

**TREASURY EXCLUDES FX SWAPS AND FX FORWARDS
FROM MOST CFTC OVERSIGHT**

The Secretary of the Treasury has issued a Final Determination to exempt foreign exchange swaps (“FX Swaps”) and foreign exchange forwards (“FX Forwards”) from the definition of “swap” in the Commodity Exchange Act.¹ A counterparty to FX Swaps or FX Forwards remains subject to the swap reporting rules promulgated by the Commodity Futures Trading Commission.

Not All Foreign Exchange Swap Transactions Are Exempt

The Treasury’s Final Determination applies to FX Swaps and FX Forwards only and does not apply to a wide range of foreign currency transactions that fall outside the narrow definitions of these terms. For example, foreign exchange options, currency swaps, and non-deliverable forwards remain within the definition of “swap” and do not qualify for the exemption.

An FX Swap is:

A transaction that solely involves (A) a physical exchange of the principal amount of two different currencies on a specific date at a fixed rate that is agreed upon on the inception of the contract covering the exchange; and (B) a reverse exchange of the principal amount of the two currencies at a later date and at a fixed rate that is agreed upon on the inception of the contract covering the exchange.²

An FX Forward is:

A transaction that solely involves the physical exchange of the principal amount of two different currencies on a specific future date at a fixed rate agreed upon on the inception of the contract covering the exchange.³

Treasury notes in its Final Determination that FX Swaps and FX Forwards are excluded from the definition of “swap” because of the distinctive characteristics of these instruments. Unlike most

¹ *Determination of Foreign Exchange Swaps and Foreign Exchange Forwards under the Commodity Exchange Act*, (Nov. 16, 2012) (the “Final Determination”). Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act authorizes Treasury to exclude FX Swaps and FX Forwards from the definition of “swap” if it determines that they “(I) should not be regulated as swaps under the Commodity Exchange Act; and (II) are not structured to evade the Dodd-Frank Wall Street Reform and Consumer Protection Act in violation of any rule promulgated by the Commission pursuant to section 721(c) of that Act.” 7 U.S.C. 1a(47)(E)(i).

² *See* 7 U.S.C. 1a(25).

³ *See* 7 U.S.C. 1a(24).

other swaps, FX Swaps and FX Forwards have fixed payment obligations, involve the physical exchange of the full principal amount of the contract in two different currencies and are predominantly short-term instruments⁴ with lower credit risk. A foreign currency transaction that does not involve full physical exchange of the two reference currencies (e.g., a contract that allows for net settlement according to profit or loss) is not within the narrow definition of FX Swap or FX Forward. Such transactions are considered swaps and the counterparties involved are subject to full regulation by the CFTC.

If a foreign currency instrument is not considered an FX Swap or FX Forward, then it would generally be considered a swap. Accordingly, a collective investment vehicle that trades such instruments could be a commodity pool under the Commodity Exchange Act. The commodity pool operator of such a pool generally would have to count such instruments toward the de minimis trading thresholds found in certain exclusions and exemptions.

Some Commodity Exchange Act Requirements Still Apply

Under the Final Determination, most requirements otherwise applicable to swaps do not apply to FX Swaps and FX Forwards. For example, FX Swaps and FX Forwards do not have to be cleared or traded on a regulated venue. In addition, counterparties to FX Swaps and FX Forwards are not subject to registration as swap dealers or major swap participants with respect to such transactions. Nevertheless, the decision to exempt FX Swaps and FX Forwards from regulation as swaps does not affect the application of other provisions under the Commodity Exchange Act.⁵

Treasury notes that counterparties to FX Swaps and FX Forwards remain subject to the CFTC's new trade-reporting requirements and enhanced anti-evasion provisions.⁶ FX Swaps and FX Forwards traded on regulated venues remain subject to all applicable Commodity Exchange Act requirements. In addition, counterparties to FX Swaps and FX Forwards will have to comply with the additional reporting required by the planned global foreign exchange trade repository. Finally, the exclusion of FX Swaps and FX Forwards from the definition of swap does not affect the jurisdiction of the CFTC over retail foreign exchange transactions.

⁴ The Final Determination notes that “over 98 percent of foreign exchange swaps and forwards mature in less than one year, and 68 percent mature in less than one week.”

⁵ See also Final Rules and Interpretations Regarding Certain Transactions Within the Scope of the Definitions of the Terms “Swap” and “Security-Based” Swap, 77 Fed. Reg. 48253 (Aug. 13, 2012).

⁶ In addition, any party to an FX Swap or FX Forward that is a swap dealer or major swap participant shall conform to the CFTC's business conduct standards.

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