Dodd–Frank and inter–affiliate trading of derivatives

Impact of new derivatives regulations becomes clearer, but key questions remain

What you need to know

Global impact
Both US and non-US domiciled companies with inter-affiliate derivatives and/or CTEs are potentially affected. Derivatives regulations being implemented in foreign jurisdictions create further complexity.

Making certain elections to accept available regulatory relief could inadvertently increase the impact - even for non-US entities within an organization.

Time to act?
Recordkeeping requirements are already in effect. Clearing and reporting requirements could go into effect in the late summer or early fall of 2013.

It is recommended that companies act now to assess the impact of the new regulations and determine how they will comply with the requirements and take advantage of exemptions that may be available.

Executive summary

• Companies that have derivative trades between affiliates, especially those that have established centralized treasury entities (CTEs) to consolidate exposure and hedging requirements, must consider the impact of new regulations for over the counter (OTC) derivatives being implemented in the US and elsewhere.
• These new regulations include mandatory clearing, trading, margining and trade data reporting; key compliance deadlines are set in the 2nd and 3rd quarters of 2013.
• Title VII of The Wall Street Reform and Consumer Protection Act (Dodd-Frank Act Title VII or Title VII) did not include a categorical exemption from new regulations for inter-affiliate/intra-group derivatives (collectively referred to below as “inter-affiliate” derivatives); similarly, there was no broad statutory exemption provided for centralized hedging entities.
• In several cases the regulators have provided guidance, exemptions and no-action relief with respect to the applicability of some of the new regulatory requirements, but there are numerous conditions and other limitations that must be considered.
• An exemption to clearing is available for trades executed by qualifying CTEs for the sole purpose of hedging or mitigating risk of related affiliates if several conditions are met, including that the CTE’s payment obligation exposures must be guaranteed by a parent or certain affiliated companies.
• The impact of new regulatory requirements and availability of new exemptions are complicated and require that corporate end users make several determinations and decisions with respect to compliance with the new rules.
• There are several key open questions regarding the impact of new regulations on centralized hedging/trading entities and inter-affiliate derivatives, including
  • Whether certain trades qualify as hedges
  • Whether the CTE is a “financial entity” under Title VII
  • Whether a financial centralized hedging entity is able to elect the end-user exception on behalf of its non-financial affiliate
  • The extent to which Title VII will apply to cross-border derivatives
  • The impact of new derivatives regulations being implemented abroad

This article and appendices discuss a number of the specific technical and business considerations that a company must navigate. However, the specific circumstances of your company’s activities may require additional analysis to reach the appropriate compliance decisions.
**Overview**

**Background**

Over the past several years, many large multinational companies have moved toward centralizing their hedging and derivatives trading operations through the use of CTEs. Among various other treasury-related functions, these CTEs enter into derivative trades with affiliated entities (i.e., inter-affiliate or intra-group derivatives) and then execute offsetting derivative trades with external, unaffiliated counterparties (e.g., dealers or market makers). The advantages of doing so are numerous, including having a comprehensive view of risk and liquidity across portfolios, centralized risk management, savings in collateral posted, reduced transactions costs, and other tax and accounting benefits.

However, companies that have set up centralized hedging and trading programs, or those that may be looking to do so, must now consider the impact of new regulations for derivatives being implemented in the US under the Dodd Frank Act. These new regulations include potential mandatory clearing, trading, collateralization and reporting requirements for the vast majority of OTC derivatives. While some may find it surprising that new regulations affect the execution of derivatives internally or out of CTEs, even when such CTEs are not domiciled in the US, there are a number of key factors that businesses need to consider in order to become compliant when the new rules becomes mandatory.

### Inter-affiliate swaps and CFTC rulemaking: recent developments

On April 1, 2013, the Commodity Futures Trading Commission (CFTC or the Commission) approved a final rule that allows a narrow exemption to clearing for swaps between affiliated counterparties if they meet specific requirements.

On April 5, 2013, the CFTC released no-action letter 13-09

On June 4, 2013, the Commission issued an additional no-action relief to clearing for eligible treasury affiliates (letter 13-22), but strict conditions need to be met, including approval from the treasury affiliate’s board.

