

Business at the same time and on the same terms and conditions.

(iii) You and the Associate investment fund are providing follow-on financing to the Small Business at the same time, on the same terms and conditions, and in the same proportionate dollar amounts as your respective investments in the previous round(s) of financing (for example, if you invested \$2 million and your Associate invested \$1 million in the previous round, your respective follow-on investments would be in the same 2:1 ratio).

\* \* \* \* \*

(g) *Public notice.* Before granting an exemption under this § 107.730, SBA will publish notice of the transaction in the **Federal Register**.

#### § 107.855 [Amended]

5. Amend § 107.855 by removing paragraph (g)(10) and redesignating current paragraphs (g)(11) through (g)(13) as (g)(10) through (g)(12).

Dated: October 6, 2010.

**Karen G. Mills,**  
*Administrator.*

[FR Doc. 2010-25729 Filed 10-13-10; 8:45 am]

BILLING CODE 8025-01-P

## COMMODITY FUTURES TRADING COMMISSION

### 17 CFR Parts 39 and 140

RIN 3038-AC98, 3038-AD02

### Financial Resources Requirements for Derivatives Clearing Organizations

**AGENCY:** Commodity Futures Trading Commission.

**ACTION:** Notice of proposed rulemaking.

**SUMMARY:** The Commodity Futures Trading Commission (Commission or CFTC) is proposing rules to implement new statutory provisions enacted by Title VII and Title VIII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). The proposed regulations establish financial resources requirements for derivatives clearing organizations (DCOs) for the purpose of ensuring that they maintain sufficient financial resources to enable them to perform their functions in compliance with the Commodity Exchange Act and the Dodd-Frank Act.

**DATES:** Submit comments on or before December 13, 2010.

**ADDRESSES:** You may submit comments, identified by RIN number, by any of the following methods:

- *Federal eRulemaking Portal:* <http://www.regulations.gov>. Follow the instructions for submitting comments.

- *Agency Web Site:* <http://www.cftc.gov>. Follow the instructions for submitting comments on the Web site.

- *E-mail:* [DCOSIDCOfinres@cftc.gov](mailto:DCOSIDCOfinres@cftc.gov). Include the RIN number in the subject line of the message.

- *Fax:* 202-418-5521.

- *Mail:* David A. Stawick, Secretary of the Commission, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW., Washington, DC 20581.

- *Hand Delivery/Courier:* Same as mail above.

All comments must be submitted in English, or if not, accompanied by an English translation. Comments will be posted as received to <http://www.cftc.gov>. You should submit only information that you wish to make available publicly. If you wish the Commission to consider information that may be exempt from disclosure under the Freedom of Information Act, a petition for confidential treatment of the exempt information may be submitted according to the established procedures in CFTC Regulation 145.9.<sup>1</sup>

**FOR FURTHER INFORMATION CONTACT:** John C. Lawton, Deputy Director and Chief Counsel, 202-418-5480,

[jlawton@cftc.gov](mailto:jlawton@cftc.gov), Phyllis P. Dietz, Associate Director, 202-418-5449, [pdietz@cftc.gov](mailto:pdietz@cftc.gov), or Eileen A. Donovan, Special Counsel, 202-418-5096, [edonovan@cftc.gov](mailto:edonovan@cftc.gov), Division of Clearing and Intermediary Oversight, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21 Street, NW., Washington, DC 20581.

#### SUPPLEMENTARY INFORMATION:

##### I. Background

###### A. Title VII

On July 21, 2010, President Obama signed the Dodd-Frank Act.<sup>2</sup> Title VII of the Dodd-Frank Act<sup>3</sup> amended the Commodity Exchange Act (CEA)<sup>4</sup> to establish a comprehensive regulatory framework to reduce risk, increase transparency, and promote market integrity within the financial system by, among other things: (1) Providing for the registration and comprehensive regulation of swap dealers and major swap participants; (2) imposing clearing and trade execution requirements on

<sup>1</sup> Commission regulations referred to herein are found at 17 CFR Ch. 1.

<sup>2</sup> See Dodd-Frank Wall Street Reform and Consumer Protection Act, Public Law 111-203, 124 Stat. 1376 (2010). The text of the Dodd-Frank Act may be accessed at <http://www.cftc.gov/LawRegulation/OTCDERIVATIVES/index.htm>.

<sup>3</sup> Pursuant to Section 701 of the Dodd-Frank Act, Title VII may be cited as the "Wall Street Transparency and Accountability Act of 2010."

<sup>4</sup> 7 U.S.C. 1 *et seq.*

standardized derivative products; (3) creating rigorous recordkeeping and real-time reporting regimes; and (4) enhancing the Commission's rulemaking and enforcement authorities with respect to all registered entities and intermediaries subject to the Commission's oversight.

Section 725(c) of the Dodd-Frank Act amends Section 5b(c)(2) of the CEA, which sets forth core principles with which a DCO must comply to be registered and to maintain registration as a DCO.

The core principles were added to the CEA by the Commodity Futures Modernization Act of 2000 (CFMA).<sup>5</sup> Consistent with the CFMA's principles-based approach to regulation, the Commission did not adopt implementing rules and regulations, but instead promulgated guidance for DCOs on compliance with the core principles.<sup>6</sup> However under Section 5b(c)(2), as amended by the Dodd-Frank Act, Congress expressly confirmed that the Commission may adopt implementing rules and regulations pursuant to its rulemaking authority under Section 8a(5) of the CEA.<sup>7</sup>

The Commission continues to believe that, where possible, each DCO should be afforded an appropriate level of discretion in determining how to operate its business within the statutory framework. At the same time, the Commission recognizes that specific bright-line regulations may be necessary in order to facilitate DCO compliance with a given core principle, and ultimately, to protect the integrity of the U.S. clearing system. Accordingly, in developing the proposed regulation, the Commission has endeavored to strike an appropriate balance between establishing general prudential standards and prescriptive requirements.

