NOS Clearing

David A. Stawick
Secretary, Commodity Futures Trading Commission
Three Lafayette Center
1155 21st Street
Washington, DC 20581
USA

Your ref: Our ref: 2011-10-01 Date: 1 July 2011

Re: Effective Date for Swap Regulation, 76 Fed. Reg. 35,372 (June 17, 2011)

Dear Mr Stawick:

NOS Clearing ASA (**NOS**) is writing to the Commodity Futures Trading Commission (**CFTC** or the **Commission**) in response to the request for comment and notice of proposed order (the **Proposed Order**) in respect of extending the effective date for swap regulation under Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the **Dodd-Frank Act**).[1] NOS appreciates the hard work and dedication of the Commission and its staff in the difficult task of drafting extensive regulations under very tight time pressure, and applauds the Commission for making the sensible decision to delay implementation of certain elements of the Dodd-Frank Act until the relevant rules are finalised. Nevertheless, NOS wishes to express its concern that the Proposed Order does not sufficiently address the applicability of the provisions added to the Commodity Exchange Act, as amended (**CEA** or the **Act**) mandating that derivatives clearing organizations (**DCOs**) may not clear swaps unless they are registered with the Commission.

More broadly, NOS notes that neither the Proposed Order, nor any other Commission rulemaking proposals, meaningfully address the extraterritorial impact of the Dodd-Frank Act on non-US DCOs, in particular amended Section 5b(h) of the CEA authorising the Commission to exempt from registration those non-US DCOs that are subject to 'comparable, comprehensive' regulation in their home jurisdiction.

1. NOS

NOS is a Norwegian clearinghouse that specialises in the clearing of over-the-counter (**OTC**) and MTF-traded freight, energy, environmental and seafood derivatives. Many of the OTC freight products cleared by NOS fall within the definition of "swap" included in Section 1a(47) of the CEA. NOS is authorised by the Norwegian Ministry of Finance to provide clearing services pursuant to the Norwegian Securities Trading Act of June 29, 2007. Ongoing supervision and regulation of NOS's clearing activities is the responsibility of the Norwegian financial supervisory authority (***Finanstilsynet***). Norway is part of the European Economic Area (**EEA**) and the internal financial market of the European Union (**EU**). NOS will become subject to the proposed European Market Infrastructure Regulation (**EMIR**), once adopted, which is the EU's intended regulatory framework for OTC derivatives, central counterparties and trade repositories.

As part of its swaps clearing activities, NOS occasionally clears for traders located in the United States or customers located in the United States acting through foreign brokers. In connection with these clearing activities with a US nexus, NOS has previously received an order from the Commission allowing it to operate as a multilateral clearing organization (**MCO**) for the purposes of clearing OTC freight

[1] Effective Date for Swap Regulation, 76 Fed. Reg. 35,372 (June 17, 2011).

derivatives.[2] In addition, NOS's business operations and regulation by *Finanstilsynet* were reviewed in connection with the Commissions' foreign board of trade (**FBOT**) no-action letter issued to the International Maritime Exchange ASA (**Imarex**) in May 2010.[3]

2. TREATMENT OF DCOs CLEARING SWAPS

For the reasons set out below, NOS does not believe that the Proposed Order provides sufficient legal certainty regarding the applicability of the registration requirements for non-US DCOs clearing swaps that have a US nexus as of 16 July 2011. Section 754 of the Dodd-Frank Act generally provides that the provisions contained therein become effective 360 days from enactment (i.e., 16 July 2011) or alternatively, 'to the extent a provision...requires a rulemaking', each such provision will take effect not less than 60 days following publication of a final rule. Accordingly, the Proposed Order arranges the provisions of Title VII of the Dodd-Frank Act into four separate categories, the second and third of which are 'self-effectuating provisions that reference terms that require further definition' and 'self-effectuating provisions that do not reference terms that require further definition', respectively.