These releases are complex and impact the availability of exemptions to the clearing and reporting requirements; you should carefully consider your firm’s unique circumstances in assessing the impact.

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### Regulators provide partial relief and guidance for inter-affiliate derivatives

Ever since the US regulators began issuing final regulations implementing the Dodd-Frank Act Title VII derivatives reforms, end users with CTEs, or who engage in trading of inter-affiliate derivatives, have been advocating for relief from the many disparate provisions that impact those internal derivatives. While those efforts have had beneficial results to some extent, the relief granted has not been as broad as many have hoped. In fact, rather than provide a categorical exemption from Dodd-Frank for all internal swaps transactions, the regulators have addressed the application of those rules on inter-affiliate transactions on a rule-by-rule basis. For those engaging in inter-affiliate derivatives, this piecemeal approach has created some compliance challenges.

For example, in the guidance accompanying the final swap recordkeeping and reporting requirements published in January 2012, the CFTC clarified that such requirements would apply to inter-affiliate derivatives but that the real-time reporting requirements, whereby pricing information for trades is disseminated publicly, would not apply if certain conditions were met. Similarly, the CFTC and the Securities and Exchange Commission (SEC) clarified that market participants would not need to aggregate the exposure from swaps executed with affiliates, subject to certain conditions, for purposes of performing the major swap participant (MSP) exposure calculations, nor would a swap executed with an affiliate be deemed to be “dealing” or “market making” for purposes of the swap dealer (SD) definition.

In early April 2013, the CFTC finalized a rule and released two no-action letters that were requested by end users and were expected to clarify whether key new clearing and reporting requirements apply to inter-affiliate derivatives. The releases are riddled with complexity and are, in key aspects, dependent upon on other rules, some of which are not final. This interrelatedness makes assessing the applicability of new requirements and eligibility for the relief a necessity for firms transacting inter-affiliate swaps, especially for those entering into inter-affiliate trades across national borders. Beyond the question of whether clearing and reporting applies, the releases present end users with various options regarding, first, whether to use the end-user exception from clearing or the inter-affiliate swap exemption from clearing, and second, whether to report inter-affiliate swaps or external swaps. Which option an end user chooses depends on a variety of business factors, as we discuss below.

In early June, the CFTC issued another non-time limited no-action letter from clearing requirements for swaps entered into by CTEs. There are several concepts of particular interest in the release. First, the no-action is designed for CTEs not able to claim exceptions or exemptions under other relief, which the staff indicates would cover entities defined as “financial entities.”

This relief specifies that the CTE is a financial entity as defined in Section 2(h)(7)(C)(vii) of the CEA — meaning that a CTE utilizing this relief has designated itself as a financial entity under Dodd Frank. Second, the CTE cannot net swaps from non-financial and financial affiliates before entering into outward-facing swaps. Third, the CTE’s unsecured credit risks must be guaranteed by a parent or specified other related entities. Many CTEs may not have existing credit guarantees from affiliates or parents. Similar to the end-user exception, the CTE must also comply with election and reporting requirements by September 9, 2013.

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1. See the final rule, Clearing Exemption for Swaps Between Certain Affiliated Parties (17 CFR Part 50).
6. SDs and MSPs are required to register with the CFTC and are subject to more substantial new regulatory requirements than other market participants.
7. See final rule for End-User Exception to the Clearing Requirement for Swaps (17 CFR part 139).
8. Letter 13-22, see note 4 supra.
9. Letter 13-22, see note 4 supra.
Details of the regulatory actions

CFTC final rule exempting certain inter-affiliate swaps from mandatory clearing and trading requirements and no-action letter providing exemptive clearing relief for inter-affiliate transactions under certain circumstances – April 1 and June 4, 2013

On April 1, 2013, the CFTC approved a final rule providing a "narrowly tailored" exemption from the mandatory clearing requirements if the affiliated counterparties to a swap meet certain eligibility requirements. While it may not be necessary for an end user to elect the inter-affiliate clearing exemption, as the swap may already be exempt from electing the more general end-user exception, there are still implications on how such transactions are monitored and reported, especially if such trades take place between a US and non-US affiliates. Regardless, if the end-user exception is not available (e.g., if a swap does not qualify as a hedge of commercial risk or if it is executed between two financial entities as defined for purposes of the end-user exception rules), then the inter-affiliate clearing exemption is the only relief from the clearing mandate.