Core Principle B, as amended by the Dodd-Frank Act, requires a DCO to possess financial resources that, at a minimum, exceed the total amount that would enable the DCO to meet its financial obligations to its clearing members<sup>8</sup> notwithstanding a default by

<sup>5</sup> See Commodity Futures Modernization Act of 2000, Public Law 106-554, 114 Stat. 2763 (2000).

<sup>6</sup> See Appendix A to Part 39, 17 CFR Part 39. The Commission notes that it intends to propose removal of Appendix A, in its entirety, as part of a future proposed rulemaking.

<sup>7</sup> Section 8a(5) of the CEA authorizes the Commission to promulgate such regulations as, in the judgment of the Commission, are reasonably necessary to effectuate any of the provisions or to accomplish any of the purposes of the CEA.

<sup>8</sup> The term "clearing members" refers to entities that have a direct financial relationship to a DCO, regardless of the DCO's organizational structure,

the clearing member creating the largest financial exposure for the DCO in extreme but plausible market conditions; and enable the DCO to cover its operating costs for a period of 1 year, as calculated on a rolling basis. The Commission is proposing to adopt Regulation 39.11 to establish requirements that a DCO will have to meet in order to comply with Core Principle B.

### B. Title VIII

Section 802(b) of the Dodd-Frank Act states that the purpose of Title VIII is to mitigate systemic risk in the financial system and to promote financial stability. Section 804 authorizes the Financial Stability Oversight Council (Council) to designate entities involved in clearing and settlement as systemically important.<sup>9</sup>

Section 805(a) of the Dodd-Frank Act allows the Commission to prescribe regulations for those DCOs that the Council has determined are systemically important. The Commission is also proposing to adopt some additional or enhanced requirements for systemically important DCOs (SIDCOs).

The Commission requests comment on all aspects of the proposed rules, as well as comment on the specific provisions and issues highlighted in the discussion below. The Commission further requests comment on an appropriate effective date for final rules, once adopted.

## II. Proposed Regulations

### A. DCOs

#### 1. Amount of Financial Resources Required

As a central counterparty, a DCO must have sufficient financial resources to be able to withstand a potential default by one of its clearing members.<sup>10</sup> In the event of a default, a DCO would continue to have obligations to the clearing members that are owed variation settlement payments and, therefore, the DCO must have sufficient liquid resources to meet those obligations in a timely fashion. Proposed Regulation 39.11(a)(1) would

*i.e.*, whether or not the DCO is a membership organization. Clearing members include futures commission merchants (FCMs) that clear on behalf of customers or themselves, and non-FCMs that clear solely on behalf of themselves. *See also* the definition of the term "clearing member" in CFTC Regulation 1.3(c).

<sup>9</sup>Commission staff has been engaged in discussions with staff of other members of the Council concerning which entities might qualify.

<sup>10</sup>Each DCO determines for itself what constitutes a "default," but generally a clearing member is considered to be in default when it fails to fulfill any obligation to the DCO.

require a DCO to maintain sufficient financial resources to meet its financial obligations to its clearing members notwithstanding a default by the clearing member creating the largest financial exposure for the DCO in extreme but plausible market conditions. This standard is consistent with the standard set forth in Core Principle B, and is also consistent with current international standards.<sup>11</sup>

There may be some instances in which one clearing member controls another clearing member or in which a clearing member is under common control with another clearing member. The Commission proposes to treat such affiliated clearing members as a single entity for purposes of determining the largest financial exposure because the default of one affiliate could have an impact on the ability of the other to meet its financial obligations to the DCO.<sup>12</sup> However, to the extent that each affiliated clearing member is treated as a separate entity by the DCO, with separate capital requirements, separate guaranty fund obligations, and separate potential assessment liability, the Commission requests comment on whether a different approach might be warranted.

Separately, proposed Regulation 39.11(a)(2) would require a DCO to maintain sufficient financial resources to cover its operating costs for at least one year, calculated on a rolling basis. This standard is consistent with the standard set forth in amended Core Principle B. It is also consistent with established accounting standards, under which an entity's ability to continue as a going concern comes into question if there is evidence that the entity may be unable to continue to meet its obligations in the next 12 months without substantial disposition of assets outside the ordinary course of business, restructuring of debt, externally forced

<sup>11</sup> In November 2004, the Task Force on Securities Settlement Systems, jointly established by the Committee on Payment and Settlement Systems (CPSS) of the central banks of the Group of Ten countries and the Technical Committee of the International Organization of Securities Commissions (IOSCO), issued its Recommendations for Central Counterparties. Under Recommendation 5, a central counterparty must maintain sufficient financial resources to withstand, at a minimum, a default by the participant to which it has the largest exposure in extreme but plausible market conditions. However, the Commission notes that CPSS and IOSCO are currently reviewing this standard and it may be revised.

<sup>12</sup> For example, the positions of each clearing member would be margined separately and would be stress tested separately. However, losses of each would be aggregated and gains would not offset losses.

revisions of its operations, or similar actions.<sup>13</sup>

### 2. Types of Financial Resources

#### a. Default Resources

Proposed Regulation 39.11(b)(1) lists the types of financial resources that would be available to a DCO to satisfy the requirements of proposed Regulation 39.11(a)(1): (1) The margin of the defaulting clearing member; (2) the DCO's own capital; (3) the guaranty fund deposits of the defaulting clearing member and non-defaulting clearing members; (4) default insurance; (5) if permitted by the DCO's rules, potential assessments for additional guaranty fund contributions on non-defaulting clearing members; and (6) any other financial resource deemed acceptable by the Commission. A DCO would be able to request an informal interpretation from CFTC staff on whether or not a particular financial resource may be acceptable to the Commission.

In the event of a default by one of its clearing members, a DCO would first seize the margin of the defaulting clearing member. If the margin were insufficient to cure the default, the DCO might use its own capital to cover the shortfall. Currently, Commission regulations do not prescribe capital requirements for DCOs. The Commission invites comment on whether it should consider adopting such requirements and if so, what those requirements should be.

