



DERIVATIVES MONTHLY INBRIEF*

JULY 11, 2014

INDUSTRY HEADLINES

- **Quick Stock Sales Toy with Volcker Rule's Spirit: July 3, 2014**
Making a mistake is one thing. But under the Volcker Rule, willingly making a bet is a no-no worthy of regulatory scrutiny. Investment banks are using quick stock sales to toy with the spirit of the Volcker Rule. Wall Street sold some \$23 billion in large trading orders, or block trades, for public companies in the first half of the year, according to Thomson Reuters data. That's almost as much as initial public offerings have raised. These deals are a handy tool for corporations. But at times, investment banks blur the line between capital-raising and banned proprietary trading. [Read more.](#)
- **Banks May Lose \$4.5 Billion a Year From Swaps Shift: June 25, 2014**
Banks stand to lose as much as \$4.5 billion in annual revenue as regulations aimed at improving financial stability alter how interest-rate swaps are bought and sold, according to a report from McKinsey & Co. That's equal to 35 percent of the \$13 billion in revenue banks worldwide earn each year from rate derivatives and comes at a time when their fixed-income, currencies and commodities businesses are flagging. The driving force is the requirement that most swaps trade on electronic systems rather than over the phone, with more price transparency and competition eating profits. [Read more.](#)
- **CFTC Extends Relief for LCH.Clearent Addressing SEF, Futures/Options Clearing: June 25, 2014**
CFTC staff extended existing no-action relief for LCH.Clearent Ltd. that will allow the clearing firm and its members to continue to clear certain swaps executed on designated contract markets (DCMs) or swap execution facilities (SEFs). In a separate action on June 25, staff extended existing relief allowing LCH and its members to clear futures and options contracts listed on Nodal Exchange LLC before LCH's designated clearing organization (DCO) registration is amended to permit such activity. As part of the same action, staff extended existing relief allowing Nodal to have its contracts cleared by LCH before the DCO is authorized to clear such transactions. [Read more.](#)

CONGRESSIONAL ACTION

HIGH-SPEED TRADING

- **SEC's High-Speed Trader Plan Embraced by Funds Including Invesco: July 9, 2014**
A sweeping blueprint designed by the SEC to reduce conflicts of interest in the stock market won support from leaders of exchanges and large money managers. Chief executives from the New York Stock Exchange to institutional investors including Citadel LLC and Invesco Ltd. backed the commission's call to rein in some high-frequency trading and make secretive trading venues known as dark pools disclose more about how they work. The SEC also should move forward with a plan to require that brokers provide investors with detailed maps of how their orders are filled, the executives said on July 8, 2014 at a hearing of the Senate Banking Committee. [Read more.](#)
- **High-Frequency Trading Fees Need Transparency, Exchanges Say: June 17, 2014**
U.S. stock exchanges and one of the world's largest mutual fund companies called for greater public disclosure or elimination of obscure incentives and fees that lawmakers said favor the interests of high-speed traders over other

*This is not an all-inclusive list of congressional, agency and market participant actions related to these issues. It is a snap-shot of what we believe is of most interest to institutional investors. Some links are to subscriber-only sites.

investors. Executives from Intercontinental Exchange Inc., owner of the New York Stock Exchange, Bats Global Markets Inc., IEX Group Inc. and Vanguard Group Inc. told the Senate's Permanent Subcommittee on Investigations that rebate fees and payments to brokers for orders should face greater regulatory scrutiny. High-frequency traders now account for about half of U.S. stock trades. Senator Carl Levin, the Michigan Democrat who leads the panel, called the hearing to examine conflicts of interest embedded deep in the plumbing of equity markets that he said are leading to the erosion of investors' trust and confidence. [Read more.](#)

SWAPS

▪ **House Appropriators Vote to Curb Swaps Rule: June 25, 2014**

The House Appropriations Committee approved a fiscal 2015 Financial Services spending bill that would reduce IRS funding and limit a Dodd Frank swaps rule. The bill was approved on a party-line vote of 28-21. It would provide \$21.3 billion in discretionary funds, a cut of \$566 million from the current fiscal year. The measure would fund the Treasury Department and agencies including the Securities and Exchange Commission and Federal Trade Commission as well as the federal payment to the District of Columbia. [Read more.](#)

