



U.S. COMMODITY FUTURES TRADING COMMISSION

Three Lafayette Centre
1155 21st Street, NW, Washington, DC 20581
Telephone: (202) 418-5977
Facsimile: (202) 418-5407
gbarnett@cftc.gov

Division of Swap Dealer and
Intermediary Oversight

Gary Barnett
Director

CFTC Letter No. 12-57
No-Action
December 18, 2012
Division of Swap Dealer and Intermediary Oversight

Cheryl Graden
Chief Legal Counsel
Natural Gas Exchange Inc.
10th Floor, 300 – 5th Avenue SW
Calgary, Alberta
Canada T2P 3C4

Re: Time-Limited No-Action Relief: Request that Swaps Transacted on Natural Gas Exchange Not Be Considered in Calculating Aggregate Gross Notional Amount for Purposes of Swap Dealer De Minimis Exception

Dear Ms. Graden:

This letter responds to a request submitted by Natural Gas Exchange Inc. (“NGX”) to the Division of Swap Dealer and Intermediary Oversight (“Division”) of the Commodity Futures Trading Commission (“Commission”) requesting time-limited no-action relief concerning the calculation of the aggregate gross notional amount of swap dealing, as it relates to certain transactions.¹ In relevant part, NGX requested that “contracts traded on NGX [for a limited time period] need not be included within the calculation of the aggregate gross notional amount for purposes of the swap dealer de minimis exception under Commission Rule 1.3(ggg)(4).”

Background

NGX, located in Calgary, Alberta, Canada, operates an exempt commercial market (“ECM”) that provides electronic trading, central counterparty clearing and data services to the North American natural gas and electricity markets. The products are traded through the IntercontinentalExchange, Inc. (“ICE”) trading platform, pursuant to an Agreement for Services entered into by NGX and ICE. NGX operates an electronic marketplace through which NGX contracting parties may enter into NGX products, which NGX characterizes as (1) forward

¹ See Letter from Cheryl Graden, Chief Legal Counsel, NGX, to Sauntia Warfield, Assistant Secretary of the Commission (Nov. 27, 2012).

contracts for natural gas and crude oil deliverable at various Canadian and U.S. natural gas hubs and crude oil locations and (2) futures contracts relating to deliverable natural gas and crude oil, and electricity, referencing various Canadian and U.S. pricing points. While transactions in electricity and oil are executed on NGX, the most actively executed transactions are for natural gas products.

On November 5, 2002, NGX notified the Commission of its operation as an ECM under section 2(h)(5) of the Commodity Exchange Act (“CEA”). On December 12, 2008, NGX was registered with the Commission as a derivatives clearing organization (“DCO”). On May 19, 2010, NGX submitted to the Commission a request for direct access no-action relief; that request was pending at the time that the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”)² was enacted and when the Commission adopted the Part 48 registration rules for foreign boards of trade (“FBOTs”) seeking to permit direct market access by their U.S. members.³

In February 2012, NGX submitted to the Commission an application for registration as an FBOT to permit its members and other participants in the United States to directly access the trade entry and order matching system pursuant to Part 48 of the Commission’s Regulations. NGX characterizes the contracts and products included in its application as futures contracts. That application is currently pending and under active review. At present, NGX continues to operate as an ECM pursuant to an Order of the Commission while its application for registration as an FBOT pursuant to Part 48 of the Commission’s Regulations is pending.

Applicable Regulatory Requirements

On July 18, 2012, the Commission approved, jointly with the Securities and Exchange Commission (“SEC”), final rules further defining the products terms “swap,” “security-based swap,” “security-based swap agreement,” and “mixed swap” (“Swap Definitions Final Rules”).⁴ The effective date of these joint final rules was October 12, 2012.

On July 3, 2012, the Commission issued a final Order (the “Second Amended Effective Date Order”) to extend the temporary exemptive relief that the Commission granted on July 14, 2011,⁵ from certain provisions of the CEA that otherwise would have taken effect on the general effective date of Title VII of the Dodd-Frank Act—July 16, 2011.⁶ The Second Amended Effective Date Order also modified the temporary exemptive relief that had previously been granted in several respects. Of particular relevance here, in light of the final joint rulemaking with the SEC further defining the entities terms “swap dealer,” “major swap participant,” and

² Pub. L. No. 111-203, 124 Stat. 1376 (2010).