Clearing members also are typically required to maintain a deposit, in the form of cash and/or securities, in a guaranty fund, which may be used by the DCO to cover any loss sustained as a result of the failure of a clearing member to discharge its obligations to the DCO. In the event of a default, the DCO may draw on the defaulting clearing member's deposit to satisfy its counterparty obligations. If the deposit is insufficient, the DCO may draw on the guaranty fund deposits of non-defaulting clearing members.

In addition, a DCO may have an assessment power that allows it to demand additional funds from non-defaulting clearing members, up to a specified amount, if the guaranty fund has been exhausted. The size of a clearing member's potential assessment obligation is usually established by a formula set forth in the DCO's rules.

Unlike margin or a guaranty fund, assessment powers are not resources on

<sup>13</sup> *See* American Institute of Certified Public Accountants Auditing Standards Board Statement of Auditing Standards No. 59, The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern, as amended.

hand but a promise to pay. A clearing member, however, may have a strong financial incentive to pay an assessment. If a clearing member failed to pay its assessment obligation, that failure would be treated as a default and the clearing member would be subject to liquidation of its positions and forfeiture of the margin in its proprietary account. Thus, in addition to a potential general interest in maintaining the viability of the DCO going forward, a non-defaulting clearing member may have a specific incentive to pay an assessment depending on the size and profitability of its positions and the margin on deposit relative to the size of the assessment.

No U.S. futures clearinghouse has ever had to exercise its assessment power. In light of the apparent low probability of a default of such magnitude as to require assessments, the use of assessment power as a backstop rather than increasing the size of guaranty funds seems to have been an efficient allocation of capital. The growth in clearing of swaps, however, creates new risks that the Commission must evaluate.

The Commission is proposing that DCOs put rules and procedures in place to ensure timely payment of assessments by clearing members. First, each DCO must require its clearing members to have the ability to meet an assessment within the time frame of a normal variation settlement cycle. Second, each DCO must monitor, on a continual basis, each clearing member's financial and operational capacity to pay potential assessments.

As discussed below, the Commission is proposing to limit the degree to which assessment powers may be considered to be an available financial resource. The Commission invites comment on whether these limits and requirements are appropriate. More generally, the Commission is also seeking comment on whether assessment powers should be considered to be a financial resource available to satisfy the requirements of proposed Regulation 39.11(a)(1).

#### b. Operating Resources

Proposed Regulation 39.11(b)(2) lists the types of financial resources that would be available to a DCO to satisfy the requirements of proposed Regulation 39.11(a)(2): (1) The DCO's own capital; and (2) any other financial resource deemed acceptable by the Commission. A DCO would be able to request an informal interpretation from CFTC staff on whether or not a particular financial resource may be acceptable to the Commission. The Commission invites commenters to

recommend particular financial resources, and explain the basis, for inclusion in the final regulation. In this regard, the Commission notes that the proposed rule does not specify that a DCO must hold equity capital. The Commission requests comment on whether such a provision would be appropriate.

#### c. Allocation of Resources

Proposed Regulation 39.11(b)(3) would allow a DCO to allocate a financial resource, in whole or in part, to satisfy the requirements of either proposed Regulation 39.11(a)(1) (default risk) or proposed Regulation 39.11(a)(2) (operating costs), but not both, and only to the extent the use of that financial resource is not otherwise limited by the CEA, Commission regulations, the DCO's rules, or any contractual arrangements to which the DCO is a party. In the event that a default would force a DCO to cease operations, the DCO would need sufficient financial resources to cover the default and conduct an orderly wind down of its business.

#### 3. Computation of the Financial Resources Requirement

Proposed Regulation 39.11(c)(1) would require a DCO to perform stress testing on a monthly basis in order to make a reasonable calculation of the financial resources it needs to meet the requirements of proposed Regulation 39.11(a)(1). In the first instance, the DCO would have reasonable discretion in determining the methodology it uses to make the calculation.<sup>14</sup> Because effective stress testing involves a great deal of judgment, the Commission is not proposing that DCOs test a particular scenario. Rather, the proposed regulation requires DCOs to take into account both historical data and hypothetical situations. (By definition, a stress test using only historical data would never cover a market move setting a new record.) Within those guidelines, DCOs would have discretion in selecting scenarios, subject to Commission review.

The Commission would review the methodology and require changes as appropriate. The methodology must address any unique risks associated with particular products, such as the jump to default risk and compounding effects of credit default swaps.

Because of the comprehensive nature of the stress tests required for

determining the size of the financial resources package, the Commission is proposing that these tests be conducted monthly. As will be discussed in a later rulemaking,<sup>15</sup> the Commission is likely to require more frequent stress testing in connection with DCO risk management programs. Such tests would be conducted for different purposes and might use different inputs. The Commission requests comment on whether monthly tests are appropriate for purposes of calculating required financial resources.

Proposed Regulation 39.11(c)(2) would require a DCO to make a reasonable calculation each month of the financial resources it needs to meet the requirements of proposed Regulation 39.11(a)(2). In the first instance, the DCO would have reasonable discretion in determining the methodology it uses to make the calculation. However, the Commission may review the methodology and require changes as appropriate.

#### 4. Valuation of Financial Resources

Proposed Regulation 39.11(d)(1) would require a DCO, no less frequently than monthly, to calculate the current market value of each financial resource used to meet its obligations under proposed Regulation 39.11(a). A DCO would be required to perform the valuation at other times as appropriate, because market values may fluctuate and proposed Regulation 39.11(a) requires the DCO to be able to meet its obligations on a rolling basis. When valuing a financial resource, a DCO would be required to reduce the value, as appropriate, to reflect any market or credit risk specific to that particular resource, *i.e.*, apply a haircut. The Commission would permit each DCO to exercise its discretion in determining the applicable haircuts. However, such haircuts would have to be evaluated on a quarterly basis, would be subject to Commission review, and would have to be acceptable to the Commission.