BUDGET

▪ **Senate SEC, CFTC Funding Bill Advances: June 24, 2014**

Senate appropriators backed a \$44.1 billion draft spending bill today funding the Internal Revenue Service, financial services regulators and other agencies for the fiscal year that begins October 1, 2014. The measure contains \$22.7 billion in discretionary funding, \$607 million more than provided for fiscal 2014, according to a summary by the Financial Services Appropriations Subcommittee. The next step for the bill is a full committee markup. The bill would increase funding for the CFTC by \$65 million, to \$280 million, and by \$350 million, to \$1.7 billion, for the SEC to help the agency implement the 2010 Dodd-Frank law. [Read more.](#)

DERIVATIVES REGULATION

▪ **House Passes CFTC Bill That Would Change Derivatives Rules: June 24, 2014**

The CFTC would be reauthorized for five years, through fiscal 2018, under a modified version of H.R. 4413 that also would make changes to derivatives regulations established in the 2010 Dodd-Frank law. The bill contains provisions from several other bills, including four that the House has already passed as stand-alone measures. The CFTC has historically overseen trading in agriculture futures, which are contracts that farmers use to predetermine the date and price at which a commodity will be purchased and ideally protect them from big price fluctuations. The Dodd-Frank financial regulatory overhaul, Public Law 111-203, expanded the agency's jurisdiction to include the swaps market and its key investment banks such as JP Morgan Chase & Co. and Citigroup Inc. The bill, called the "Customer Protection and End-User Relief Act," would make changes to the CFTC's operations and address regulations on futures brokers and swaps end users. [Read more.](#)

AGENCY ACTION

1. **Agency Announcements**

COMINGS & GOINGS

▪ **Massad Makes CFTC Staff Appointments: June 17, 2014**

Jonathan Marcus will remain general counsel of the Commodity Futures Trading Commission under incoming Chairman Timothy Massad, who announced several key staff appointments June 17. Marcus has held the position for approximately 14 months. He previously was deputy general counsel for litigation, where he helped defend several rules adopted by the commission under the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act against legal challenges.

In other staffing decisions, Massad named House aide Clark Ogilvie chief of staff and Senate aide Cory Claussen director of Legislative Affairs. In a release, the commission said Ogilvie has been on the staff of House Agriculture Committee ranking member Collin Peterson (D-Minn.), while Claussen comes from the staff of Senate Agriculture Committee Chairwoman Debbie Stabenow (D-Mich.).

Meanwhile, Lawranne Stewart will remain as interim senior counsel, a position she took under Acting CFTC Chairman Mark Wetjen. She previously was chief counsel to the House Financial Services Committee. Steven Adamske will remain director of Public Affairs and agency spokesman, a position he has held for approximately three years.

On June 10, Massad named former federal prosecutor Aitan Goelman director of Enforcement. [Read more.](#)

▪ **Miller to Leave Treasury In September After Volcker Rule Work: June 12, 2014**

Mary Miller, the U.S. Treasury Department official who led implementation of new financial regulations including the Volcker rule, is leaving the department in early September. Miller, 58, has been the undersecretary for domestic finance since 2012 and was assistant secretary for financial markets for two years before that. A successor would have to be nominated by President Barack Obama and confirmed by the Senate. The Treasury hasn't named anyone to replace her on an interim basis once she leaves. Miller spent 26 years at Baltimore-based asset manager T. Rowe Price Group Inc. as director of fixed income, head of the municipal bond department and a portfolio manager. She led a public conference last month at the Treasury on whether asset managers pose a potential threat to financial stability and should be designated systemically important by a council of U.S. regulators. Miller also coordinated five U.S. agencies that wrote the Volcker rule intended to limit risks from proprietary trading at banks. The rule, which regulators worked on for more than three years, was completed in December. [Read more.](#)

▪ **U.S. CFTC Names Former Prosecutor Goelman to Head Enforcement: June 11, 2014**