In the Proposed Order, the Commission proposes extending the effective date for those provisions of the Dodd-Frank Act falling into the second category above, on the basis that such provisions rely on terms for which the Commission must finalise definitions. However, the discussion of this second category casts doubt on whether the implementation deadline can be extended for amended Section 5b(a) of the CEA, which prohibits a DCO from clearing swaps without first registering with the Commission.[4] The Commission appears to feel its discretion is limited by the provisions of amended Section 4(c) of the CEA, which prohibits the Commission from issuing exemptions under certain sections of the CEA, including amended Section 5b(a).

NOS respectfully believes that the statutory text does not mandate such an outcome. A reasonable reading of amended Section 5b(a) could lead to the conclusion that, because the provision clearly relies on the definition of 'swap', it plainly falls within the second category of provisions benefiting from the extended effective date in the Proposed Order. In addition, NOS believes that the Commission could permissibly determine that Section 754 of the Dodd-Frank Act, not amended Section 4(c) of the CEA, is the controlling text regarding effective dates. On this reading, the Commission could justifiably conclude – rightfully, in NOS's view – that, because amended Section 5b(a) relies on the definition of 'swap', it 'requires a rulemaking' and therefore falls within the second category in the Proposed Order. In addition, such a reading recognises that, although the Commission has the authority under amended Section 5b(h) of the CEA to exempt non-US DCOs clearing swaps with a US nexus from DCO registration, any such non-US DCO could not request an exemption from DCO registration until the rules implementing the DCO core principles are finalised; hence the implementation of the provisions of the Dodd-Frank Act regarding such non-US DCOs implicitly 'requires a rulemaking'. Accordingly, NOS urges the Commission to reconsider the basis for its tentative conclusions in footnote 15 of the Proposed Order regarding the effective date for amended Section 5b(a).

Should the Commission be uncomfortable with the statutory reading presented above, the Commission should consider pursuing an different means of providing temporary relief from the registration requirement for non-US DCOs clearing swaps

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[2] Recognition of Multilateral Clearing Organizations, 67 Fed. Reg. 2,419 (January 17, 2002).
[3] Letter from Richard Shilts, Director of the Division of Market Oversight, to Carolyn Jackson, Allen & Overy LLP, CFTC No-Action Letter No. 10-20 (May 11, 2010).
[4] Footnote 15 of the Proposed Order.

with a US nexus. NOS notes that the staffs of the Division of Clearing and Intermediary Oversight and the Division of Market Oversight have published a draft staff no-action letter stating that the staffs would not recommend an enforcement action against persons that, *inter alia*, are in violation of amended Section 5b(a) as of 16 July 2011.[5] Such a no-action letter, if issued, would provide a minimal amount of legal certainty to non-US DCOs clearing swaps with a US nexus, however NOS would urge the Commission to consider issuing a determination or a Commission-level no-action letter to provide greater legal and regulatory robustness to the relief provided.

3. EXTRATERRITORIALITY

In addition to recommending that the Commission provide relief from the provisions of amended Section 5b(a) of the Act in the Proposed Order or via a no-action letter as described above, NOS is also writing to urge the Commission to more directly address the extraterritoriality impact of the Dodd-Frank Act and the significant uncertainty such potential impact creates for non-US DCOs with a US nexus to their swaps clearing business, such as NOS. Currently, NOS is subject to a considerable level of legal uncertainty regarding its compliance obligations under the Dodd-Frank Act beyond the question of effective dates discussed above.

In the first instance, amended Section 2(i) provides that the provisions of the CEA shall not apply to activities outside the United States unless such activities have a 'direct and significant connection with activities in or effect on' US commerce. However, the CFTC has not yet given any substantive guidance on the meaning of the phrase 'direct and significant connection'. For example, NOS notes that many of its clearing members are subsidiaries of US financial institutions. It is not yet clear the extent to which the non-US derivatives business of such non-US subsidiaries would be caught by the Dodd-Frank Act, and what effect that may have on clearing activities of such non-US subsidiaries with NOS.[6] A number of non-US entities have already asked the Commission for clarification on the meaning of amended Section 2(i) of the CEA and it is not acceptable that the Commission will address the effective dates of the provisions of the Dodd-Frank Act without simultaneously addressing the extraterritorial impact of those provisions.