³ See Registration of Foreign Boards of Trade, 76 Fed. Reg. 80674 (Dec. 23, 2011).

⁴ Further Definition of “Swap,” “Security-Based Swap,” and “Security-Based Swap Agreement”; Mixed Swaps; Security-Based Swap Agreement Recordkeeping, 77 Fed. Reg. 48208 (Aug. 13, 2012).

⁵ Effective Date for Swap Regulation, 76 Fed. Reg. 42508 (July 19, 2011).

⁶ Second Amendment to July 14, 2011 Order for Swap Regulation, 77 Fed. Reg. 41260 (July 13, 2012).

“eligible contract participant,”⁷ the Second Amended Effective Date Order removed references to those terms. Thus, the Second Amended Effective Date Order no longer provided relief with respect to certain provisions of the CEA, as amended or added by the Dodd-Frank Act, that reference one or more of such entities terms.

With respect to the products terms, the Second Amended Effective Date Order extended the relief previously provided with respect to certain provisions of the CEA,⁸ as amended or added by the Dodd-Frank Act, that specifically relate to such terms, but provided that such relief would expire upon the earlier of the effective date of the rulemaking further defining those terms, or December 31, 2012. Accordingly, upon the effective date of the joint final rules to further define these terms—*i.e.*, October 12, 2012—the relief under the Second Amended Effective Date Order with respect to the application of the provisions of the CEA that reference such terms expired.

The Second Amended Effective Date Order generally permitted parties to continue to rely on the various exclusions and exemptions that the CEA established for swaps (*i.e.*, CEA Sections 2(d), 2(e), 2(g), 2(h) and 5d) prior to its amendment by the Dodd-Frank Act, notwithstanding the fact that as of July 16, 2011, those provisions were removed from the CEA by the Dodd-Frank Act and replaced by various provisions that subjected swap activity to Commission oversight. However, section (4)c of the Second Amended Effective Date Order states that the relief provided in the Order shall not “[a]ffect any effective or compliance date set forth in any rulemaking issued by the Commission to implement provisions of the Dodd-Frank Act.” In other words, as particular Dodd-Frank Act-implementing rulemakings become effective, any applicable exemption or exclusion ceases and compliance with that new regulatory requirement begins.

Accordingly, with the October 12, 2012 effective date of the Swap Definitions Final Rules, all swaps entered into by a person after October 12, 2012, in connection with the person’s swap dealing activities are relevant in determining whether the person is within the swap dealer definition and therefore must register as a swap dealer.⁹

On October 12, 2012, the Division issued a no-action letter¹⁰ that provided time-limited relief with respect to cleared swaps referencing exempt commodities.¹¹ Specifically, the letter read as follows:

⁷ Further Definition of “Swap Dealer,” “Security-Based Swap Dealer,” “Major Swap Participant,” “Major Security-Based Swap Participant,” and “Eligible Contract Participant,” 77 Fed. Reg. 30596 (May 23, 2012)

⁸ The relief with respect to such products terms had extended to such provisions in the CEA which were listed in Category 2 of the Appendix to the initial exemptive Order and expired upon the further definition of those terms. 76 Fed. Reg. at 42522.

⁹ The Division has issued staff letters providing further guidance and no-action relief on this issue. Copies of staff letters relating to the Dodd-Frank Act are available on the Commission’s website at: <http://www.cftc.gov/LawRegulation/DoddFrankAct/GuidanceQandA/index.htm> .

¹⁰ CFTC Letter No. 12-16 (Oct. 12, 2012). In the no-action letter, the Division noted its belief “that limited transitional no-action relief is warranted in order to provide participants in the market for cleared swaps . . . referencing exempt commodities . . . sufficient time to determine whether and in what manner to transition those

[T]he Division will not recommend that the Commission take enforcement action against any person for failure to include, in its calculation of the aggregate gross notional amount of swaps connected with its swap dealing activity for purposes of Commission Regulation 1.3(ggg)(4), a swap that (i) references an exempt commodity . . . , (ii) is executed prior to December 31, 2012, and (iii) is . . . cleared on a [DCO] registered with the Commission¹²