Aitan Goelman, a former federal prosecutor and criminal defense lawyer, was named director of enforcement at the U.S. regulator in charge of rooting out fraud and manipulation in derivatives markets. Goelman, a Washington-based partner at Zuckerman Spaeder LLP, will join the CFTC, agency chairman Timothy Massad said yesterday in a statement announcing his first high-profile personnel move since he was sworn in last week. Goelman has been a litigation partner at Zuckerman Spaeder for 11 years, including recently defending a former analyst at Steven Cohen's hedge fund SAC Capital Advisors LP in an insider-trading investigation. [Read more.](#)

DERIVATIVES

▪ **ISDA, SIFMA Urge CFTC to Forego Position Limits Until Cause Can be Shown: July 7, 2014**

The International Swaps and Derivatives Association and the Securities Industry and Financial Markets Association jointly urged the CFTC on July 7, 2014 to forego mandating position limits until the agency can demonstrate that they are necessary. ISDA and SIFMA successfully sued the CFTC over its position limits rule in 2011, saying the agency did not demonstrate that such limits were necessary to curb excessive speculation. [Read more.](#)

▪ **Big Brokers Need More Capital to Avert Failure, SEC's Stein Says: June 12, 2014**

The biggest Wall Street brokerages should face stricter capital requirements as regulators search for tools to limit the impact of a firm's failure on the broader financial system, a member of the U.S. Securities and Exchange Commission said. Stein also said the agency needs to accelerate its progress on rules required by the 2010 Dodd-Frank Act, which called for most swap contracts to be centrally cleared and traded on exchanges. The SEC hasn't adopted many of the required rules intended to curb the risks posed by swaps, complex derivatives once dubbed "financial weapons of mass destruction" by Warren Buffett. [Read more.](#)

CROSS-BORDER SWAPS

▪ **Wall Street Defends Steps to Shield Overseas Swap Trading From U.S. Regulation: July 1, 2014**

Responding to warnings from U.S. regulators that banks are finding ways around new curbs on financial risks, Wall Street is mobilizing to defend its latest tactic to keep overseas derivatives beyond the reach of U.S. rules. The industry campaign comes as regulators at the Commodity Futures Trading Commission, Federal Deposit Insurance Corporation and Securities and Exchange Commission, as well as the top Democrat on the House Financial Services Committee, has expressed concerns that lifting guarantees might sidestep rules designed to limit risk in the financial system. Under Dodd-Frank, non-guaranteed affiliates must comply with fewer regulations than foreign branches and guaranteed affiliates of banks. [Read more.](#)

▪ **SEC Extends Curbs on Swaps Overseas With Possible Loophole: June 25, 2014**

U.S. banks' overseas derivative trades face new curbs under a SEC plan adopted today, even as some members warned it may not go far enough to rein in Wall Street efforts to escape the Dodd-Frank Act. The five-member SEC voted unanimously to extend the agency's rules to transactions executed by foreign divisions of banks including JPMorgan Chase & Co. and Goldman Sachs Group Inc. when a unit's trades are guaranteed by the parent company. The new rule comes as Wall Street has removed those guarantees to avoid Dodd-Frank regulations issued by another agency, the Commodity Futures Trading Commission. [Read more.](#)

▪ **Risk of Banks Dodging Swaps Rules Leads to Scrutiny by FDIC: June 6, 2014**

The U.S. regulator responsible for making sure banks aren't too-big-to-fail is examining whether the biggest firms are shifting trades overseas in a way that may undermine rules designed to prevent a repeat of the 2008 financial crisis. In recent months, large banks have restructured their overseas transactions to trade swaps—contracts blamed

for exacerbating the crisis—outside of rules required by the 2010 Dodd-Frank Act. That law also gave the Federal Deposit Insurance Corporation the power to take over and dismantle large, failing banks, a job that Vice Chairman Thomas Hoenig said Wall Street may be making tougher by the overseas dodge. The FDIC has joined the Commodity Futures Trading Commission in “actively monitoring developments” in the banks’ overseas affiliates and watching for any impacts, Andrew Gray, an FDIC spokesman, said in an e-mail. [Read more.](#)

