

CLIENT UPDATE

CFTC EXTENDS REGISTRATION RELIEF AND GRANTS ADDITIONAL RELIEF FOR CERTAIN PERSONS

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On December 28, 2012, the Commodity Futures Trading Commission (the “CFTC”) issued a no-action letter (the “AP Relief Extension Letter”)¹ extending certain registration relief for associated persons (“APs”) of a futures commission merchant (“FCM”), introducing broker (“IB”), commodity pool operator (“CPO”) or commodity trading advisor (“CTA”) which was initially granted by a no-action letter dated October 11, 2012 (the “Original AP No-Action Letter”).²

On December 31, 2012, the CFTC issued another no-action letter (the “IB/CTA No-Action Letter”) providing no-action relief from the IB and CTA registration requirements to persons coming within the IB or CTA definitions solely as a result of their involvement in certain activities in connection with swaps entered into by their employers or certain of their affiliates.³

¹ CFTC No-Action Letter No. 12-69 issued on December 28, 2012, <http://www.cftc.gov/PressRoom/PressReleases/pr6486-12>

² See our client memorandum “CFTC Grants Registration Relief for Certain Persons and Other Relief for Certain Associated Persons” <http://www.debevoise.com/clientupdate20121017a/>

³ CFTC No-Action Letter No. 12-70 issued on December 31, 2012, <http://www.cftc.gov/PressRoom/PressReleases/pr6487-12>

BACKGROUND

Original AP No-Action Letter

The Original AP No-Action Letter provided that the Division of Swap Dealer and Intermediary Oversight of the CFTC (“DSIO”) would not recommend that the CFTC commence an enforcement action against certain persons for failure to be registered under the Commodity Exchange Act (the “CEA”) by October 12, 2012. Among the persons to whom this relief (the “AP Temporary Registration Relief”) applies are APs of an FCM, IB, CPO or CTA who are required to register with the CFTC solely by virtue of their involvement with (1) swaps or (2) the transition of certain contracts (“ICE/NYMEX Contracts”) by the Intercontinental Exchange, Inc. and the New York Mercantile Exchange to clearing as commodity futures and options transactions. This relief is conditioned on the employing FCM, IB, CPO or CTA filing a Form 8-R and a fingerprint card for such AP.

The purpose of the AP Temporary Registration Relief was to prevent market disruptions during the transition to the new regulatory regime mandated by Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”), to provide eligible persons with sufficient time to complete the applicable registration process and to relieve the pressure on the National Futures Association (the “NFA”) and the new registration system as a result of the sudden influx of numerous registration applications.

Registration as an IB or CTA Based on Swap-Related Activities

Section 1a(31)⁴ of the CEA, as amended by the Dodd-Frank Act, defines “introducing broker” to include any person engaged in soliciting or accepting orders for the purchase or sale of a swap and who does not accept any money, securities or property (or extend credit in lieu thereof) to margin, guarantee or secure any trades or contracts that may result therefrom.

Section 1a(12), as amended by the Dodd-Frank Act, defines “commodity trading advisor” to include any person who, for compensation or profit, engages in the business of advising others as to the value of or the advisability of trading in any swap.

The CFTC has similarly amended the IB and CTA definitions in Regulations 1.3(mm) and 1.3(bb), respectively, to incorporate swap-related activities.

⁴ Unless otherwise stated, all Section references are to sections of the CEA.

If a person comes within these definitions, it is subject to registration as an IB or CTA (as applicable) under Section 4d or 4m, respectively.⁵ Registration includes, among other things, vetting of the applicant for registration, its principals and its APs to confirm that none of these persons is subject to a statutory disqualification under Section 8a(2) or 8a(3) (“Statutory Disqualification”). While applicants for registration as an AP must typically pass the National Commodity Futures Examination (“Series 3”), NFA Registration Rule 401 provides that the Series 3 testing requirement is not applicable to APs whose activities are limited to swaps.

REQUESTS FOR RELIEF

DSIO received numerous requests to extend the AP Temporary Registration Relief due to significant administrative burdens which continue to affect the ability of certain applicants, some of which may have hundreds of APs, to comply by the December 31, 2012 filing deadline for those APs.