On December 11, 2012, in order to “ensure that industry practices would not be unduly disrupted during the transition to the new Dodd-Frank Act regulatory regime,” the Commission’s Division of Market Oversight issued time-limited no-action relief, which stated that it would not:

recommend that the Commission commence an enforcement action regarding any agreement, contract, or transaction, or any person or entity offering, entering into, or rendering advice or rendering other services with respect to, any such agreement, contract, or transaction, that conforms with the requirements, as set forth in the Commission’s Second Amendment to July 14, 2011 Order, . . . in paragraphs (3) and (4), in connection with exempt and excluded commodities, except as this relief specifically provides herein.¹³

The no-action relief provided by the Division of Market Oversight will expire on the earlier of June 30, 2013, or “the effective date of the swap execution facility (“SEF”) final rulemaking, unless a facility relying on this relief has filed a designated contract market (“DCM”) or SEF registration application on or before the effective date of the SEF final rules, in which case the relief shall remain in place during the pendency of the application.”¹⁴ The relief further stated that “this no-action relief is provided to facilities who operate CEA Section 2(d), 2(e), 2(g), 2(h), or 5d-compliant platforms (as those sections were in effect prior to July 16,

swap activities to similar products in the futures markets that will become available in the near future, and to enable any such transition to proceed in an orderly manner.” *Id.* at 4.

¹¹ The term “exempt commodity” is defined under CEA Section 1a(14) as a “commodity that is not an excluded commodity or an agricultural commodity.” An “excluded commodity” is defined under CEA Section 1a(13) as:

(i) an interest rate, exchange rate, currency, security, security index, credit risk or measure, debt or equity instrument, index or measure of inflation, or other macroeconomic index or measure; (ii) any other rate, differential, index, or measure of economic or commercial risk, return, or value that is— (I) not based in substantial part on the value of a narrow group of commodities not described in clause (i); or (II) based solely on one or more commodities that have no cash market; (iii) any economic or commercial index based on prices, rates, values, or levels that are not within the control of any party to the relevant contract, agreement, or transaction; or (iv) an occurrence, extent of an occurrence, or contingency (other than a change in the price, rate, value, or level of a commodity not described in clause (i)) that is— (I) beyond the control of the parties to the relevant contract, agreement, or transaction; and (II) associated with a financial, commercial, or economic consequence.

¹² *Id.* at 4.

¹³ CFTC Letter No. 12-48, at 2 (Dec. 11, 2012).

¹⁴ *Id.*

2011), as well as any person or entity offering, entering into, or rendering advice or rendering other services with respect to, any agreement, contract, or transaction on such facility.”¹⁵

Time-Limited No-Action Relief Granted

Based on the foregoing and the information provided by NGX, the Division believes that time-limited no-action relief is warranted. In particular, the Division notes that NGX has submitted a completed FBOT registration application to the Commission, NGX has characterized all of the products included in its application as futures contracts, and such contracts currently are cleared on NGX’s DCO.¹⁶

Accordingly, the Division will not recommend that the Commission take an enforcement action against any person for failure to include a swap executed on NGX prior to the earlier of March 31, 2013, or the granting or denial of NGX’s application for registration as an FBOT, in its calculation of the aggregate gross notional amount of swaps connected with its swap dealing activity for purposes of Commission Regulation 1.3(ggg)(4).

This letter, and the positions taken herein, represent the view of this Division only, and do not necessarily represent the position or view of the Commission or of any other office or division of the Commission. The relief issued by this letter does not excuse persons relying on it from compliance with any other applicable requirements contained in the Act or in the Regulations issued thereunder. Further, this letter, and the relief contained herein, is based upon the representations made to the Division. Any different, changed or omitted material facts or circumstances might render this no-action relief void.

Should you have any questions, please do not hesitate to contact Frank Fisanich, Chief Counsel, at 202-418-5949, or Ward Griffin, Associate Chief Counsel, at 202-418-5425.

Very truly yours,

Gary Barnett
Director
Division of Swap Dealer and
Intermediary Oversight

¹⁵ *Id.*

¹⁶ This no-action relief is not intended to be an indication that the Commission will or will not grant registration to NGX as an FBOT.