



## U.S. COMMODITY FUTURES TRADING COMMISSION

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Division of Clearing and Risk

CFTC Letter No. 18-18  
No-Action  
July 31, 2018  
Division of Clearing and Risk

Mr. Karl Chen  
Chief Financial Officer  
Shanghai Clearing House  
No. 2 East Beijing Road  
Huangpu District  
Shanghai, People's Republic of China

Re: Extension of No-Action Relief with Regard to Section 5b(a) of the Commodity Exchange Act and Commission Regulations Thereunder

Dear Mr. Chen:

By letter dated May 31, 2016 (CFTC Letter No. 16-56), the Division of Clearing and Risk (“Division”) of the Commodity Futures Trading Commission (“Commission”) first provided relief to Shanghai Clearing House (“SHCH”), stating that the Division would not recommend that the Commission take enforcement action against SHCH for failure to register as a derivatives clearing organization (“DCO”) pursuant to the requirements of Section 5b(a) of the Commodity Exchange Act (the “CEA”) and Commission regulations thereunder, subject to certain conditions described in the letter. The relief subsequently was extended several times for periods of up to one year each.<sup>1</sup> The Division is hereby extending the relief for three years, for the reasons discussed below.

Under the terms of the letter, SHCH is permitted to clear certain swaps subject to mandatory clearing in the People's Republic of China for the proprietary trades<sup>2</sup> of SHCH clearing members that are U.S. persons or affiliates of U.S. persons. The letter was provided to SHCH while the Division reviews SHCH's petition<sup>3</sup> to the Commission for an exemption from registration as a DCO pursuant to Section 5b(h) of the CEA.

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<sup>1</sup> CFTC Letter No. 16-56 granted relief until May 31, 2017. The relief was extended until November 30, 2017, by CFTC Letter No. 17-26 (May 16, 2017), until February 28, 2018, by CFTC Letter No. 17-62 (November 20, 2017), and until February 28, 2019, by CFTC Letter No. 18-04 (February 22, 2018).

<sup>2</sup> See 17 C.F.R. § 1.3(y) (definition of “proprietary account”).

<sup>3</sup> Petition received November 22, 2016.

Before the Commission grants an exemption from DCO registration, it must first execute a Memorandum of Understanding (“MOU”) on cooperation and the exchange of information with the clearing organization’s home country regulator. Discussions with SHCH’s regulator, the People’s Bank of China (“PBOC”), regarding a potential MOU remain ongoing.

The Division believes that legitimate business interests are facilitated by permitting, on a temporary basis and subject to certain conditions, U.S. persons to clear swaps through SHCH. Because SHCH is the only clearinghouse that clears onshore Chinese renminbi-denominated interest rate swaps<sup>4</sup> and because PBOC requires several such products to be cleared, those wishing to transact in such products must clear them through SHCH.

Although the existing no-action relief permits U.S. persons to clear their proprietary swap trades through SHCH, SHCH does not currently have any U.S. clearing members. The Division understands that, given the amount of time needed to become a clearing member and the tenor of most interest rate swaps, the one-year limitation of the current relief makes it difficult for such financial institutions to pursue clearing membership due to concerns that they will be forced to terminate such membership and unwind any trades should the no-action relief not be further extended before a final decision can be made on SHCH’s DCO exemption petition.

To permit time for continued discussions between the CFTC and the PBOC on the MOU while providing sufficient regulatory certainty to permit U.S. persons to pursue clearing membership and to clear products such as Chinese renminbi-denominated interest rate swaps through SHCH, the Division is extending the relief initially provided in CFTC Letter No. 16-56 to July 31, 2021.

#### Extension of No-Action Relief

Based on the facts presented and the representations SHCH has made, the Division will not recommend that the Commission take enforcement action against SHCH for failure to register as a DCO pursuant to the requirements of Section 5b(a) of the CEA, subject to:

- (1) the conditions specified in CFTC Letter No. 16-56, and
- (2) the condition that SHCH shall submit to the Commission 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
  - (i) 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, SHCH must report initial

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<sup>4</sup> Other clearinghouses clear certain products related to “offshore Chinese renminbi.” Offshore Chinese renminbi, denoted by the currency code “CNH,” refers to certain Chinese currency traded outside the People’s Republic of China. Its value may differ from that of so-called “onshore Chinese renminbi,” denoted by the currency code “CNY,” which refers to Chinese currency traded within the People’s Republic of China.

margin requirements and initial margin on deposit for all such positions on a combined basis for each such clearing member; and

(ii) 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, SHCH must separately list the mark-to-market amount collected from or paid to each such clearing member, on a combined basis.

The Division is adding the above daily reporting condition because the Division anticipates that one or more U.S. persons may seek to become clearing members of SHCH in the near future. SHCH has represented to the Division that it is ready to comply with this condition, which will help demonstrate the effect, if any, of relevant law(s) (such as the Law of the People's Republic of China on Protection of State Secrets and Law of the People's Republic of China on Cybersecurity) on SHCH's ability to comply in a timely manner with the reporting requirements to which it would be subject should the Commission grant its petition for exemption from registration as a DCO.

The no-action relief shall expire at the earlier of: (i) July 31, 2021, or (ii) the date on which the Commission exempts SHCH from registration as a DCO under Section 5b(h) of the CEA.

The relief granted herein supersedes that granted in CFTC Letter No. 18-04 (February 22, 2018).

The position taken herein concerns enforcement action only and does not represent a legal conclusion with respect to the applicability of any provision of the CEA or the Commission's regulations. In addition, the Division's position does not necessarily reflect the views of the Commission or any other division or office of the Commission. Because this position is based on the representations contained in SHCH's original request letter, any different, changed, or omitted material facts or circumstances may require a different conclusion or render this letter void. Finally, as with all no-action letters, the Division retains the authority to condition further, modify, suspend, terminate, or otherwise restrict the terms of the no-action relief provided herein, in its discretion.

Should you have questions regarding this matter, please contact Brian Baum, Special Counsel (bbaum@cftc.gov, 202-418-5654), or Eileen Donovan, Deputy Director (edonovan@cftc.gov, 202-418-5096).

Sincerely,

Brian A. Bussey  
Director