirements and (ii) facilitate uniformity in supervision and regulation of both registered and exempt DCOs.

Proposed Regulation 39.6 may also promote competition among registered and exempt DCOs because it would permit exempt DCOs to clear the same types of swap transactions for the proprietary accounts of U.S. persons that may be cleared by registered DCOs. Unlike their foreign counterparts, U.S.-based DCOs would still be required to register with the Commission in order to clear proprietary swap positions for U.S. persons and would not be eligible for an exemption under the proposed regulation (or under Section 5b(h) of the CEA). Potentially, this different treatment may create a competitive disadvantage for U.S.-based DCOs, which would be subject to the requirements of the CEA and Commission regulations. However, exempt DCOs would be subject to a foreign supervisory and regulatory framework that is consistent with the internationally recognized standards set forth in the PFMI.

Proposed Regulation 39.6 would be expected to maintain the financial integrity of clearing organizations that clear proprietary transactions for U.S. persons because exempt clearing organizations would be subject to supervision and regulation by a home country regulator within a legal framework that is consistent with the PFMI. Such supervision and regulation is comparable to that applicable to DCOs under the CEA and Commission regulations, and is sufficiently comprehensive. In addition, the proposed regulation may contribute to the financial integrity of the broader financial system by spreading the

potential risk of particular cleared swaps among a greater number of registered and exempt DCOs.

### 3. Price Discovery

Price discovery is the process by which prices for underlying instruments may be determined by, or inferred from, prices of derivative contracts. The Commission has not identified any impact that proposed Regulation 39.6 would have on price discovery.

### 4. Sound Risk Management Practices

Proposed Regulation 39.6 would contribute to the sound risk management practices of clearing organizations that provide clearing services to U.S. persons for their proprietary transactions because exempt DCOs would be subject to the risk management standards that are included in the PFMI. Although the risk management requirements of the CEA and the Commission regulations applicable to registered DCOs would not be binding upon exempt DCOs, the risk management standards in the PFMI are substantially similar.

### 5. Other Public Interest Considerations

The Commission notes the public interest in access to clearing organizations outside the United States in light of the international nature of many swap transactions. The proposed amendments to Part 39 would codify the exemption process for non-U.S. clearing organizations that would permit them to clear proprietary swap transactions for certain U.S. persons, when such clearing organizations meet the eligibility requirements and conditions of the proposed rule. Having a more open and transparent process for obtaining an exemption from registration may encourage more non-U.S. clearing

organizations to seek an exemption, providing greater harmonization of the U.S. and global financial markets.

## **VI. Related Matters**

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

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 and, if so, provide a regulatory flexibility analysis on the impact.<sup>44</sup> The regulations proposed by the Commission will affect only clearing organizations. The Commission 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.<sup>45</sup> The Commission has previously determined that clearing organizations are not small entities for the purpose of the RFA.<sup>46</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>47</sup> provides that Federal agencies, including the Commission, may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid control number from the Office of Management and Budget (OMB). This proposed rulemaking contains reporting

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<sup>44</sup> 5 U.S.C. 601 et seq.

<sup>45</sup> 47 FR 18618 (Apr. 30, 1982).

<sup>46</sup> See 66 FR 45604, 45609 (Aug. 29, 2001).

<sup>47</sup> 44 U.S.C. 3501 et seq.

requirements that are collections of information within the meaning of the PRA.

Although the Commission anticipates that fewer than ten persons will be subject to these requirements, which is below the “ten or more persons” threshold for PRA compliance, the PRA applies to “[a]ny recordkeeping, reporting, or disclosure requirement contained in a rule of general applicability.”<sup>48</sup> The Commission is proposing to revise Information Collection 3038-0076, which contains the requirements for applications for registration as a DCO, and Information Collection 3038-0096, which contains swap data reporting requirements, to include the collection of information in proposed Regulation 39.6. The responses to the collection of information would be necessary to obtain the requested exemption from DCO registration.

