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## CFTC Adopts Final Order Extending Delay in Compliance Dates for Dodd-Frank Derivatives Requirements

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**On July 3, 2012, the Commodity Futures Trading Commission (“CFTC”) adopted an order to further extend temporary relief from the effective dates of many new requirements for swaps under Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”) that otherwise would have taken effect on July 16, 2012 (the “Final Order”). The CFTC first granted temporary relief from the effectiveness of these requirements in a final order issued on July 14, 2011 (the “July 14 Order”), which granted relief from compliance with most of the new requirements under Dodd-Frank through December 31, 2011. The CFTC extended this relief through July 16, 2012 through an amended July 14 Order made effective on December 23, 2011. Apart from the changes detailed below, the Final Order further extends the relief of the amended July 14 Order until the earlier of December 31, 2012, or such other compliance date determined by the CFTC.**

### Background

In the July 14 Order,<sup>1</sup> the CFTC distinguished four categories of Dodd-Frank provisions. Certain provisions required a rulemaking to become effective (“Category 1 Provisions”) and so were not covered in the order. The CFTC granted market participants relief from certain self-effectuating provisions that either reference terms subject to further definition by the CFTC pursuant to Sections 712(d)(1) and 721(c) of Dodd-Frank (“Category 2 Provisions”) or repealed provisions of then current law (“Category 3 Provisions”). The CFTC did not extend relief to a certain number of self-effectuating Dodd-Frank provisions (“Category 4 Provisions”), and those provisions became effective in July 2011.

<sup>1</sup> For a summary of the July 14 Order, you may wish to consult our client publication, “CFTC and SEC Relief with Respect to Dodd-Frank Effective Dates for Derivatives Regulation” (June 28, 2011).

## The Final Order

The Final Order extends relief from compliance with Category 2 Provisions until the earlier of the effective date set forth in the final rule adopted by the CFTC further defining the relevant term, or December 31, 2012. Where the CFTC has adopted a final rule implementing a Dodd-Frank provision that sets forth a specific effective date or compliance date, the exemption does not apply (although many of those final rules by their own terms tie compliance dates to the effectiveness of the swap definition rulemaking).

At the time of the Final Order, the CFTC and SEC had issued a final rule further defining the terms “swap dealer,” “major swap participant”<sup>2</sup> and “eligible contract participant,” and the key remaining term subject to further definition for purposes of the July 14 Order is the definition of “swap.” Thus, the relief for Category 2 Provisions is limited to those that specifically reference and relate to the term “swap.” Subsequently, the CFTC has adopted final rules further defining that term, which will be effective 60 days after publication in the Federal Register (and accordingly are expected to be effective in September 2012). Accordingly, this aspect of the exemptive relief should expire upon the effectiveness of the swap definition rule.

Following the publication in the Federal Register of a Notice of Proposed Amendment of the amended July 14 Order (the “Proposed Order”), the CFTC received comments seeking additional guidance regarding the relief detailed in the Proposed Order. Some comments addressed the removal of “eligible contract participant” as a term subject to further definition by the CFTC and SEC. Noting that the CFTC and SEC have indicated they may issue further guidance regarding the meaning of “eligible contract participant,” commenters argued that the Final Order should continue to consider the term to be subject to further definition until market participants have greater clarity as to who is an “eligible contract participant” in order to comply with the relevant provisions of the Commodity Exchange Act.

In the Final Order, the CFTC maintains “eligible contract participant” among the terms already defined by the SEC and CFTC, but issues additional guidance regarding the treatment of an inadvertent violation of the Commodity Exchange Act’s prohibition on the entry into over-the-counter swap transactions by non-eligible contract participants. The CFTC advises in the Final Order that, absent other material factors, it will not bring an enforcement action against a person who entered into a swap with a counterparty that the CFTC and SEC later further define or interpret as not being an eligible contract participant if the person has implemented and followed reasonably designed policies and procedures to verify the swap counterparty’s status as an eligible contract participant and, notwithstanding good faith compliance with such policies and procedures, the person enters into a swap with a counterparty who is not an eligible contract participant. Such policies and procedures must satisfy the requirements for swap dealers and major swap participants set forth in the CFTC’s final rule on business conduct standards for these market participants.<sup>3</sup> The CFTC advises in the Final Order that one could demonstrate “good-faith compliance” by seeking, prior to entering into a swap transaction or devising the policies and procedures required by CFTC rules, additional guidance from one’s counsel or CFTC staff, which could provide more targeted advice on a case-by-case basis with the benefit of specific facts and circumstances. This guidance from the CFTC does not apply to any