Under the recently finalized rules, an inter-affiliate swap is eligible for an exemption to mandatory clearing if either one of the counterparties to the affiliate swap directly or indirectly owns a majority interest in the other, or if they are both under common majority ownership of a third entity, and if that the majority-owning entity reports its financial statements on a consolidated basis under GAAP or IFRS reporting. In addition, the final rule stipulates a number of requirements that must be met, including:

- Both counterparties must elect not to clear the swap.
- The affiliates must have in writing a swap trading relationship document that includes all terms governing the relationship between them.
- The inter-affiliate swap must be subject to a centralized risk management program that is reasonably designed to monitor and manage the risks of the swap.
- Swaps entered into (by either affiliated counterparty) with an unaffiliated third party to hedge the risk associated with the exempted trade must comply with applicable US or comparable non-US clearing requirements or be eligible for US or comparable non-US exemptions to clearing.

Furthermore, when the inter-affiliate swap exemption is elected, the reporting party should provide to a swap data repository (SDR), or to the CFTC if no SDR is available to accept the information, a confirmation that both affiliates satisfy the additional conditions above. Optionally, in regulations similar to those applicable to the end-user exception to clearing, each affiliate may report, on an annual basis in anticipation of electing the inter-affiliate swap exemption in the following 365 days for one or more swaps, how each of the affiliate counterparties will generally meet its financial obligations for non-cleared swaps (such as a written credit support agreement, pledged or segregated assets, collateral as part of a credit support annex, a written guarantee or other means). Also similar to the end-user exception rules, if an electing affiliate counterparty is an SEC-filing entity, it should provide the relevant SEC central index key number and an acknowledgment that an appropriate committee of the board of directors (or equivalent body) has reviewed and approved the decision to enter into swaps that are exempt from the mandatory clearing and trading requirements.

Nevertheless, many companies with CTEs would not be able to use the exemption. Depending on the type of activity and structure of the inter-affiliate transactions, many CTEs could be considered financial entities and therefore excluded from the scope of the clearing exemption. This exclusion had the potential of making companies choose between the efficiency of central portfolio management and the bilateral credit management.

On June 4, 2013, in response to a number of inquiries received, many of which citing that CTEs are financial entities that exist solely to consolidate, hedge and mitigate commercial risks of other affiliates, the CFTC released a targeted no-action relief (letter 13-22) for certain eligible treasury affiliates that meet a five-part definitional test and a five-part general conditions test, the details of which can be found in Appendix 2.

In particular, in order to qualify, the CTE must not be wholly or majority-owned by a financial entity; be affiliated with an SD, an MSP or a nonbank financial company that is designated as systemically important; and not be a bank or insurance company, among other requirements. Furthermore, the CTE must only engage in swaps that hedge or mitigate the commercial risk of its affiliates, and it cannot have swaps with any affiliate that is a financial entity.

In addition, CTEs that elect this no-action relief must meet requirements similar to those under the end-user exception to clearing, including for SEC filers the need to obtain board approval to elect the exemption to clearing. As with the other no-action relief offered, this does not exempt the electing counterparty from recordkeeping requirements under Part 43, 45 or 46.

Reporting requirements – non-SD, non-MSP financial entities

<table>
<thead>
<tr>
<th>Reporting deadline for interest rate and credit swaps (unchanged)</th>
<th>May 29, 2013</th>
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</thead>
<tbody>
<tr>
<td>Backload FX, commodity, equity swaps between April 10 and May 29, 2013</td>
<td>June 29, 2013</td>
</tr>
<tr>
<td>New deadline for initial reporting of FX, commodity, equity swaps</td>
<td>Sept 30, 2013</td>
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<tr>
<td>Report historical swap data under Part 46</td>
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</tbody>
</table>
Additional no-action relief from reporting requirements for certain inter-affiliate swaps – April 5 and April 9, 2013

In addition to the final rule and the June 4 no-action letter discussed above, the Commission has released two no-action letters that, while granting relief in some respects, require companies to thoroughly evaluate the impact stemming from a complex set of decisions and fact patterns.