Beyond asking the Commission to clarify the threshold question of the extraterritorial reach of the CEA's jurisdiction, NOS is also concerned about the lack of clarity under the CEA for non-US entities that have previously relied on forms of relief available on the basis of mutual recognition that will no longer be available once the Dodd-Frank Act is effective. For example, NOS has received an order that it may operate an MCO for clearing OTC derivatives, however Section 740 of the Dodd-Frank Act abolishes MCOs. Similarly, NOS has offered clearing for US customers acting through non-US brokers that rely on Part 30.10 of the CFTC's rules and therefore are not required to register as futures commission merchants (**FCMs**). NOS understands that the Commission staff does not read the Dodd-Frank Act amendments to the CEA to permit foreign brokers clearing swaps for US customers to rely on Part 30.10 relief; instead, such foreign brokers will be required to register as FCMs.[7] Given that NOS's swaps clearing business has until now relied on provisions of the CEA and

[5] A draft of this letter has been made publicly available at: http://www.cftc.gov/ucm/groups/public/@newsroom/documents/file/noaction061411.pdf

[6] NOS notes in this regard the letter sent on May 17, 2011 from several members of Congress to the Chairman of the CFTC, the Chairman of the Federal Reserve Board, the Chairman of the Federal Deposit Insurance Corporation and the Acting Comptroller of the Currency expressing their view that the non-US derivatives business of non-US subsidiaries of US financial institutions should not be subject to the Dodd-Frank Act's margin requirements.

[7] NOS notes that amended Section 1a(28)(B) of the CEA gives the Commission the authority to issue rules or regulations to exclude certain persons from the definition of FCM. NOS would encourage the Commission to consider issuing rules for foreign brokers and non-US DCOs clearing swaps with a US nexus that would provide relief similar to the long-standing and successful Part 30.10 regime for foreign brokers and non-US DCOs trading and clearing commodity futures and options.

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CFTC rules that will not be available once the Dodd-Frank Act takes effect, it is essential that the Commission provide greater clarity regarding the extraterritorial reach and scope of the Dodd-Frank Act so that NOS can prepare accordingly and adjust its swaps clearing business model if necessary.

One way to provide NOS with greater clarity under the CEA would be for the Commission to elaborate a robust framework to give effect to the provisions of amended Section 5b(h) of the CEA, which provides in pertinent part:

> *'The Commission may exempt, conditionally or unconditionally, a [DCO] from registration...for the clearing of swaps if the Commission determines that the [DCO] is subject to comparable, comprehensive supervision and regulation by...the appropriate government authorities in the home country of the organization...'*

This language expressly allows the CFTC to adopt a mutual recognition framework for the regulation of non-US DCOs clearing swaps with a US nexus. The CFTC has historically been a leader in global mutual recognition initiatives through its MCO orders, its Part 30.10 relief program as well as through the vetting of foreign regulatory regimes in the context of FBOT no-action letters. As noted above, NOS has received an order permitting it to operate an MCO and the regulation of the derivatives markets by the *Finanstylsinet* was reviewed in the context of the Imarex FBOT letter.

Accordingly, the Norwegian derivatives regulatory framework, equal to that of the EU, is an excellent candidate to qualify as offering 'comparable, comprehensive' supervision and regulation under amended Section 5b(h) of the CEA. The Commission may attach additional conditions to any relief it provides pursuant to Section 5b(h), however the existing mutual recognition of foreign jurisdictions – including that of Norway as discussed above – provides a sound, practical basis for establishing a workable mutual recognition framework for non-US DCOs that clear swaps. In light of the urgency need for non-US DCOs clearing swaps to obtain additional clarity regarding their status under the Dodd-Frank Act, NOS respectfully submits that the Commission consider explicitly addressing extraterritoriality and mutual recognition for non-US DCOs clearing swaps, either in the final text of the Proposed Order or in a separate Commission issuance published simultaneously.

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NOS applauds the Commission's sensible steps to address the effective date of the Dodd-Frank Act's rulemakings and appreciates the opportunity to provide our views on several additional areas where the Commission should take action. Please feel free to contact me or General Counsel Mr. Gaute S. Gravir (gsg@imarexgroup.com) with any questions.

Sincerely,

Morten Erichsen
Managing Director