Notwithstanding a DCO's general discretion in applying haircuts, proposed Regulation 39.11(d)(2)(i) would require a 30 percent haircut on the value of a DCO's assessment power. This is because in the event of a default, the defaulting clearing member would not be able to pay its assessment and other clearing members might also be unable or unwilling to pay. Based on the significant percentage of total margin that may be attributable to a few of the largest clearing members, failure to pay

<sup>14</sup> This is consistent with DCO Core Principle A, which gives a DCO "reasonable discretion in establishing the manner in which it complies with the core principles." See Section 5b(c)(2)(A) of the CEA, 7 U.S.C. 7a-1(c)(2)(A).

<sup>15</sup> The Commission will propose, at a later time, additional regulations to implement Core Principle D (risk management).

assessments could approach the 30 percent level. The Commission invites comment on whether this proposed valuation of assessments is appropriate.

To further increase the likelihood that the DCO will have resources immediately available to meet a default, the Commission is proposing that, in calculating the financial resources available to meet its obligations, a DCO may only count the value of assessments, after the haircut, to meet up to 20 percent of the resources requirement generated by the stress testing. The Commission requests comment on this restriction.

#### 5. Liquidity of Financial Resources

In assessing the adequacy of a DCO's financial resources, the liquidity of resources must be considered. For example, the time span of an intra-day settlement cycle (from the time positions are marked to market until the time clearing members are required to pay) may be only a few hours. In the event of a clearing member defaulting on a payment to the DCO during the intra-day settlement cycle, the DCO would need access to liquid assets easily convertible to cash. DCOs often use committed lines of credit to provide this liquidity.

Proposed Regulation 39.11(e)(1) would require a DCO to have financial resources sufficiently liquid to enable the DCO to fulfill its obligations as a central counterparty during a one-day settlement cycle.

In particular, the proposed regulations would require a DCO to have sufficient capital in the form of cash to cover the average daily settlement variation pay per clearing member over the last fiscal quarter. For purposes of this calculation, if a clearing member had pays in both its house and customer accounts, the amount would be the sum of the two pays. If the clearing member had a pay in its house account and a collect in its customer account, the amount would be that of the house pay. If the clearing member had collects in both of its accounts, that day's variation settlement would not be included in the calculation. The DCO would be permitted to take into account a committed line of credit or similar facility for the purpose of meeting the remainder of the liquidity requirement.

The Commission requests comment on the proposed liquidity standards. In particular, the Commission requests comment on whether the liquidity requirement should cover more than a one-day cycle. The Commission also requests comment on what standards might be applicable to lines of credit. For example, should the Commission

require that there be a diversified set of providers or that a line of credit have same-day drawing rights?

Proposed Regulation 39.11(e)(2) would require DCOs to maintain unencumbered liquid financial assets in the form of cash or highly liquid securities, equal to six months' operating costs. The Commission believes that having six months' worth of unencumbered liquid financial assets would give a DCO time to liquidate the remaining financial assets it would need to continue operating for the last six months of the required one-year period. If a DCO does not have six months' worth of unencumbered liquid financial assets, it may use a committed line of credit or similar facility to satisfy this requirement.

The Commission notes that a committed line of credit or similar facility is not listed in proposed Regulations 39.11(b)(1) or 39.8(b)(2) as a financial resource available to a DCO to satisfy the requirements of proposed Regulations 39.11(a)(1) and 39.11(a)(2), respectively. A DCO may only use a committed line of credit or similar facility to meet the liquidity requirements set forth in proposed Regulations 39.11(e)(1) and 39.11(e)(2).

To the extent that a DCO relies on a guaranty fund, adequate liquidity is crucial. To address liquidity concerns, proposed Regulation 39.11(e)(3) provides that: (i) Assets in a guaranty fund must have minimal credit, market, and liquidity risks and must be readily accessible on a same-day basis, (ii) cash balances must be invested or placed in safekeeping in a manner that bears little or no principal risk, and (iii) letters of credit are not a permissible asset for a guaranty fund.

#### 6. Reporting Requirements

Under proposed Regulation 39.11(f)(1), at the end of each fiscal quarter, or at any time upon Commission request, a DCO would be required to report to the Commission: (i) The amount of financial resources necessary to meet the requirements set forth in the regulation; and (ii) the value of each financial resource available to meet those requirements. The DCO would have to include with its report a financial statement, including the balance sheet, income statement, and statement of cash flows, of the DCO or its parent company (if the DCO does not have an independent financial statement and the parent company's financial statement is prepared on a consolidated basis). If one of the financial resources a DCO is using to meet the regulation's requirements is a guaranty fund, the DCO would also have

to report the value of each individual clearing member's guaranty fund deposit.

Proposed Regulation 39.11(f)(2) requires a DCO to provide the Commission with sufficient documentation that explains both the methodology it used to calculate its financial requirements and the basis for its determinations regarding valuation and liquidity. The DCO also must provide copies of any agreements establishing or amending a credit facility, insurance coverage, or other arrangement that evidences or otherwise supports its conclusions. The sufficiency of the documentation would be determined by the Commission in its sole discretion.

A DCO would have 17 business days<sup>16</sup> from the end of the fiscal quarter to file its report, but would also be able to request an extension of time from the Commission.

#### B. SIDCOs

As DCOs, SIDCOs would remain subject to the requirements of Title VII and the regulations thereunder, except to the extent the Commission promulgated higher standards pursuant to Title VIII. With regard to Core Principle B, the Commission is proposing higher standards in two respects, as described below.