DSIO also received various registration no-action requests regarding certain swap dealers (“SDs”), persons excluded from the swap dealer definition under Regulation 1.3(ggg)(4) (“De Minimis Dealers,” or “DMDs”),⁶ SD affiliates who are not registered with the CFTC in any capacity (“Agent Affiliates”) and employees of these SDs, DMDs and Agent Affiliates. These petitioners represented that SDs may deal in swaps through multiple affiliates, such that employees of one SD (an “Agent SD”) or an Agent Affiliate may engage in certain activities in support of an affiliated SD or affiliated DMD in connection with a swap transaction to be entered by such affiliated SD or affiliated DMD as counterparty to the swap (“Affiliate SD Counterparty” or “Affiliate DMD Counterparty”, respectively). These activities (“Affiliate Support Activities”) may include soliciting, negotiating, structuring, recommending and/or accepting as agent, swap transactions on behalf of the Affiliate SD Counterparty or Affiliate DMD Counterparty.

Additionally, these petitioners represented that Agent SDs and Agent Affiliates may (1) engage in Affiliate Support Activities in connection with new swaps as well as with respect to a subsequent modification, termination or exercise of rights under an existing swap; and (2) receive compensation from an Affiliate SD Counterparty or Affiliate DMD Counterparty for Affiliate Support Activities performed by their employees in connection

⁵ The CEA and the Regulations provide exemptions from registration as an intermediary for certain persons (e.g., Section 4m(1) and Regulation 4.14, providing exemptions from CTA registration). The IB/CTA No-Action Letter does not affect the availability of such an exemption to persons covered by such letter.

⁶ Regulation 1.3(ggg)(4) provides an exception from the swap dealer definition for certain persons who engage in a de minimis amount of swap dealing.

with cost and/or revenue allocation arrangements with the Affiliate SD Counterparty or Affiliate DMD Counterparty.

Petitioners therefore requested no-action relief for Agent SDs, Agent Affiliates and their respective employees from the requirement to register as an IB or a CTA (1) where the Agent SD, Agent Affiliate or employee engages in Affiliate Support Activities on behalf of an Affiliate SD Counterparty; or (2) in the case of an Agent SD and its employees, where such Agent SD or employee engages in Affiliate Support Activities on behalf of an Affiliate DMD Counterparty.

Additionally, petitioners requested registration relief for employees of Affiliate DMD Counterparties who are engaged in IB activities on behalf of and in connection with a swap transaction to be entered into by the employer Affiliate DMD Counterparty itself.

Finally, DSIO received requests for no-action relief from AP registration for employees of a registered FCM or IB who are engaged in Affiliate Support Activities.

NO-ACTION RELIEF

Extension of Registration Relief for Certain Associated Persons

The AP Relief Extension Letter provides that DSIO will not recommend that the CFTC commence an enforcement action against a person for failure to be registered as an AP of an FCM, IB, CPO or CTA where the requirement to be registered as such arises solely from (1) the swap activity of the person or (2) the person being involved with ICE/NYMEX Contracts, provided that:

- On or before March 31, 2013, the FCM, IB, CPO or CTA completes and files with the NFA a registration application for the person, including a Form 8-R and a fingerprint card, as applicable; and
- Subject to the foregoing, on and after March 31, 2013, the person is subject to and makes a good faith effort to comply with the CEA and the CFTC Regulations applicable to its activities as an AP of an FCM, IB, CPO or CTA as if the person was in fact registered as such.

This extended registration relief will terminate on either of the following dates:

- the date on which the NFA provides notice in accordance with Regulation 3.2(c) that the person relying on such relief is registered as an AP; or

- five (5) days after service by the NFA of a notice on such person pursuant to NFA Registration Rule 504 that the person may be subject to Statutory Disqualification.