#### 1. Application for Exemption and Ongoing Reporting Obligations under Proposed Regulation 39.6

The number of potential respondents was estimated based on the number of non-U.S. clearing organizations that have already applied for, or been granted, an exemption from DCO registration by the Commission. Based on its experience in addressing petitions for exemption, the Commission anticipates receiving one or two applications for exemption per year. Burden hours and costs were estimated based on existing information collections for DCO registration and reporting, adjusted to reflect the significantly lower burden of the proposed regulations. The number of respondents for the daily and quarterly reporting and annual certification requirements is conservatively estimated at a maximum of seven, based on the number of existing exempt DCOs and the number of pending petitions. Reporting of specific events and termination of an

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<sup>48</sup> 5 CFR 1320.3(c)(4)(i).

exemption are expected to occur infrequently. The burden is estimated conservatively at two per year for event-specific reporting and at one per year for reporting of an exemption termination. The Commission has estimated the burden hours for this proposed collection of information as follows:

#### Application for exemption

Estimated number of respondents: 2

Estimated number of reports per respondent: 1

Average number of hours per report: 32

Estimated gross annual reporting burden: 64

#### Information requested by the Commission

Estimated number of respondents: 2

Estimated number of reports per respondent: 1

Average number of hours per report: 3

Estimated gross annual reporting burden: 6

#### Daily reporting

Estimated number of respondents: 7

Estimated number of reports per respondent: 250

Average number of hours per report: 0.1

Estimated gross annual reporting burden: 175

#### Quarterly reporting

Estimated number of respondents: 7

Estimated number of reports per respondent: 4

Average number of hours per report: 2

Estimated gross annual reporting burden: 56

#### Event-specific reporting

Estimated number of respondents: 2

Estimated number of reports per respondent: 1

Average number of hours per report: 0.5

Estimated gross annual reporting burden: 1

#### Annual certification

Estimated number of respondents: 7

Estimated number of reports per respondent: 1

Average number of hours per report: 1.5

Estimated gross annual reporting burden: 21

#### Termination of exemption by request of clearing organization

Estimated number of respondents: 1

Estimated number of reports per respondent: 1

Average number of hours per report: 2

Estimated gross annual reporting burden: 2

#### Notice to clearing members of termination of exemption

Estimated number of respondents: 1

Estimated number of reports per respondent: 22

Average number of hours per report: 0.1

Estimated gross annual reporting burden: 2.2

## 2. Reporting by Exempt DCOs in accordance with Part 45

Proposed Regulation 39.6(d) would require an exempt DCO to report data regarding the two swaps resulting from the novation of an original swap to a registered SDR, if the original swap had been reported to a registered SDR pursuant to part 45 of the Commission's regulations. The Commission is proposing to revise the information collection for part 45 to add exempt DCOs as an additional category of reporting entity. The burden for exempt DCOs reporting in accordance with part 45 is estimated to be approximately one-quarter of the burden for registered DCOs with respect to both non-recurring and recurring costs because exempt DCOs will not be required to report all swaps, only those that result from the novation of original swaps that have been reported to an SDR.<sup>49</sup> Consequently, the burden hours for the proposed collection of information in this rulemaking have been estimated as follows:

Reporting in accordance with part 45

Estimated number of respondents: 7

Estimated number of reports per respondent: 1987

Average number of hours per report: 0.1

Estimated gross annual reporting burden: 1393

### **List of Subjects**

#### 17 CFR Part 39

Commodity futures, Exemption, Risk management, Settlement procedures, Default rules and procedures, System safeguards.

#### 17 CFR Part 140

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<sup>49</sup> Details of the estimated burden related to non-recurring and recurring costs under Part 45 are discussed in the Part 45 adopting release. See Swap Data Recordkeeping and Reporting Requirements, 77 FR at 2171-2176.

Authority delegations (Government agencies), Organization and functions (Government agencies).

For the reasons stated in the preamble, the Commission proposes to amend 17 CFR parts 39 and 140 as follows:

**PART 39 – DERIVATIVES CLEARING ORGANIZATIONS**

1. The authority citation for part 39 continues to read as follows:

**Authority:** 7 U.S.C. 2, 7a–1, and 12a; 12 U.S.C. 5464; 15 U.S.C. 8325.

2. Revise § 39.1 to read as follows:

**§ 39.1 Scope.**

The provisions of this subpart A apply to any derivatives clearing organization, as defined under section 1a(15) of the Act and § 1.3 of this chapter, that is registered or is required to register with the Commission as a derivatives clearing organization pursuant to section 5b(a) of the Act, or that is applying for an exemption from registration pursuant to section 5b(h) of the Act.

3. Revise § 39.2 to add the following definitions:

**§ 39.2 Definitions.**

\* \* \* \* \*

Exempt derivatives clearing organization means a derivatives clearing organization that the Commission has exempted from registration under section 5b(a) of the Act, pursuant to section 5b(h) of the Act and § 39.6 of this part.