##### 1. Amount of Financial Resources Required

Because the failure of a SIDCO to meet its obligations would have a greater impact on the financial system than the failure of other DCOs, the Commission is proposing that SIDCOs be required to meet a higher standard. Specifically, proposed Regulation 39.29(a) would require a SIDCO to maintain sufficient financial resources to meet its financial obligations to its clearing members notwithstanding a default by the two clearing members creating the largest combined financial exposure for the SIDCO in extreme but plausible market conditions.

A fundamental premise of the Dodd-Frank Act is that more over-the-counter (OTC) products must be brought into the cleared environment. Although no U.S. futures clearinghouse has ever had more than one clearing member default at a time, the size and complexity of the OTC derivatives markets may increase the chance that more than one clearing member could default simultaneously. Consequently, the Commission has determined that SIDCOs should be

<sup>16</sup> This filing deadline is consistent with the deadline imposed on FCMs for the filing of monthly financial reports. See 17 CFR 1.10(b).

subject to regulations that increase their ability to contain the effects of such defaults.

## 2. Valuation of Financial Resources

In order to add another layer of protection for SIDCOs, proposed Regulation 39.29(b) would require that a SIDCO may not count the value of assessments to meet the obligations arising from a default by the clearing member creating the single largest financial exposure. This means that a SIDCO would be required to hold a greater percentage of its financial resources in margin and the guaranty fund than a DCO that is not a SIDCO.

However, because the Commission believes that assessment powers can be a capital efficient means of providing a back-up source of funding, the Commission is proposing to permit SIDCOs to count the value of assessments, after the 30 percent haircut, to meet up to 20 percent of the obligations arising from a default by the clearing member creating the second largest financial exposure. This is the standard proposed for non-systemically important DCOs in connection with the largest potential exposure.

The Commission requests comment on the proposed higher standards for SIDCOs. In particular, the Commission requests comment on the potential competitive effects of imposing higher standards on a subset of DCOs.

## III. Technical Amendments

Proposed Regulation 140.94 would allow the Commission to delegate the authority to perform certain functions that are reserved to the Commission under proposed Regulation 39.11. Specifically, the Director of the Division of Clearing and Intermediary Oversight would be given the authority to deem a financial resource acceptable under proposed Regulations 39.11(b)(1)(vi) and (b)(2)(ii); to review methodology and require changes under proposed Regulations 39.11(c)(1) and (c)(2); to request information under proposed Regulation 39.11(f)(1); and to grant an extension of the filing deadline for financial reports in accordance with proposed Regulation 39.11(f)(4).

## IV. Related Matters

### A. Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA) requires that agencies consider whether the rules they propose will have a significant economic impact on a substantial number of small entities and, if so, provide a regulatory flexibility analysis respecting the

impact.<sup>17</sup> The rules proposed by the Commission will affect only DCOs (some of which will be designated as SIDCOs). The Commission has previously established certain definitions of “small entities” to be used by the Commission in evaluating the impact of its regulations on small entities in accordance with the RFA.<sup>18</sup> The Commission has previously determined that DCOs are not small entities for the purpose of the RFA.<sup>19</sup> Accordingly, the Chairman, on behalf of the Commission, hereby certifies pursuant to 5 U.S.C. 605(b) that the proposed rules will not have a significant economic impact on a substantial number of small entities.

### B. Paperwork Reduction Act

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid control number. OMB has not yet assigned a control number to the new collection. The Paperwork Reduction Act of 1995 (PRA)<sup>20</sup> imposes certain requirements on Federal agencies (including the Commission) in connection with their conducting or sponsoring any collection of information as defined by the PRA. This proposed rulemaking would result in new collection of information requirements within the meaning of the PRA. The Commission therefore is submitting this proposal to the Office of Management and Budget (OMB) for review. If adopted, responses to this collection of information would be mandatory. The Commission will protect proprietary information according to the Freedom of Information Act and 17 CFR Part 145, “Commission Records and Information.” In addition, section 8(a)(1) of the CEA strictly prohibits the Commission, unless specifically authorized by the CEA, from making public “data and information that would separately disclose the business transactions or market positions of any person and trade secrets or names of customers.” The Commission is also required to protect certain information contained in a government system of records according to the Privacy Act of 1974, 5 U.S.C. 552a.

### 1. Information Provided by Reporting Entities/Persons

The proposed regulations require each respondent to file information with the

Commission on a quarterly basis, which would result in four annual responses per respondent. Commission staff estimates that each respondent would expend 10 hours to prepare each filing required under the proposed regulations. Commission staff estimates that it would receive filings from 12 respondents annually. Accordingly the burden in terms of hours would in the aggregate be 40 hours annually per respondent and 480 hours annually for all respondents.

Commission staff estimates that respondents could expend up to \$1,840 annually, based on an hourly wage rate of \$46, to comply with the proposed regulations. This would result in an aggregated cost of \$22,080 per annum (12 respondents × \$1,840).

### 2. Information Collection Comments

The Commission invites the public and other federal agencies to comment on any aspect of the reporting and recordkeeping burdens discussed above. Pursuant to 44 U.S.C. 3506(c)(2)(B), the Commission solicits comment in order to: (i) Evaluate whether the proposed collection of information is necessary for the proper performance of the functions of the Commission, including whether the information will have practical utility; (ii) evaluate the accuracy of the Commission’s estimate of the burden of the proposed collection of information; (iii) determine whether there are ways to enhance the quality, utility, and clarity of the information to be collected; and (iv) minimize the burden of the collection of information on those who are to respond, including through the use of automated collection techniques or other forms of information technology.

Comments may be submitted directly to the Office of Information and Regulatory Affairs, by fax at (202) 395–6566 or by e-mail at [OIRASubmissions@omb.eop.gov](mailto:OIRASubmissions@omb.eop.gov). Please provide the Commission with a copy of submitted comments so that all comments can be summarized and addressed in the final rule preamble. Refer to the Addresses section of this notice of proposed rulemaking for comment submission instructions to the Commission. A copy of the supporting statements for the collections of information discussed above may be obtained by visiting [RegInfo.gov](http://RegInfo.gov). OMB is required to make a decision concerning the collection of information between 30 and 60 days after publication of this document in the Federal Register. Therefore, a comment is best assured of having its full effect if OMB receives it within 30 days of publication.