On April 5, 2013, the CFTC granted no-action relief (letter 13-09) from Part 45 prospective reporting requirements, Part 46 historical reporting requirements, and the new Part 50 reporting requirements noted above related to reporting certain affiliate exemption data to SDRs, for certain inter-affiliate swaps between non-SD/MSP affiliated counterparties. Specifically, in cases where one affiliate is a majority – or wholly owned subsidiary of the other (whether direct or indirect), or if both are under common ownership, swaps transacted between the two affiliates need not be reported by the April 10, 2013, deadline established earlier by the CFTC. Importantly, among other requirements, neither of the affiliated counterparties under that no-action relief can be a financial entity, SD, MSP, or otherwise deemed a systemically important financial institution, and the swap must not have been executed on an exchange or regulated trading platform or submitted for clearing. In addition, entities are still subject to the recordkeeping requirements of Part 45, and all swaps with external counterparties must be reported to an SDR regardless of the location of the affiliated counterparty. For a detailed list of these requirements, refer to Appendix 1.

Also, on April 9, 2013, the CFTC released a more general but time-limited no-action letter (letter 13-10) providing relief from reporting requirements for almost all swaps between non-SD/MSP entities, not just among affiliates. This relief, available to non-SDs and non-MSPs, extends the date by which swaps would be required to be reported to an SDR; however, it does not exempt them from recordkeeping requirements, as the swaps transacted during the relief period would have to be reported or backloaded at a later date.

The relief provided in the April 9 no-action letter varies depending on whether one of the non-SD/MSP parties is a financial entity, as defined under Title VII of Dodd-Frank. The deadlines for reporting swaps between entities where neither is an SD or MSP, but one of which is a financial entity, is extended from April 10, 2013, as follows:

- For foreign exchange (FX), commodity, and equity swaps, until 12:01 a.m. on May 29, 2013, on the condition that before 12:01 a.m. on June 29, 2013, the financial entity backloads and reports all transaction data, for the period from April 10, 2013, to May 29, 2013, that would have been required to be reported by the financial entity absent the no-action relief.
- In addition, for reporting historical swap transaction data pursuant to Part 46, the deadline is extended until 12:01 a.m. on September 30, 2013.

The deadline for reporting interest rate and credit default swaps was not changed from April 10, 2013, as the CFTC felt that the financial entities engaged in these trades are more likely to have systems in place to facilitate such reporting. In addition, for a swap between a financial entity and a non-financial entity, the financial entity would be required to satisfy the reporting obligation so long as the non-financial entity is a US person.

The deadlines for reporting swaps between non-financial entities neither of which is an SD or MSP is extended from April 10, 2013, as follows:

- For interest rate and credit swaps, until July 1, 2013, on the condition that, by 12:01 a.m. on August 1, 2013, the non-financial counterpart party that has been appointed the reporting party backloads and reports to an SDR all transaction data, for the period from April 10, 2013, to July 1, 2013, that the party would have been required to report absent the no-action relief.
- For FX, commodity and equity swaps, until 12:01 a.m. on August 19, 2013, on the condition that before 12:01 a.m. on September 19, 2013, the non-financial counterpart party that has been appointed the reporting party report to an SDR all transaction data, for the period of April 10, 2013, to August 19, 2013, that the reporting party would have been required to report absent the no-action relief.
- In addition, the deadline for reporting historical swap transaction data pursuant to Part 46 is now extended until 12:01 a.m. on October 31, 2013.

It is important to note that the April 9 no-action letter does not grant any relief from the recordkeeping requirements under the Part 43, Part 45 and Part 46 rules regardless of whether both parties to the swap are non-financial entities.