Good regulatory standing means, with respect to a derivatives clearing organization that is organized outside of the United States, and is licensed, registered, or otherwise authorized to act as a clearing organization in its home country, that either (a) there has

been no finding by the home country regulator of material non-observance of the Principles for Financial Market Infrastructures or other relevant home country legal requirements, or (b) there has been a finding by the home country regulator of material non-observance of the Principles for Financial Market Infrastructures or other relevant home country legal requirements but any such finding has been or is being resolved to the satisfaction of the home country regulator by means of corrective action taken by the derivatives clearing organization.

Home country means, with respect to a derivatives clearing organization that is organized outside of the United States, the jurisdiction in which the derivatives clearing organization is organized.

Home country regulator means, with respect to a derivatives clearing organization that is organized outside of the United States, an appropriate government authority which licenses, regulates, supervises, or oversees the derivatives clearing organization's clearing activities in the home country.

\* \* \* \* \*

Principles for Financial Market Infrastructures means the Principles for Financial Market Infrastructures jointly published by the Committee on Payments and Market Infrastructures and the Technical Committee of the International Organization of Securities Commissions in April 2012, as updated, revised, or otherwise amended.

\* \* \* \* \*

4. Add § 39.6 to read as follows:

**§ 39.6 Exemption from derivatives clearing organization registration.**

(a) Eligibility for exemption. The Commission may exempt, conditionally or unconditionally, a derivatives clearing organization that is organized outside of the United States, from registration as a derivatives clearing organization for the clearing of swaps for U.S. persons, and thereby exempt such derivatives clearing organization from compliance with provisions of the Act and Commission regulations applicable to derivatives clearing organizations, if:

(1) The derivatives clearing organization is subject to comparable, comprehensive supervision and regulation by a home country regulator as demonstrated by the following:

(i) The derivatives clearing organization is organized in a jurisdiction in which a home country regulator applies to the derivatives clearing organization, on an ongoing basis, statutes, rules, regulations, policies, or a combination thereof that, taken together, are consistent with the Principles for Financial Market Infrastructures;

(ii) The derivatives clearing organization observes the Principles for Financial Market Infrastructures in all material respects; and

(iii) The derivatives clearing organization is in good regulatory standing in its home country; and

(2) A memorandum of understanding or similar arrangement satisfactory to the Commission is in effect between the Commission and the derivatives clearing organization's home country regulator, pursuant to which, among other things, the home country regulator agrees to provide to the Commission any information that the Commission deems necessary to evaluate the initial and continued eligibility of the

derivatives clearing organization for exemption from registration or to review its compliance with any conditions of such exemption.

(b) Conditions of exemption. An exemption from registration as a derivatives clearing organization shall be subject to any conditions the Commission may prescribe including, but not limited to:

(1) Clearing by or for U.S. persons and futures commission merchants. The exempt derivatives clearing organization shall maintain rules that limit swaps clearing services for U.S. persons and futures commission merchants to the following circumstances:

(i) A U.S. person that is a clearing member of the exempt derivatives clearing organization may clear swaps for itself and those persons identified in the definition of “proprietary account” set forth in § 1.3 of this chapter;

(ii) A non-U.S. person that is a clearing member of the exempt derivatives clearing organization may clear swaps for any affiliated U.S. person identified in the definition of “proprietary account” set forth in § 1.3 of this chapter; and

(iii) An entity that is registered with the Commission as a futures commission merchant may be a clearing member of the exempt derivatives clearing organization, or otherwise maintain an account with an affiliated broker that is a clearing member, for the purpose of clearing swaps for itself and those persons identified in the definition of “proprietary account” set forth in § 1.3 of this chapter.

(2) Open access. The exempt derivatives clearing organization shall maintain rules with respect to swaps to which one or more of the counterparties is a U.S. person. Such rules shall:

(i) Provide that all swaps with the same terms and conditions, as defined by product specifications established under the exempt derivatives clearing organization's rules, submitted to the exempt derivatives clearing organization for clearing are economically equivalent within the exempt derivatives clearing organization and may be offset with each other within the exempt derivatives clearing organization, to the extent offsetting is permitted by the exempt derivatives clearing organization's rules; and

(ii) Provide that there shall be non-discriminatory clearing of a swap executed bilaterally or on or subject to the rules of an unaffiliated electronic matching platform or trade execution facility.