Additional Relief for Certain Persons from IB and CTA Registration Requirements

Agent SDs and Employees

Because Affiliate Support Activities include activities that may bring a person within the IB and/or CTA definition, an Agent SD who engages in Affiliate Support Activities on behalf of an Affiliate SD Counterparty or Affiliate DMD Counterparty may be required to register as an IB or a CTA,⁷ and its employees may be required to register as APs of the Agent SD in its capacity as an IB.⁸ In the IB/CTA No-Action Letter, DSIO notes that, in connection with the Agent SD's application for registration as an SD, the Agent SD, its principals and its APs will have been vetted to confirm that none of them is subject to a Statutory Disqualification.⁹

Accordingly, the IB/CTA No-Action Letter provides that DSIO will not recommend that the CFTC commence an enforcement action against an Agent SD or any employee thereof for failure to register as an IB or a CTA if the Agent SD or employee engages in Affiliate Support Activities on behalf of an Affiliate SD Counterparty or Affiliate DMD Counterparty in connection with a swap entered or to be entered into by the Affiliate SD Counterparty or Affiliate DMD Counterparty, subject to the following conditions:

- The Agent SD and the Affiliate SD Counterparty or Affiliate DMD Counterparty are "majority-owned affiliates" as described in Regulation 1.3(ggg)(6);
- The employee is an AP of the Agent SD, as defined in Regulation 1.3(aa)(6), and neither the employee nor any person in such employee's supervisory chain of command is subject to a Statutory Disqualification;

⁷ While Regulation 4.6 excludes from the CTA definition a registered SD and its employees and principals where the commodity interest and swap advisory activities of the SD are solely incidental to the conduct of its business as an SD, the exclusion does not address SDs (such as Agent SDs) that engage in CTA activities on behalf of an Affiliate SD Counterparty or Affiliate DMD Counterparty.

⁸ Section 4k(1) makes it unlawful for a person to associate with an IB in soliciting customers' orders unless the person is registered as an AP of an IB. Regulation 1.3(mm) provides an exclusion from the IB definition for, and therefore makes the prohibition inapplicable to, an AP of an SD acting in such capacity. Because an AP must be a natural person under Regulation 1.3(aa), this exclusion would not be available to an Agent SD that is not a natural person. Section 4k(3) makes it unlawful for a person to associate with a CTA in soliciting discretionary trading accounts unless the person is registered as an AP of the CTA. Since the representations made by the petitioners in support of CTA registration relief do not pertain to discretionary trading, registration as an AP of a CTA is not at issue in the scenarios discussed in the IB/CTA No-Action Letter.

⁹ While the CFTC has not required APs of SDs to register as such, Regulation 23.22 prohibits an SD from employing an AP that is subject to Statutory Disqualification.

- The Agent SD and the employee provide commodity interest trading advice in a manner solely incidental¹⁰ to the conduct of the business of the Agent SD as an SD;
- Neither the Agent SD nor the employee is otherwise engaged in activity that would require registration as an IB, CTA or AP thereof;
- The Agent SD and the Affiliate SD Counterparty or Affiliate DMD Counterparty execute in writing an undertaking by which (1) they each agree to be jointly and severally liable for any violation of the CEA or the Regulations by any employee of the Agent SD engaged in any Affiliate Support Activity on behalf of the Affiliate SD Counterparty or Affiliate DMD Counterparty; and (2) in the case of an Affiliate DMD Counterparty, the Affiliate DMD Counterparty consents to the jurisdiction of the CFTC to investigate and take enforcement action against the Affiliate DMD Counterparty for any violation of the CEA or the Regulations in connection with the Affiliate Support Activity by any employee of the Agent SD on behalf of the Affiliate DMD Counterparty; and
- The Agent SD maintains such written undertaking at its main business office and in accordance with Regulation 1.31.