**Reporting requirements – non-SD, non-MSP non-financial entities**

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<thead>
<tr>
<th>April</th>
<th>May</th>
<th>June</th>
<th>July</th>
<th>August</th>
<th>Sept</th>
<th>Oct</th>
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<tbody>
<tr>
<td>April 10, 2013</td>
<td>Original deadline</td>
<td></td>
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<tr>
<td>July 1, 2013</td>
<td>Backload interest rate and credit swaps data between April 10 and July 1</td>
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<tr>
<td>August 1, 2013</td>
<td>Backload interest rate and credit swaps data between April 10 and August 19</td>
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</tr>
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<td>Sept 19, 2013</td>
<td>Report historical swap data under Part 46</td>
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<td>Aug 19, 2013</td>
<td>Report FX, commodity, equity swaps</td>
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</tbody>
</table>
Questions and considerations for selecting your compliance path

Navigating these rules means that companies must make a number of important decisions regarding whether a trade is eligible for the end-user exception from clearing and eligible for the inter-affiliate swap exemption from clearing, whether to report inter-affiliate swaps or external swaps. Which option an end user chooses depends on a variety of business and legal factors. End users should consider the types of instruments that are traded (e.g., whether they involve the initial category of interest rate and credit swaps or they involve foreign exchange, commodity or equities only), as well as the location of non-US affiliates and the types of transactions they carry out.

**Do you transact inter-affiliate interest rate or CDS transactions (so-called covered swaps)?**

If yes, then you will need to address whether you are exempt from clearing, under either the end-user exception or the inter-affiliate clearing exemption, by as early as June 10, 2013 (the effective date of the exemption). Additionally, if you have non-US affiliates that have outward-facing transactions in jurisdictions other than the EU, Japan or Singapore, important additional conditions, such as required margining, may apply. If you do not have interest rate or credit default swaps, impacts from this issue on your inter-affiliate transactions will not occur until 2014 at the earliest.

**Do you have swaps between affiliates and a parent company/CTE?**

If yes, then the consideration is primarily on whether the parent entity or CTE is domiciled in the US or not. If you have cross-border inter-affiliate trades, your potential risks from the reporting exemption become much greater. For example, if you rely on the no-action relief on reporting requirements provided under the 13-09 letter and have non-US affiliates that execute outward-facing swaps, then you may become responsible for reporting all outward-facing swaps by your non-US affiliates. Indeed, the decision as to which reporting regime to accept will greatly impact your obligations.

**Do you have uncleared swaps between your CTE and third parties?**

If yes, then you have a two-part test to go through. First, is the CTE “predominantly engaged in activities of a financial nature, as defined by section 4(k) of the Bank Holding Act of 1956? This test is solely for the CTE as a standalone entity — it cannot include the activities of the rest of the firm in the analysis. If the answer is no, then the inter-affiliate clearing exemption is available. If the answer is yes, then no-action relief provided under the June 4 letter can apply if the CTE and its affiliate counterparties satisfy the definitional and five general conditions and reporting conditions for relief.

### Impact of decisions

<table>
<thead>
<tr>
<th>Chose end-user exception (ignore affiliate rules)</th>
<th>Chose inter-affiliate clearing exception</th>
<th>Chose inter-affiliate no action for reporting – no expiration date</th>
<th>Chose blanket no-action for reporting – time limited</th>
</tr>
</thead>
<tbody>
<tr>
<td>Only one-sided end-user exception applicability and election</td>
<td>Affiliate clearing exception must be applicable and elected by both affiliates</td>
<td>Does not cover SD, MSP or systemically important financial entity affiliates</td>
<td>Covers all non-SD/non-MSP entities – differing timing for financial and non-financial</td>
</tr>
<tr>
<td>Rule 43, 45 and 46 reporting on trades with a third party</td>
<td>Rule 45 and 46 reporting required</td>
<td>Does not cover trades via SEF, DCM, FBOT or transparent electronic markets</td>
<td>Requires Part 45 reporting retroactive to April 10, 2013, at expiration</td>
</tr>
<tr>
<td>No extension of reporting requirements to non-US affiliates</td>
<td>No extension of reporting requirements to non-US affiliate</td>
<td>Does not cover swaps or EFRPs (e.g., exchange for physicals) submitted for clearing</td>
<td>Differing time lines for differing products</td>
</tr>
<tr>
<td>Does not speak to margining</td>
<td>May require margining or clearing of outward-facing non-US trades</td>
<td>Does not cover swaps under inter-affiliate clearing exception</td>
<td>Does not reference inter-affiliate rules</td>
</tr>
<tr>
<td>Will not cover spec trading by US firm</td>
<td>Will not cover spec trading by US firm</td>
<td>Requires Part 43, 45 and 46 reporting of all third-party swaps by either affiliate</td>
<td>Does not export reporting to non-US affiliate</td>
</tr>
</tbody>
</table>
Areas requiring future actions or lacking clarity

While the regulators have provided guidance and relief regarding the key issues discussed above, there are several key open issues that will dictate the extent to which regulatory requirements apply to inter-affiliate derivatives and CTEs.