(3) Consent to jurisdiction; designation of agent for service of process. The exempt derivatives clearing organization shall:

(i) Consent to jurisdiction in the United States;

(ii) Designate, authorize, and identify to the Commission, an agent in the United States who shall accept any notice or service of process, pleadings, or other documents, including any summons, complaint, order, subpoena, request for information, or any other written or electronic documentation or correspondence issued by or on behalf of the Commission or the United States Department of Justice to the exempt derivatives clearing organization, in connection with any actions or proceedings brought against, or investigations relating to, the exempt derivatives clearing organization or any U.S. person or futures commission merchant that is a clearing member, or that clears swaps through an affiliated clearing member, of the exempt derivatives clearing organization; and

(iii) Promptly inform the Commission of any change in its designated and authorized agent.

(4) Compliance. The exempt derivatives clearing organization shall comply, and shall demonstrate compliance as requested by the Commission, with any condition of its exemption.

(5) Inspection of books and records. The exempt derivatives clearing organization shall make all documents, books, records, reports, and other information related to its operation as an exempt derivatives clearing organization open to inspection and copying by any representative of the Commission; and in response to a request by any representative of the Commission, the exempt derivatives clearing organization shall, promptly and in the form specified, make the requested books and records available and provide them directly to Commission representatives.

(6) Observance of the Principles for Financial Market Infrastructures. On an annual basis, within 60 days following the end of its fiscal year, the exempt derivatives clearing organization shall provide to the Commission a certification that it continues to observe the Principles for Financial Market Infrastructures in all material respects.

(7) Representation of good regulatory standing. On an annual basis, within 60 days following the end of its fiscal year, the Commission shall receive from a home country regulator, at the request of the exempt derivatives clearing organization, a written representation that the exempt derivatives clearing organization is in good regulatory standing.

(c) General reporting requirements. (1) An exempt derivatives clearing organization shall provide to the Commission the information specified in this paragraph and any other information that the Commission deems necessary, including, but not limited to, information for the purpose of the Commission evaluating the continued eligibility of the

exempt derivatives clearing organization for exemption from registration, reviewing compliance by the exempt derivatives clearing organization with any conditions of the exemption, or conducting oversight of U.S. persons and their affiliates, and the swaps that are cleared by such persons through the exempt derivatives clearing organization. Information provided to the Commission under this paragraph shall be submitted in accordance with § 39.19(b) of this part.

(2) Each exempt derivatives clearing organization shall provide to the Commission the following information:

(i) A report compiled as of the end of each trading day and submitted to the Commission by 10:00 a.m. U.S. Central time on the following business day, containing:

(A) Initial margin requirements and initial margin on deposit for each U.S. person, with respect to swaps; provided, however, if a clearing member margins on a portfolio basis its own positions and the positions of its affiliates, and either the clearing member or any of its affiliates is a U.S. person, the exempt derivatives clearing organization shall report initial margin requirements and initial margin on deposit for all such positions on a combined basis for each such clearing member; and

(B) Daily variation margin, separately listing the mark-to-market amount collected from or paid to each U.S. person, with respect to swaps; provided, however, if a clearing member margins on a portfolio basis its own positions and the positions of its affiliates, and either the clearing member or any of its affiliates is a U.S. person, the exempt derivatives clearing organization shall separately list the mark-to-market amount collected from or paid to each such clearing member, on a combined basis.

(ii) A report compiled as of the last day of each fiscal quarter of the exempt derivatives clearing organization and submitted to the Commission no later than 17 business days after the end of the exempt derivatives clearing organization's fiscal quarter, containing the following information:

(A) The aggregate clearing volume of U.S. persons during the fiscal quarter, with respect to swaps. If a clearing member is a U.S. person, the volume figure shall include the transactions of the clearing member and all affiliates. If a clearing member is not a U.S. person, the volume figure shall include only transactions of affiliates that are U.S. persons.

(B) The average open interest of U.S. persons during the fiscal quarter, with respect to swaps. If a clearing member is a U.S. person, the open interest figure shall include the positions of the clearing member and all affiliates. If a clearing member is not a U.S. person, the open interest figure shall include only positions of affiliates that are U.S. persons.

(C) A list of U.S. persons and futures commission merchants that are either clearing members or affiliates of any clearing member, with respect to the clearing of swaps, as of the last day of the fiscal quarter.