<sup>17</sup> 5 U.S.C. 601 *et seq.*

<sup>18</sup> 47 FR 18618 (Apr. 30, 1982).

<sup>19</sup> See 66 FR 45605, 45609 (August 29, 2001).

<sup>20</sup> 44 U.S.C. 3501 *et seq.*

### C. Cost-Benefit Analysis

Section 15(a) of the CEA requires that the Commission, before promulgating a regulation under the CEA or issuing an order, consider the costs and benefits of its action. By its terms, Section 15(a) does not require the Commission to quantify the costs and benefits of a new regulation or determine whether the benefits of the rule outweigh its costs. Rather, Section 15(a) simply requires the Commission to “consider the costs and benefits” of its action.

Section 15(a) further specifies that costs and benefits shall be evaluated in light of the following considerations: (1) Protection of market participants and the public; (2) efficiency, competitiveness, and financial integrity of futures markets; (3) price discovery; (4) sound risk management practices; and (5) other public interest considerations. Accordingly, the Commission could, in its discretion, give greater weight to any one of the five considerations and could, in its discretion, determine that, notwithstanding its costs, a particular regulation was necessary or appropriate to protect the public interest or to effectuate any of the provisions or to accomplish any of the purposes of the CEA.

The Commission has evaluated the costs and benefits of the proposed regulations in light of the specific considerations identified in Section 15(a) of the CEA, as follows:

1. *Protection of market participants and the public.* The proposed regulations would require DCOs to continually assess and monitor the adequacy of their financial resources under standards established by the Commission. This would further the goal of avoiding market disruptions and financial losses to market participants and the general public.

2. *Efficiency and competition.* The proposed regulations would promote financial strength and stability, thereby fostering efficiency and a greater ability to compete in the broader financial markets. The proposed regulations would reward efficiency insofar as DCOs that operate efficiently would have lower operating costs and therefore would require fewer resources to comply with the regulations.

3. *Financial integrity of futures markets and price discovery.* The proposed regulations are designed to ensure that DCOs can sustain their market operations and meet their financial obligations to market participants, thus contributing to the financial integrity of the futures and options markets as a whole. This, in

turn, further supports the price discovery and risk transfer functions of such markets.

4. *Sound risk management practices.* The proposed regulations, by setting specific standards with respect to how DCOs should assess, monitor, and report the adequacy of their financial resources, would contribute to their maintenance of sound risk management practices and further the goal of minimizing systemic risk.

5. *Other public considerations.* As highlighted by recent events in the global credit markets, maintaining sufficient financial resources is a critical aspect of any financial entity's risk management system, and ultimately contributes to the goal of stability in the broader financial markets. Therefore, the Commission believes it is prudent to include financial resources requirements for entities applying to become or operating as DCOs.

Accordingly, after considering the five factors enumerated in the CEA, the Commission has determined to propose the regulations set forth below.

#### List of Subjects in 17 CFR Parts 39 and 140

Commodity futures, Reporting and recordkeeping requirements.

For the reasons stated in the preamble, the Commission proposes to amend 17 CFR parts 39 and 140 as follows:

#### PART 39—DERIVATIVES CLEARING ORGANIZATIONS

1. The authority citation for part 39 is revised to read as follows:

**Authority:** 7 U.S.C. 7a–1 as amended by Pub. L. 111–203, 124 Stat. 1376.

2. Add § 39.11 to read as follows:

##### § 39.11 Financial resources requirements.

(a) *General rule.* A derivatives clearing organization shall maintain financial resources sufficient to cover its exposures with a high degree of confidence and to enable it to perform its functions in compliance with the core principles set out in section 5b of the Act. A derivatives clearing organization shall identify and adequately manage its general business risks and hold sufficient liquid resources to cover potential business losses that are not related to clearing members' defaults, so that the derivatives clearing organization can continue to provide services as an ongoing concern. Financial resources shall be considered sufficient if their value, at a minimum, exceeds the total amount that would:

(1) Enable the derivatives clearing organization to meet its financial obligations to its clearing members notwithstanding a default by the clearing member creating the largest financial exposure for the derivatives clearing organization in extreme but plausible market conditions; *Provided that* if a clearing member controls another clearing member or is under common control with another clearing member, the affiliated clearing members shall be deemed to be a single clearing member for purposes of this provision; and

(2) Enable the derivatives clearing organization to cover its operating costs for a period of at least one year, calculated on a rolling basis.

(b) *Types of financial resources.* (1) Financial resources available to satisfy the requirements of paragraph (a)(1) may include:

(i) Margin of a defaulting clearing member;

(ii) The derivatives clearing organization's own capital;

(iii) Guaranty fund deposits;

(iv) Default insurance;

(v) Potential assessments for additional guaranty fund contributions, if permitted by the derivatives clearing organization's rules; and

(vi) Any other financial resource deemed acceptable by the Commission.

(2) Financial resources available to satisfy the requirements of paragraph (a)(2) may include:

(i) The derivatives clearing organization's own capital; and

(ii) Any other financial resource deemed acceptable by the Commission.

(3) A financial resource may be allocated, in whole or in part, to satisfy the requirements of either paragraph (a)(1) or paragraph (a)(2), but not both paragraphs, and only to the extent the use of such financial resource is not otherwise limited by the Act, Commission regulations, the derivatives clearing organization's rules, or any contractual arrangements to which the derivatives clearing organization is a party.

(c) *Computation of financial resources requirement.* (1) A derivatives clearing organization shall, on a monthly basis, perform stress testing that will allow it to make a reasonable calculation of the financial resources needed to meet the requirements of paragraph (a)(1). The derivatives clearing organization shall have reasonable discretion in determining the methodology used to compute such requirements, provided that the methodology must take into account both historical data and hypothetical scenarios. The Commission

may review the methodology and require changes as appropriate.