2. Agency Rulemaking

CROSS-BORDER SWAPS

▪ **SEC Final Rule: Application of Security-Based Swap Dealer and Major Security-Based Swap Participant Definitions to Cross-Border Security-Based Swap Activities (79 FR 39067)**

- **Published:** **July 9, 2014**
- **Effective:** **September 8, 2014**
- The Securities and Exchange Commission (SEC or Commission) is adopting rules and providing guidance to address the application of certain provisions of the Securities Exchange Act of 1934 (Exchange Act) that were added by Subtitle B of Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), to cross-border security-based swap activities.
- These rules and guidance in large part focus on the application of the Title VII definitions of security-based swap dealer and major security-based swap participant in the cross-border context.
- The Commission also is adopting a procedural rule related to the submission of applications for substituted compliance. In addition, the Commission is adopting a rule addressing the scope of our authority, with respect to enforcement proceedings, under section 929P of the Dodd-Frank Act. [Read more.](#)

DERIVATIVES POSITIONS

▪ **CFTC Proposed Rule: Position Limits for Derivatives and Aggregation of Positions (79 FR 37973)**

- **Published:** **July 3, 2014**
- **Comment Deadline Extended:** **August 4, 2014**
- On December 12, 2013, the Commodity Futures Trading Commission (Commission) published in the Federal Register a notice of proposed rulemaking (the Position Limits Proposal) to establish speculative position limits for 28 exempt and agricultural commodity futures and options contracts and the physical commodity swaps that are economically equivalent to such contracts.
- On November 15, 2013, the Commission published in the Federal Register a notice of proposed rulemaking (the Aggregation Proposal) to amend existing regulations setting out the Commissions policy for aggregation under its position limits regime.
- In addition, the Commission directed staff to hold a public roundtable on June 19, 2014, to consider certain issues regarding position limits for physical commodity derivatives.
- In order to provide interested parties with an opportunity to comment on the issues to be discussed at the roundtable, the Commission published notice in the Federal Register on May 29, 2014, that the comment periods for the Position Limits Proposal and the Aggregation Proposal were reopened, starting June 12, 2014 (one week before the roundtable) and ending July 3, 2014 (two weeks following the roundtable).
- To provide commenters with a sufficient period of time to respond to questions raised and points made at the roundtable, the Commission is now further extending the comment period.
- Comments should be limited to the issues of hedges of a physical commodity by a commercial enterprise, including gross hedging, cross-commodity hedging, anticipatory hedging, and the process for obtaining a non-enumerated exemption; the setting of spot month limits in physical-delivery and cash-settled contracts and a conditional spot-month limit exemption; the setting of non-spot limits for wheat contracts; the aggregation exemption for certain ownership interests of greater than 50 percent in an owned entity; and aggregation based on substantially identical trading strategies. [Read more.](#)

CREDIT DEFAULT SWAPS

▪ **SEC Proposed Rule Change: Extend the Implementation of FINRA Rule 4240 (79 FR 39031)**

- **Published:** **July 2, 2014**
- **Effective:** **July 17, 2015**
- **Comments Due:** **July 30, 2014**

Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Extend the Implementation of FINRA Rule 4240 (on Margin Requirements for Credit Default Swaps). The Notice extends the implementation of the FINRA Rule from July 17, 2014 to July 17, 2015. [Read more.](#)

SWAPS REPORTING

- **CFTC Staff Extends Time-Limited, No-Action Relief for Swap Dealers and Major Swap Participants from Compliance with Reporting Obligations**
 - **Published:** July 1, 2014
 - **Effective:** June 30, 2015

The CFTC's Division of Market Oversight (Division) issued a no-action letter extending until June 30, 2015 the relief previously provided in no-action letter 13-34, expiring on June 30, 2014. The relief is provided to Swap Dealers (SDs) and Major Swap Participants (MSPs) from the obligation to report valuation data for cleared swaps as required by Section 45.4(b)(2)(ii) of the Commission's regulations. [Read more.](#)