(iii) Prompt notice regarding any change in the home country regulatory regime that is material to the exempt derivatives clearing organization's continuing observance of the Principles for Financial Market Infrastructures or with any of the requirements set forth in this section or in the order of exemption issued by the Commission;

(iv) As available to the exempt derivatives clearing organization, any assessment of the exempt derivatives clearing organization's or the home country regulator's

observance of the Principles for Financial Market Infrastructures, or any portion thereof, by a home country regulator or other national authority, or an international financial institution or international organization;

(v) As available to the exempt derivatives clearing organization, any examination report, examination findings, or notification of the commencement of any enforcement or disciplinary action by a home country regulator;

(vi) Immediate notice of any change with respect to the exempt derivatives clearing organization's licensure, registration, or other authorization to act as a derivatives clearing organization in its home country;

(vii) In the event of a default by a U.S. person or futures commission merchant clearing swaps, with such event of default determined in accordance with the rules of the exempt derivatives clearing organization, immediate notice of the default including the name of the U.S. person or futures commission merchant, a list of the positions held by the U.S. person or futures commission merchant, and the amount of the U.S. person's or futures commission merchant's financial obligation; and

(viii) Notice of action taken against a U.S. person or futures commission merchant by an exempt derivatives clearing organization, no later than two business days after the exempt derivatives clearing organization takes such action against a U.S. person or futures commission merchant.

(d) Swap data reporting requirements. If a clearing member clears through an exempt derivatives clearing organization a swap that has been reported to a registered swap data repository pursuant to part 45 of this chapter, the exempt derivatives clearing organization shall report to a registered swap data repository data regarding the two

swaps resulting from the novation of the original swap that had been submitted to the exempt derivatives clearing organization for clearing. The exempt derivatives clearing organization shall also report the termination of the original swap accepted for clearing by the exempt derivatives clearing organization, to the swap data repository to which the original swap was reported. In order to avoid duplicative reporting for such transactions, the exempt derivatives clearing organization shall have rules that prohibit the part 45 reporting of the two new swaps by the original counterparties to the original swap.

(e) Application procedures. (1) An entity seeking to be exempt from registration as a derivatives clearing organization shall file an application for exemption with the Secretary of the Commission in the format and manner specified by the Commission. The Commission will review the application for exemption and may approve or deny the application or, if deemed appropriate, exempt the applicant from registration as a derivatives clearing organization subject to conditions in addition to those set forth in paragraph (b) of this section.

(2) Application. An applicant for exemption from registration as a derivatives clearing organization shall submit to the Commission the information and documentation described in this section. Such information and documentation shall be clearly labeled as outlined in this section. The Commission will not commence processing an application unless the applicant has filed a complete application. Upon its own initiative, an applicant may file with its completed application for exemption additional information that may be necessary or helpful to the Commission in processing the application. The application shall include:

(i) A cover letter containing the following information:

- (A) Exact name of applicant as specified in its charter, and the name under which business will be conducted (including acronyms);
  - (B) Address of applicant's principal office;
  - (C) List of principal office(s) and address(es) where clearing activities are/will be conducted;
  - (D) A list of all regulatory licenses or registrations of the applicant (or exemptions from any licensing requirement) and the regulator granting such license or registration;
  - (E) Date of the applicant's fiscal year end;
  - (F) Contact information for the person or persons to whom the Commission should address questions and correspondence regarding the application; and
  - (G) A signature and date by a duly authorized representative of the applicant.
- (ii) A description of the applicant's business plan for providing clearing services as an exempt derivatives clearing organization, including information as to the classes of swaps that will be cleared and whether the swaps are subject to a clearing requirement issued by the Commission or the applicant's home country regulator;
  - (iii) Documents that demonstrate that applicant is organized in a jurisdiction in which its home country regulator applies to the applicant, on an ongoing basis, statutes, rules, regulations, policies, or a combination thereof that, taken together, are consistent with the Principles for Financial Market Infrastructures;
  - (iv) A written representation from the applicant's home country regulator that the applicant is in good regulatory standing;
  - (v) Copies of the applicant's most recent disclosures that are necessary to observe the Principles for Financial Market Infrastructures, including the financial market

infrastructure disclosure template set forth in Annex A to the Disclosure Framework and Assessment Methodology for the Principles for Financial Market Infrastructures, any other such disclosure framework issued under the authority of the International Organization of Securities Commissions that is required for observance of the Principles for Financial Market Infrastructures, and the URL to the specific page(s) on the applicant's website where such disclosures may be found;