**US regulators' guidance on cross-border derivative trades:** the CFTC released proposed guidance on July 12, 2012, that sets forth the regulatory requirements that would apply to derivative trades that involve a US person, an affiliate of a US person, a US guarantor of a non-US entity’s trade, and a non-US entity that has registered as an SD or MSP under Title VII. On May 1, 2013, the SEC released their proposed guidance on the same topic, which gave greater deference to foreign regulations for certain cross-border derivative transactions. The final versions of these rules, yet to be released, and the extent to which there are differences will have an important impact on which specific Title VII regulatory requirements apply to cross-border derivative transactions and whether both Title VII and foreign regulations could apply to the same trades.

**Foreign derivatives regulations:** at the G-20 Summit in Pittsburgh in September 2009, all of the G-20 member nations pledged to coordinate efforts to regulate OTC derivatives. Since that time, several new laws have been passed, and rules are in the process of being implemented in the global financial centers through which the majority of derivatives trades are executed. While international regulators continue to coordinate, they have acknowledged that complete harmonization is impossible and that there are important differences between their approaches. Corporate end users that enter into derivative trades abroad will have to assess the impact of new foreign regulations in addition to those being implemented under Title VII.
Appendix 1 – relief under April 5 letter

No-action relief from “prospective” reporting requirements for inter-affiliate swaps between wholly owned affiliates

Swaps between wholly owned affiliates will not be subject to reporting requirements, subject to the following conditions:

- The relief is limited to swaps between affiliated counterparties where one of the following is true:
  - One affiliated counterparty, directly or indirectly, holds a 100% ownership interest in the other counterparty, and the affiliated counterparty that holds the 100% ownership interest in the other counterparty reports its financial statements on a consolidated basis under US GAAP or International Financial Reporting Standards (IFRS), and such consolidated financial statements include the financial results of the 100%-owned counterparty.
  - A third party, directly or indirectly, holds a 100% ownership interest in both affiliated counterparties, and the third party reports its financial statements on a consolidated basis under US GAAP or IFRS, and such consolidated financial statements include the financial results of both of the affiliated counterparties.

- The relief does not apply to any swap entered into by an affiliate that is an SD or MSP, is affiliated with an SD or MSP, or is affiliated with a financial company that has been designated as systemically important by the Financial Stability Oversight Council.

- The relief does not apply to any swap executed on an exchange or regulated trading platform (i.e., a designated contract market, swap execution facility, foreign board of trade or other trading platforms).

- The relief does not apply to any swap that is submitted for clearing (but note that the clearinghouse would be required to report such cleared swaps anyway).

- The relief does not apply for swaps for which both affiliated counterparties are systemically important by the Financial Stability Oversight Council.

- All swaps entered into between either one of the affiliates and an unaffiliated counterparty (i.e., for an external swap), regardless of the location of the affiliate counterparty, must be reported to an SDR pursuant to Parts 43, 45 and 46.

- An entity relying on this relief must maintain records according to Part 45 and must maintain an internally generated swap identifier for each swap subject to this relief.

- The relief does not apply to any swap that is required to be reported pursuant to real-time reporting under Part 43.

No-action relief from quarterly prospective reporting requirements for inter-affiliate swaps between majority-owned affiliates

Swaps between majority-owned affiliates will not be subject to reporting requirements, subject to the following conditions:

- The relief is limited to swaps between affiliated counterparties where one of the following is true:
  - One affiliated counterparty, directly or indirectly, holds a majority ownership interest in the other counterparty, and the affiliated counterparty that holds the majority ownership interest in the other counterparty reports its financial statements on a consolidated basis under US GAAP or IFRS, and such consolidated financial statements include the financial results of the majority-owned counterparty.