Agent Affiliates and Employees

Similarly, an Agent Affiliate who engages in Affiliate Support Activities on behalf of an Affiliate SD Counterparty may be required to register as an IB or a CTA, and its employees may be required to register as an AP of the Agent Affiliate acting in its capacity as an IB. In the IB/CTA No-Action Letter, DSIO notes that, because an Agent Affiliate will not otherwise be registered with the CFTC, none of the firm, its principals or its APs will have been vetted to confirm that they are not subject to a Statutory Disqualification. However, DSIO notes that, in prior situations raising similar concerns, the CFTC has nonetheless provided registration no-action relief based on the particular facts presented to it, subject to certain conditions.¹¹

Accordingly, the IB/CTA No-Action Letter provides that DSIO will not recommend that the CFTC commence an enforcement action against an Agent Affiliate or any employee thereof for failure to register as an IB or a CTA if the Agent Affiliate or employee engages in Affiliate Support Activities on behalf of an Affiliate SD Counterparty in connection with a

¹⁰ See, e.g., 77 Fed. Reg. 9734, 9739-9740 (Feb. 17, 2012) (discussing the “solely incidental” requirement set forth in Regulation 4.6(a)(3) for the exclusion from the CTA definition available therein).

¹¹ See, e.g., CFTC Staff Letter No. 03-13 (Mar. 19, 2003); CFTC Staff Letter No. 97-85 (Oct. 8, 1997).

swap entered or to be entered into by the Affiliate SD Counterparty, subject to the following conditions:

- The Agent Affiliate is registered or licensed with, or subject to regulation by, a financial services, prudential or banking regulator (including a self-regulatory organization) in the United States, a country that is a member of the European Union, Switzerland, Canada, Japan, Hong Kong, Singapore or Australia (the “Regulated Entity Condition”); and
- The Agent Affiliate and the Affiliate SD Counterparty are “majority-owned affiliates” as described in Regulation 1.3(ggg)(6);
- None of the Agent Affiliate, the employee or any person in such employee’s supervisory chain of command is subject to a Statutory Disqualification;
- The Agent Affiliate and the employee provide commodity interest trading advice in a manner solely incidental to the conduct of the business of the Agent Affiliate for which it is subject to regulation under the Regulated Entity Condition;
- Neither the Agent Affiliate nor the employee is otherwise engaged in activity that would require registration as an IB, CTA or AP thereof;
- The Agent Affiliate and the Affiliate SD Counterparty execute in writing an undertaking by which (1) they each agree to be jointly and severally liable for any violation of the CEA or the Regulations by any employee of the Agent Affiliate engaged in any Affiliate Support Activity on behalf of the Affiliate SD Counterparty; and (2) the Agent Affiliate consents to the jurisdiction of the CFTC to investigate and take enforcement action against the Agent Affiliate or any employee thereof engaged in any Affiliate Support Activity on behalf of the Affiliate SD Counterparty for any violation of the CEA or the Regulations by the employee; and
- The Affiliate SD Counterparty maintains such written undertaking at its main business office and in accordance with Regulation 1.31.

In the IB/CTA No-Action Letter, DSIO notes that, while it is aware that Agent Affiliates may engage in Affiliate Support Activities on behalf of Affiliate DMD Counterparties, it has not received any requests for registration relief on behalf of Agent Affiliates in this context and is not granting any such relief at this time.

Employees of DMD Counterparties

The IB/CTA No-Action Letter provides that, consistent with the fact that Affiliate DMD Counterparties are excluded from the SD definition, and therefore are not required to register as an SD, if an employee of an Affiliate DMD Counterparty is engaged solely in IB

activities on behalf of and in connection with a swap transaction to be entered into by its employer Affiliate DMD Counterparty, such employee would not come within the IB definition and, thus, would not be required to register as an IB.

No Registration Relief for APs of FCMs and IBs

DSIO declined to provide no-action relief from AP registration to employees of a registered FCM or IB who are engaged in Affiliate Support Activities. However, DSIO acknowledges in the IB/CTA No-Action Letter that FCMs and IBs that employ individuals who must register as APs solely as a result of their involvement with swaps may be facing significant burdens in ensuring that registration applications for such individuals are filed by December 31, 2012. DSIO notes that it has therefore issued the AP Relief Extension Letter, which extends to March 31, 2013 the date by which registration applications for such APs must be filed.

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Please do not hesitate to contact us if you have any questions.

January 31, 2013