(2) A derivatives clearing organization shall, on a monthly basis, make a reasonable calculation of its projected operating costs over a 12-month period in order to determine the amount needed to meet the requirements of paragraph (a)(2) of this section. The derivatives clearing organization shall have reasonable discretion in determining the methodology used to compute such projected operating costs. The Commission may review the methodology and require changes as appropriate.

(d) *Valuation of financial resources.*

(1) At appropriate intervals, but not less than monthly, a derivatives clearing organization shall compute the current market value of each financial resource used to meet its obligations under paragraph (a) of this section. Reductions in value to reflect market and credit risk (haircuts) shall be applied as appropriate and evaluated on a monthly basis.

(2) If assessments for additional guaranty fund contributions are permitted by the derivatives clearing organization's rules, in calculating the financial resources available to meet its obligations under paragraph (a)(1) of this section:

(i) The derivatives clearing organization shall have rules requiring that its clearing members have the ability to meet an assessment within the time frame of a normal variation settlement cycle;

(ii) The derivatives clearing organization shall monitor, on a continual basis, the financial and operational capacity of its clearing members to meet potential assessments;

(iii) The derivatives clearing organization shall apply a 30 percent haircut to the value of potential assessments, and

(iv) The derivatives clearing organization shall only count the value of assessments, after the haircut, to meet up to 20 percent of those obligations.

(e) *Liquidity of financial resources.*

(1) The derivatives clearing organization shall effectively measure, monitor, and manage its liquidity risks, maintaining sufficient liquid resources such that it can, at a minimum, fulfill its cash obligations when due. The derivatives clearing organization shall hold assets in a manner where the risk of loss or of delay in its access to them is minimized. The financial resources allocated by the derivatives clearing organization to meet the requirements of paragraph (a)(1) of this section shall be sufficiently liquid to enable the derivatives clearing organization to fulfill its obligations as

a central counterparty during a one-day settlement cycle. The derivatives clearing organization shall have sufficient capital in the form of cash to meet the average daily settlement variation pay per clearing member over the last fiscal quarter. If any portion of the remainder of the financial resources is not sufficiently liquid, the derivatives clearing organization may take into account a committed line of credit or similar facility for the purpose of meeting this requirement.

(2) The financial resources allocated by the derivatives clearing organization to meet the requirements of paragraph (a)(2) of this section must include unencumbered, liquid financial assets (*i.e.*, cash and/or highly liquid securities) equal to at least six months' operating costs. If any portion of such financial resources is not sufficiently liquid, the derivatives clearing organization may take into account a committed line of credit or similar facility for the purpose of meeting this requirement.

(3)(i) Assets in a guaranty fund shall have minimal credit, market, and liquidity risks and shall be readily accessible on a same-day basis;

(ii) Cash balances shall be invested or placed in safekeeping in a manner that bears little or no principal risk; and

(iii) Letters of credit shall not be a permissible asset for a guaranty fund.

(f) *Reporting requirements.* (1) Each fiscal quarter, or at any time upon Commission request, a derivatives clearing organization shall:

(i) Report to the Commission;

(A) The amount of financial resources necessary to meet the requirements of paragraph (a);

(B) The value of each financial resource available, computed in accordance with the requirements of paragraph (d); and

(C) How the derivatives clearing organization meets the liquidity requirements of paragraph (e);

(ii) Provide the Commission with a financial statement, including the balance sheet, income statement, and statement of cash flows, of the derivatives clearing organization or of its parent company; and

(iii) Report to the Commission the value of each individual clearing member's guaranty fund deposit, if the derivatives clearing organization reports having guaranty funds deposits as a financial resource available to satisfy the requirements of paragraph (a)(1) of this section.

(2) The calculations required by this paragraph shall be made as of the last business day of the derivatives clearing organization's fiscal quarter.

(3) The derivatives clearing organization shall provide the Commission with:

(i) Sufficient documentation explaining the methodology used to compute its financial resources requirements under paragraph (a) of this section,

(ii) Sufficient documentation explaining the basis for its determinations regarding the valuation and liquidity requirements set forth in paragraphs (d) and (e) of this section, and

(iii) Copies of any agreements establishing or amending a credit facility, insurance coverage, or other arrangement evidencing or otherwise supporting the derivatives clearing organization's conclusions.

(4) The report shall be filed not later than 17 business days after the end of the derivatives clearing organization's fiscal quarter, or at such later time as the Commission may permit, in its discretion, upon request by the derivatives clearing organization.

3. Add § 39.29 to read as follows:

**§ 39.29 Financial resources requirements.**

(a) *General rule.* Notwithstanding the requirements of § 39.11(a)(1) of this part, a systemically important derivatives clearing organization shall maintain financial resources sufficient to enable it to meet its financial obligations to its clearing members notwithstanding a default by the two clearing members creating the largest combined financial exposure for the systemically important derivatives clearing organization in extreme but plausible market conditions.

(b) *Valuation of financial resources.* Notwithstanding the requirements of § 39.11(d)(2) of this part, if assessments for additional guaranty fund contributions are permitted by the systemically important derivatives clearing organization's rules, in calculating the financial resources available to meet its obligations under paragraph (a) of this section:

(1) The systemically important derivatives clearing organization may not count the value of assessments to meet the obligations arising from a default by the clearing member creating the largest financial exposure for the systemically important derivatives clearing organization in extreme but plausible market conditions; and

(2) The systemically important derivatives clearing organization may only count the value of assessments, after the haircut set forth in § 39.11(d)(2)(iii) of this part, to meet up to 20 percent of the obligations arising from a default by the clearing member

creating the second largest financial exposure for the systemically important derivatives clearing organization in extreme but plausible market conditions.