<sup>2</sup> Further Definition of “Swap Dealer,” “Security-Based Swap Dealer,” “Major Swap Participant,” “Major Security-Based Swap Participant” and “Eligible Contract Participant”, 77 Fed. Reg. 30,596 (May 23, 2012) (to be codified at 17 C.F.R. pts. 1 and 240).

<sup>3</sup> Business Conduct Standards for Swap Dealers and Major Swap Participants With Counterparties, 77 Fed. Reg. 9734 (Feb. 17, 2012) (to be codified at 17 C.F.R. pts. 4 and 23).

aspect of the “eligible contract participant” definition that was (i) not amended by Dodd-Frank; (ii) covered by a regulation promulgated in the final rule defining the term “eligible contract participant” or (iii) the subject of an interpretation or other guidance set forth in the final rule defining the term “eligible contract participant.” Furthermore, upon a final determination or interpretation by the CFTC and SEC that a counterparty is not an eligible contract participant, new swaps with any such ineligible counterparty would be prohibited under the Commodity Exchange Act.

The Final Order also extends the exemptions in the July 14 Order for Category 3 Provisions that in effect permitted market participants to continue to rely on the pre-Dodd-Frank exclusions and exemptions for derivatives transactions under old Commodity Exchange Act Sections 2(d), 2(e), 2(g) and 2(h) and Part 35 of the CFTC regulations. This exemption is extended until the earlier of December 31, 2012, or such other compliance date as the CFTC specifies. However, the Final Order modifies the exemption applicable to agricultural swaps to reflect final rules issued to amend Part 35 of the CFTC Rules, which permits the clearing of agricultural swaps to the same extent as other swaps.<sup>4</sup> However, under the Final Order, agricultural swaps may only be entered into or executed bilaterally, on a designated contract market (“DCM”) or on a swap execution facility (“SEF”). (The Final Order thus does not change the pre-Dodd-Frank prohibition on platform-trading of agricultural swaps on an exempt commercial market (“ECM”) or exempt board of trade (“EBOT”).)

Finally, the Final Order supplants the ECM/EBOT Grandfather Order issued by the CFTC relieving ECMs, EBOTs and markets that relied on Section 2(d)(2) of the Commodity Exchange Act prior to Dodd-Frank (“Section 2(d)(2) Markets”) from compliance with new Dodd-Frank provisions. The relief provided by the Final Order constitutes the sole basis of relief for such market participants. The Final Order provides that this relief will continue until the earlier of December 31, 2012, or the effective date of the DCM or SEF final rules, whichever is later, unless the ECM, EBOT or Section 2(d)(2) Market files a DCM or SEF application on or before the effective date of the DCM or SEF final rules, whichever is later, in which case the relief shall remain in place during the pendency of the application.

As with the July 14 Order, the Final Order does not limit the CFTC’s anti-fraud or anti-manipulation authority, or apply to any Dodd-Frank provision or CFTC rule already in effect.

We will continue to keep clients updated on any developments concerning the implementation or effectiveness of the Title VII Dodd-Frank requirements.

<sup>4</sup> Agricultural Swaps, 76 Fed. Reg. 49,291 (Aug. 10, 2011) (to be codified at 17 C.F.R. pt. 35).

This memorandum is intended only as a general discussion of these issues. It should not be regarded as legal advice. We would be pleased to provide additional details or advice about specific situations if desired.

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