



## Financial Services & Products ADVISORY ■

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### CFTC Provides Swap Clearing Relief for Smaller Bank Holding Companies and Savings and Loan Holding Companies

On January 8, 2016, the U.S. Commodity Futures Trading Commission's (CFTC) Division of Clearing and Risk (DCR) issued a no-action letter ([CFTC Letter 16-01](#)) providing relief from the clearing requirement for some swaps entered into by bank holding companies (BHCs) and savings and loan holding companies (SLHCs) with consolidated total assets of \$10 billion or less.

Under the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), once the CFTC has determined that a particular category of swaps is subject to mandatory clearing, any swap of that type must be done on a cleared basis unless the "end-user exception" from clearing is available to at least one of the parties. Currently, the following types of swaps are subject to mandatory clearing:

- Interest rate swaps: fixed-to-floating swaps, basis swaps, forward rate agreements and overnight index swaps.
- Credit default swaps: North American untranching CDS indices and European untranching CDS indices.

Under Dodd-Frank, the end-user exception from clearing is available to entities that are not "financial entities"<sup>1</sup> and to banks and savings associations with \$10 billion or less in total assets.<sup>2</sup> However, Dodd-Frank does not include a statutory basis for an exception from mandatory swap clearing for small BHCs and SLHCs. The DCR has filled in that gap with its no-action letter, which provides that the DCR will not recommend the CFTC take enforcement action against a BHC or SLHC with consolidated total assets of \$10 billion or less for failure to comply with the swap clearing requirement, as long as the other conditions for the end-user exception from clearing are fulfilled. In determining a BHC's or SLHC's total consolidated assets, the CFTC no-action letter specifies that each of its subsidiaries' assets are measured as of the last day of its most recent fiscal year.

<sup>1</sup> Dodd-Frank defines "financial entity" to include, among others, "a person predominantly engaged in activities that are in the business of banking, or in activities that are financial in nature," as defined in the Bank Holding Company Act.

<sup>2</sup> The CFTC used its statutory authority to extend the end-user exception to small depository institutions.

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The additional requirements for the end-user exception that must be met by small BHCs and SLHCs include:

- The excepted swap must be used by the BHC or SLHC to hedge or mitigate commercial risk.
- Certain information about the BHC's or SLHC's swap activity (including its eligibility for the end-user exception from clearing and how it meets its financial obligations associated with uncleared swaps) must be submitted to a CFTC-registered swap data repository either on a transaction-by-transaction basis by the party fulfilling Dodd-Frank's swap reporting requirement or on an annual basis by the BHC or SLHC.
- If the BHC or SLHC is, or is a subsidiary of, a public company or a company whose securities are registered with the Securities and Exchange Commission, an appropriate board committee must authorize the use of non-cleared swaps.

In issuing the no-action letter, the DCR recognized that the considerations behind the CFTC's rule allowing small banks and savings and loans to use the end-user exception largely apply to small BHCs and SLHCs as well, including the burden of fixed costs of clearing relative to the small number of swaps for these institutions.<sup>3</sup> In light of Dodd-Frank's principle of central clearing as a means for reducing systemic risk associated with swaps, the exception from clearing for non-financial end users, small banks and now small BHCs and SLHCs brings an important balance to the regulatory scheme arising out of Dodd-Frank.

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<sup>3</sup> We note that the issuance of CFTC Letter 16-02, which provides similar no-action relief to community development financial institutions (CDFIs), on the same day as CFTC Letter 16-01 suggests that the CFTC has acknowledged the burdens, financial and administrative, that clearing imposes on smaller institutions.

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