#### **PART 140—ORGANIZATION, FUNCTIONS, AND PROCEDURES OF THE COMMISSION**

4. The authority citation for part 140 continues to read as follows:

**Authority:** 7 U.S.C. 2 and 12a.

5. In § 140.94, revise paragraphs (a)(4) and (a)(5) and add a new paragraph (a)(6) to read as follows:

##### **§ 140.94 Delegation of authority to the Director of the Division of Clearing and Intermediary Oversight.**

(a) \* \* \*

(4) All functions reserved to the Commission in § 5.12 of this chapter, except for those relating to nonpublic treatment of reports set forth in § 5.12(i) of this chapter;

(5) All functions reserved to the Commission in § 5.14 of this chapter; and

(6) All functions reserved to the Commission in §§ 39.11(b)(1)(vi), (b)(2)(ii), (c)(1), (c)(2), (f)(1), and (f)(4) of this chapter.

\* \* \* \* \*

Issued in Washington, DC, on October 1, 2010, by the Commission.

**David A. Stawick,**

*Secretary of the Commission.*

[FR Doc. 2010-25322 Filed 10-13-10; 8:45 am]

**BILLING CODE P**

## **DEPARTMENT OF VETERANS AFFAIRS**

### **38 CFR Parts 1 and 2**

**RIN 2009-AN72**

#### **Release of Information From Department of Veterans Affairs Records**

**AGENCY:** Department of Veterans Affairs.

**ACTION:** Proposed rule.

**SUMMARY:** The Department of Veterans Affairs (VA) proposes to amend its regulations governing the submission and processing of requests for information under the Freedom of Information Act (FOIA) in order to implement provisions of the E-FOIA Act and the Openness in Government Act, and to reorganize and clarify existing regulations. The proposed regulations would establish the procedures and rules necessary for VA to process requests for information

under the FOIA, including matters such as how to file a request or appeal, how requests for business information are handled, and how issues regarding fees are resolved. The intended effect of these regulations is to implement legislative changes made to the FOIA, as noted above, and to provide the public clear instructions and useful information regarding the filing and processing of FOIA requests.

**DATES:** Comments must be received on or before December 13, 2010.

**ADDRESSES:** Written comments may be submitted through <http://www.Regulations.gov/>; by mail or hand-delivery to the Director, Regulations Management (02REG), Department of Veterans Affairs, 810 Vermont Avenue, NW., Room 1068, Washington, DC 20420; or by fax to (202) 273-9026. Comments should indicate that they are submitted in response to “RIN 2900-AN72, Release of Information from Department of Veterans Affairs Records.” Copies of comments received will be available for public inspection in the Office of Regulation Policy and Management, Room 1063B, between the hours of 8 a.m. and 4:30 p.m., Monday through Friday (except holidays). Please call (202) 461-4902 for an appointment. In addition, during the comment period, comments may be viewed online through the Federal Docket Management System (FDMS) at <http://www.Regulations.gov/>.

#### **FOR FURTHER INFORMATION CONTACT:**

Catherine Nachmann, Staff Attorney, Office of the General Counsel (024), Department of Veterans Affairs, 810 Vermont Avenue, NW., Washington, DC 20420, (202) 461-7684. (This is not a toll free number.)

**SUPPLEMENTARY INFORMATION:** The FOIA, codified at 5 U.S.C. 552, requires an agency to publish public guidance regarding its implementation of the statute, such as rules of procedure and substantive rules of general applicability. The Privacy Act of 1974, as amended, codified at 5 U.S.C. 552a, requires an agency to publish its rules and procedures implementing that statute. Section 501(a) of title 38, U.S.C., authorizes the Secretary of Veterans Affairs to prescribe rules and regulations to carry out the laws administered by VA, including when information may be released from claimant records under 38 U.S.C. 5701, what activities fall within 38 U.S.C. 5705 regarding confidentiality of medical quality assurance records, whether and to whom information pertaining to those activities may be released, and when information may be released from records covered by 38

U.S.C. 7332 regarding the identity, diagnosis, or treatment of drug abuse, alcoholism or alcohol abuse, infection with the human immunodeficiency virus, and sickle cell anemia.

We propose to amend VA's regulations pertaining to release of information under 5 U.S.C. 552. VA's current FOIA regulations are codified at 38 CFR 1.550 through 1.557, including reserved §§ 1.558 and 1.559. This proposed rule would implement the FOIA in §§ 1.550 through 1.562. The proposed rule would in large part cover the same issues as are covered in VA's current regulations, such as how to submit a request for records, how VA addresses a request for records, and fees for addressing record requests under the FOIA. We propose to update these regulations to accommodate current means of communication with VA, streamline the existing procedures based on our experience administering the FOIA, incorporate changes in the procedural requirements of the FOIA since promulgation of current regulations, make VA's procedures easier for the public to understand, and generally reorganize and renumber the applicable provisions.

In addition, we propose to add new provisions to explicitly implement the E-FOIA Act, Public Law 104-231, and the Openness in Government Act, Public Law 110-175. For additional resources on any of the procedural requirements of the FOIA, E-FOIA Act, or Openness in Government Act in particular, see the detailed information available at the U.S. Department of Justice (DOJ) website. For example, a copy of the FOIA can be located at <http://www.justice.gov/oip/amended-foia-redlined.pdf>. The current edition of the VA FOIA Reference Guide can be located at <http://www.foia.va.gov/docs/RequesterHandbook.pdf>, and specific information about implementing the FOIA and its amendments can be found in guidance issued by DOJ through its FOIA Updates and FOIA Post publications, located at <http://www.usdoj.gov/oip/foi-upd.htm> and <http://www.justice.gov/oip/foiapist/mainpage.htm>.

#### **Changes to 38 CFR Part 1**

##### *1.550 Purpose*

Current § 1.550 is entitled “General” and provides a general statement of VA policy regarding disclosure of information to the extent permitted by law, including when VA would otherwise be authorized to withhold the information, if the disclosure is for a useful purpose or when disclosure will not affect the proper conduct of official