(vi) A representation that the applicant will comply with each of the requirements and conditions of exemption set forth in paragraphs (b), (c), and (d) of this section, and the terms and conditions of its order of exemption as issued by the Commission;

(vii) A copy of the applicant's rules that meet the requirements of paragraphs (b)(2) and (d) of this section, as applicable; and

(viii) The applicant's consent to jurisdiction in the United States, and the name and address of the applicant's designated agent in the United States, pursuant to paragraph (b)(3) of this section.

(3) Submission of supplemental information. At any time during its review of the application for exemption from registration as a derivatives clearing organization, the Commission may request that the applicant submit supplemental information in order for the Commission to process the application, and the applicant shall file such supplemental information in the format and manner specified by the Commission.

(4) Amendments to pending application. An applicant for exemption from registration as a derivatives clearing organization shall promptly amend its application if it discovers a material omission or error, or if there is a material change in the

information provided to the Commission in the application or other information provided in connection with the application.

(5) Public information. The following sections of an application for exemption from registration as a derivatives clearing organization will be public: the cover letter set forth in paragraph (e)(2)(i) of this section; the documentation required in paragraphs (e)(2)(iii) and (e)(2)(v) of this section; rules that meet the requirements of paragraphs (b)(2) and (d) of this section, as applicable; and any other part of the application not covered by a request for confidential treatment, subject to § 145.9 of this chapter.

(f) Modification of an exemption. The Commission may, either at the request of the exempt derivatives clearing organization or on its own initiative, modify the terms and conditions of an order of exemption, based on changes to or omissions in material facts or circumstances pursuant to which the order of exemption was issued, or for any reason in its discretion.

(g) Termination of exemption upon request by an exempt derivatives clearing organization. (1) An exempt derivatives clearing organization may petition the Commission to terminate its exemption if:

(i) Changed circumstances result in the exempt derivatives clearing organization no longer qualifying for an exemption;

(ii) The exempt derivatives clearing organization intends to cease clearing swaps for U.S. persons; or

(iii) In conjunction with the petition, the exempt derivatives clearing organization submits a completed Form DCO to become a registered derivatives clearing organization pursuant to section 5b(a) of the Act.

(2) The petition for termination of exemption shall include a detailed explanation of the facts and circumstances supporting the request and the exempt derivatives clearing organization's plans for, as may be applicable, the liquidation or transfer of the swaps positions and related collateral of U.S. persons.

(3) The Commission shall issue an order of termination within a reasonable time appropriate to the circumstances or, as applicable, in conjunction with the issuance of an order of registration.

(h) Notice to clearing members of termination of exemption. Following the Commission's issuance of an order of termination (unless issued in conjunction with the issuance of an order of registration), the exempt derivatives clearing organization shall provide immediate notice of such termination to its clearing members. Such notice shall include:

(1) A copy of the Commission's order of termination;

(2) A description of the procedures for orderly disposition of any open swaps positions that were cleared for U.S. persons; and

(3) An instruction to clearing members, requiring that they provide the exempt derivatives clearing organization's notice of such termination to all U.S. persons clearing swaps through such clearing members.

5. Revise § 39.9 to read as follows:

**§ 39.9 Scope.**

The provisions of this subpart B apply to any derivatives clearing organization, as defined under section 1a(15) of the Act and § 1.3 of this chapter, that is registered with the Commission as a derivatives clearing organization pursuant to section 5b of the Act.

The provisions of this subpart B do not apply to any exempt derivatives clearing organization, as defined under § 39.2 of this part.

**PART 140 – ORGANIZATION, FUNCTIONS, AND PROCEDURES OF THE COMMISSION**

6. The authority citation for part 140 continues to read as follows:

**Authority:** 7 U.S.C. 2(a)(12), 12a, 13(c), 13(d), 13(e), and 16(b).

7. Amend § 140.94 to redesignate paragraphs (c)(4) through (c)(13) as paragraphs (c)(5) through (c)(14) and add new paragraph (c)(4) to read as follows:

**§ 140.94 Delegation of authority to the Director of the Division of Swap Dealer and Intermediary Oversight and the Director of the Division of Clearing and Risk.**

\* \* \* \* \*

(c) The Commission hereby delegates, until such time as the Commission orders otherwise, the following functions to the Director of the Division of Clearing and Risk and to such members of the Commission’s staff acting under his or her direction as he or she may designate from time to time:

\* \* \*

(4) All functions reserved to the Commission in § 39.6 of this chapter, except for the authority to:

- (i) Grant an exemption under paragraph (a);
- (ii) Prescribe conditions to an exemption under paragraph (b);
- (iii) Modify an exemption under paragraph (f); and
- (iv) Terminate an exemption under paragraph (g)(3).