SIFIs

- **FSOC Notice and Request for Comments: Proposed Information Collection on Designation of Financial Market Utilities as Systemically Important, pursuant to Section 804 of the Dodd-Frank Act (12 CFR part 1320)**
 - **Release Date:** May 27, 2014
 - **Comments Due:** July 28, 2014
 - The FSOC is soliciting comments concerning its collection of information related to its authority to designate financial market utilities as systemically important. Section 804 of the Dodd-Frank Wall Street Reform and Consumer Protection (the "Dodd-Frank Act") provides the Council the authority to designate a financial market utility ("FMU") that the Council determines is or is likely to become systemically important because the failure of or a disruption to the functioning of the FMU could create, or increase, the risk of significant liquidity or credit problems spreading among financial institutions or markets and thereby threaten the stability of the United States financial system. [Read more.](#)

FUTURES & SWAPS

- **CFTC Final Rule: Ownership and Control Reports, Forms 102/102S, 40/40S, and 71**
 - **Release Date:** November 18, 2013
 - **Effective Date:** February 18, 2014
 - **Compliance Date:** August 15, 2014
 - The CFTC is adopting new rules and related forms to enhance its identification of futures and swap market participants.
 - These final rules will leverage the CFTC's current position and transaction reporting programs by requiring the electronic submission of trader identification and market participant data on amended Forms 102 and 40, and on new Form 71.
 - The new and amended forms require the reporting of certain trading accounts active on reporting markets that are designated contract markets or swap execution facilities. [Read more.](#)

3. Comment Periods Ended, Letters Received

SWAPS

SEC PROPOSED RULE: Recordkeeping and Reporting Requirements for Security-Based Swap Dealers, Major Security-Based Swap Participants, and Broker-Dealers; Capital Rule for Certain Security-Based Swap Dealers (79 FR 25193)

Senator Carl Levin, Chairman of Permanent Subcommittee on Investigations, U.S. Senate Committee on Homeland Security and Governmental Affairs (Comment letter filed with the SEC on July 3, 2014)

- The purpose of this letter is to express support for and suggest enhancements to the proposed rule of the U.S. Securities and Exchange Commission (SEC or Commission) to establish new recordkeeping, reporting, and notification requirements for security-based swap dealers (SBSDs) and major security-based swap participants (MSBSPs). This rule, which is long overdue, is critical to preventing SBSBs

and MSBSPs from taking on excessive risk at the potential expense of American taxpayers, as well as promoting fairer and more efficient markets.

- In addition to supporting the proposed rule this letter offers three suggestions for improvements: including requirements for contemporaneous hedging documentation; adding guidance on the valuation of security-based swaps; and replacing the references to "unique counterparty identifiers" for SBSB and MSBSP swap counterparties with references to Legal Entity Identifiers. [Read more.](#)

SIFMA (Comment letter filed with the SEC on July 1, 2014)

- As noted in the June 20 letter, SIFMA believes that the comment period is not long enough to provide comprehensive feedback on a proposal of this magnitude and technical construct.
- The industry is devoting significant time and resources to analyzing this proposal, and SIFMA staff has been in regular contact with Commission staff regarding the time it would take to prepare thoughtful and comprehensive comments.
- As we have explained to Commission staff, providing the Commission with thorough feedback by the July 1, 2014 deadline is not feasible.

SIFMA (Comment letter filed with the SEC on June 20, 2014)

- The SBSB Recordkeeping and Reporting Proposal is comprehensive and complex, and it would have a significant impact on the industry.
- In addition, the Commission's proposal includes more than 100 specific requests for comment.
- SIFMA's member firms are devoting significant time and resources to studying the proposal, tapping into multiple levels of subject matter expertise. We believe it is critical that industry members and interested individuals have sufficient time to review and evaluate the proposal so that the Commission can have the benefit of the most thoughtful and detailed feedback possible.
- SIFMA believes that a 60-day comment period is not long enough to provide the public the opportunity to develop comprehensive feedback on a proposal of this magnitude.
- As a result, we respectfully request that the Commission extend the deadline for comments on the SBSB Recordkeeping and Reporting Proposal by at least 90 days, to no earlier than October 1, 2014.