- A third party, directly or indirectly, holds a majority ownership interest in both affiliated counterparties, and the third party reports its financial statements on a consolidated basis under US GAAP or IFRS, and such consolidated financial statements include the financial results of both of the affiliated counterparties.

No-action relief from Part 46 historical reporting requirements for inter-affiliate swaps

The CFTC grants no-action relief from historical reporting requirements subject to the following conditions:

- The inter-affiliate swap must be between entities that are at least majority-owned, as defined above.

- The relief does not apply to any swap entered into by an affiliate that is an SD or MSP, is affiliated with an SD or MSP, or is affiliated with a financial company that has been designated as systemically important by the Financial Stability Oversight Council.

- The relief does not apply to any swap that is executed on an exchange or trading platform (as defined above).

- The relief does not apply to any swap that is submitted for clearing.

- The reporting counterparty must maintain records of historical swaps as required under Part 46 and must make such records available to the CFTC promptly upon request in a reportable form pursuant to Part 46 or in any other form that the CFTC may request.
Appendix 2 – relief under June 4 letter

In order to be eligible to elect the no-action relief, CTEs, or eligible treasury entities under the letter, are defined as having the following qualifications:

- The entity must have a non-financial parent, i.e., it is directly, wholly owned by a non-financial entity or by another eligible treasury entity, and it is not indirectly majority-owned by a financial entity.
- The entity cannot have a financial entity as the ultimate parent, and that more than half of all wholly and majority-owned affiliates within the corporate umbrella must qualify for the end-user exception to clearing under Part 50.
- The CTE is considered a financial entity solely as a result of its acting as principal to swaps with or on behalf of its related affiliates, or providing other services that are financial in nature to them.
- The CTE is not, and is not affiliated with, an SD, an MSP or a nonbank financial company that is deemed to be systemically important by the Financial Stability Oversight Council.
- The CTE is not a bank holding company, insured depository institution, credit union, commodity pool, a benefit plan, or an insurance company.

Furthermore, the CTE’s swaps activity must satisfy the following five general conditions:

- The CTE enters into the exempted swaps for the sole purpose of hedging or mitigating the commercial risk of its affiliates that was transferred to the CTE via inter-affiliate swaps.
- The CTE does not enter into any swaps that are not for the purpose of hedging or mitigating the commercial risk of its related affiliates.
- Neither the CTE itself, nor any of its related affiliates with whom the CTE has swaps, can enter into any swaps with or on behalf of any affiliates that is a financial entity (financial affiliates), nor can it otherwise assume, net or consolidate the risk of swaps entered into by its financial affiliates.
- Each swap executed by the CTE is subject to a centralized risk management program that is reasonably designed to monitor and manage the risks associated with the swap.
- The payment obligations of the CTE on the exempted swaps are guaranteed by its non-financial parent, by an entity that wholly owns or is wholly owned by the non-financial parent, or by the related affiliates for which the swap hedges or mitigates commercial risk.

If the CTE and its swaps activity satisfy both sets of requirements above, then, similar to the election of the end-user exception, the following information must be provided to an SDR or directly to the CFTC:

- Notice of the election of the exemption and confirmation that the electing counterparty satisfies the five general conditions from above.
- How the electing counterparty generally meets its financial obligations when it enters into uncleared swaps, by one or more of the following:
  - A written credit support agreement.
  - Pledged or segregated assets (including the posting and receiving of margin under a credit support agreement).
  - A written guarantee from another party.
  - The electing counterparty’s available resources.
- Means other than the above.
- If the electing counterparty is an SEC filer.
- The relevant SEC Central Index Key number.
- An acknowledgement that an appropriate committee of the board of directors (or equivalent body) of the electing counterparty has reviewed and approved the decision to use the clearing exemption.

If there is more than one electing counterparty to a swap, then the information above needs to be provided for each of the electing counterparties. The information above may be reported annually in anticipation of electing the relief for one or more swaps, and any material changes to the information during the 365 days following reporting should be reported as well. Furthermore, each reporting counterparty needs to have a reasonable basis to believe that the electing counterparty meets all the general conditions above.

Learn more

To learn more about our experience advising companies on new derivatives regulations, please contact one of the following Ernst & Young LLP professionals.

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