(5) All functions reserved to the Commission in § 39.10(c)(4)(iv) of this chapter;

(6) All functions reserved to the Commission in § 39.11(b)(1)(vi), (b)(2)(ii), (c)(1), (c)(2), (f)(1), and (f)(4) of this chapter;

(7) All functions reserved to the Commission in § 39.12(a)(5)(i)(B) of this chapter;

(8) All functions reserved to the Commission in § 39.13(g)(8)(ii), (h)(1)(i)(C), (h)(1)(ii), (h)(3)(i), (h)(3)(ii), and (h)(5)(i)(A) of this chapter;

(9) The authority to request additional information in support of a rule submission under § 39.15(b)(2)(iii)(A) of this chapter and in support of a petition pursuant to section 4d of the Act under § 39.15(b)(2)(iii)(B) of this chapter;

(10) All functions reserved to the Commission in § 39.19(c)(3)(iv), (c)(5)(i), (c)(5)(ii), and (c)(5)(iii) of this chapter;

(11) All functions reserved to the Commission in § 39.20(a)(5) of this chapter;

(12) All functions reserved to the Commission in § 39.21(d) of this chapter;

(13) All functions reserved to the Commission in § 39.31 of this chapter; and

(14) The authority to approve the requests described in §§ 39.34(d) and 39.39(f) of this chapter.

\* \* \* \* \*

Issued in Washington, DC, on August 8, 2018, by the Commission.

Christopher Kirkpatrick,

*Secretary of the Commission.*

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

**Appendices to Exemption from Derivatives Clearing Organization Registration –  
Commission Voting Summary and Chairman’s Statement**

## **Appendix 1 – Commission Voting Summary**

On this matter, Chairman Giancarlo and Commissioners Quintenz and Behnam voted in the affirmative. No Commissioner voted in the negative.

## **Appendix 2 – Statement of Chairman J. Christopher Giancarlo**

This proposal is part of Project KISS’s simple and straightforward efforts to make what has been an internal process public and transparent. Under the Commodity Exchange Act (CEA), the Commission may conditionally or unconditionally exempt a derivatives clearing organization (DCO) from registration for the clearing of swaps if the Commission determines that the clearing organization is subject to “comparable, comprehensive supervision and regulation” by appropriate government authorities in the clearing organization’s home country. Pursuant to this authority, the Commission has exempted four non-U.S. clearing organizations from DCO registration.

The Commission is proposing to adopt regulations that would codify the policies and procedures that the Commission is currently following with respect to granting exemptions from DCO registration. The proposed regulations are consistent with the policies and procedures that the Commission is currently following, and with the terms and conditions that the Commission has imposed on each of the clearing organizations to which it has previously issued orders of exemption.

The exempt DCO process applies a comparable, outcomes-based approach to reflect the Commission’s recognition that a foreign jurisdiction may have different regulations for its central counterparties (CCP) but share the same regulatory goals. Under the proposal, for CCPs in foreign jurisdictions, a framework that conforms to the Committee on Payments and Market Infrastructures (CPMI) and the International

Organization of Securities Commissions (IOSCO) Principles for Financial Market Infrastructures (PFMI) would be deemed comparable to the CFTC's requirements for domestic CCPs.

The proposal is part of the Commission's continued efforts to foster cross-border cooperation and show deference to home country regulation that is deemed comparable to the Commission's regulations. As our regulatory counterparts continue to implement swaps reforms in their markets, it is critical that the Commission endeavor to ensure that its rules do not unnecessarily conflict and fragment the global marketplace. For this reason, the Commission should operate on the basis of comity, not uniformity, with non-U.S. regulators. This avoids the untenable state of overlapping and duplicative regulations. The current proposal reflects this vision.

I support this proposed rule from the Division of Clearing and Risk (DCR). I look forward to hearing comments on the proposal.