

REGULATION OF U.S. CURRENCY TRANSACTIONS

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Introduction

Currency transactions, which prior to the market disruption of 2008 were among the least regulated transactions in the U.S. financial markets, are now highly regulated and are subject to one of the most complex regulatory regimes. The Dodd-Frank Wall Street Transparency and Accountability Act of 2010 (“Dodd-Frank”)¹ made substantial changes to the Commodity Exchange Act (“CEA”) relating to currency trading, some of which are still being implemented and defined. The current regulatory architecture imposes different requirements on currency transactions depending upon factors including: the type of product being traded; whether the transaction is physically or cash-settled; the type of person trading the product (*i.e.*, whether institutional or retail investors are the counterparties);² and whether the instrument is traded on a securities or futures exchange or in the over-the-counter (“OTC”) market.³

Notwithstanding the broad reach of the current U.S. regulatory regime governing foreign exchange, there are still issues that are open to interpretation. For example, language in regulatory releases suggests that there is uncertainty about whether a physically-settled currency contract⁴ could be recharacterized as a swap if it is settled through an offsetting physically-settled contract rather than an exchange of the designated currencies. Such a characterization would result in substantially different regulatory and operational treatment, including with respect to mandatory clearing, margin, trade execution on a designated contract market (“DCM”) or swap execution facility (“SEF”) and reporting requirements.⁵ There is also uncertainty with respect to the applicability and scope of margin requirements as a result of a supervisory policy issued by the Board of Governors of the Federal Reserve System (“Federal Reserve”) that suggests that banking institutions under the supervision of the Federal Reserve, which includes the largest foreign exchange dealers, may be expected to post and collect variation margin in connection with OTC physically-settled foreign exchange derivatives, even though such products are otherwise excepted from the margin requirements under Dodd-Frank as a result of the determination made by the U.S. Department of the Treasury (the “Treasury”).⁶ There also continue to be areas of uncertainty in the retail context. For example, under the current guidance, it is



not clear how an OTC transaction with a retail investor should be treated at unwind if that investor has, since the trade commenced, attained institutional status by qualifying as an ECP. We discuss each of the issues in greater detail in Section III of this article.

Most foreign exchange and currency transactions (“Currency Transactions”) conducted in the U.S. market are subject to the CEA and the rules of the CFTC and the National Futures Association (“NFA”). Other financial regulators, such as the federal banking regulators and the SEC, also play a significant role. This article provides an overview of the history of the regulation of Currency Transactions in the United States, including the patterns of bad conduct and aberrations in that market that have led to the increase in regulation. We summarize below the existing regulatory framework and focus on the regulation of both retail and institutional OTC Currency Transactions by the CFTC. In terms of the scope of Currency Transactions discussed in this article, we consider: (i) swaps and options on foreign exchange, including non-deliverable forwards (“NDFs”), which are primarily traded in the OTC market between ECPs but which Dodd-Frank contemplates migrating to trading on a DCM or SEF and being subject to central clearing through a derivatives clearing organization (“DCO”) if the transactions become sufficiently commoditized; (ii) physically-settled currency forwards defined as “foreign exchange forwards” under the CEA⁷ (“Currency Forwards”) and physically-settled foreign exchange swaps defined as “foreign exchange swaps” under the CEA (“Physically-Settled FX Swaps”)⁸ traded between ECPs; (iii) spot transactions that result in an exchange of currencies within two days;⁹ and (iv) off-exchange Currency Transactions entered

into with persons who are not ECPs and that are regulated pursuant to CEA Sections 2(c)(2)(B), (C) and (E), which we refer to as “Retail Forex.”¹⁰ We do not discuss regulation of (i) currency options traded on regulated securities exchanges,¹¹ which are regulated by the SEC and margined, traded, cleared and settled in substantially the same way as U.S. listed securities options,¹² or (ii) currency futures and options on currency futures, which are regulated, margined, traded, cleared and settled in substantially the same way as other U.S. financial futures contracts and options thereon.

I. History of Foreign Exchange and Currency Regulation

The regulation of Currency Transactions has evolved significantly over time as Congress, the CFTC, NFA and other regulators have attempted to curb various forms of misconduct and respond to market disruptions, while still preserving the liquidity and robustness of the market. The most comprehensive change to the regulation of Currency Transactions came in 2010 with the adoption of Dodd-Frank. Under Dodd-Frank, Congress enacted a new regulatory framework for institutional OTC Currency Transactions (among other products) entered into between ECPs. This framework distinguishes between cash-settled and physically-settled Currency Transactions and contemplates that physically-settled Currency Transactions may be eligible for exemption from many of the regulatory requirements applicable to cash-settled Currency Transactions that are fully regulated as “swaps.” Dodd-Frank also enhanced regulation of Retail Forex by requiring those regulators that oversee entities conducting Retail Forex to adopt substantive regulations applicable to such entities addressing disclosures,

recordkeeping, capital and margin, reporting, business conduct, documentation and other requirements deemed to be necessary by such regulators.¹³

A. Regulation Prior to Dodd-Frank

Federal regulation of Currency Transactions dates back to the passage of the Commodity Futures Trading Commission Act of 1974, which created the CFTC. When the bill was being considered, the Treasury expressed concerns that the CFTC's jurisdiction as proposed in the bill would overreach and capture the OTC foreign currency market, which was characterized by trading between banks and large institutional customers and viewed by the Treasury as being more properly regulated by federal banking regulators.¹⁴ The bill was amended to include language proposed by the Treasury (the "Treasury Amendment")¹⁵ that excluded from regulation under the CEA specified transactions involving foreign currency, which were not transactions "for future delivery conducted on a board of trade." The CFTC generally interpreted the Treasury Amendment narrowly to exclude from CFTC oversight only those Currency Transactions conducted in the OTC market between banks and other institutional market participants.¹⁶ In the years that followed, the CFTC bolstered its jurisdiction over retail Currency Transactions in various interpretive actions,¹⁷ while still recognizing the limits of its jurisdiction over Currency Transactions in the institutional OTC market.¹⁸ The scope of the Treasury Amendment was subject to substantial litigation between 1974 and 2000. Although courts upheld the CFTC's jurisdiction over OTC Currency Transactions in many cases,¹⁹ several key decisions interpreted the exclusion for for-

eign currency transactions in the Treasury Amendment broadly and significantly limited the CFTC's jurisdiction over OTC Currency Transactions. The debate around the scope of the Treasury Amendment culminated in a U.S. Supreme Court decision in *Dunn v. CFTC* in 1997.²⁰ In that case, the U.S. Supreme Court held that OTC foreign currency options were among the products excluded from CFTC jurisdiction by the Treasury Amendment, noting that "[t]he legislative history strongly suggests ... that Congress' broad purpose in enacting the Treasury Amendment was to provide a general exemption from CFTC regulation for sophisticated off exchange foreign currency trading, which had previously developed entirely free from supervision under the commodities laws."²¹ In an even more sweeping decision, the U.S. Court of Appeals for the Ninth Circuit held that the Treasury Amendment precluded the CFTC's jurisdiction over OTC Currency Transactions because the Treasury Amendment was intended to apply to all OTC Currency Transactions.²² These judicially-imposed restrictions on the CFTC's jurisdiction impeded the ability of the CFTC to bring enforcement actions against foreign exchange "bucket shops," a proliferating group of foreign exchange dealers that targeted retail investors with fraudulent practices. This situation prompted calls for Congress to rethink the Treasury Amendment to provide necessary protections to retail investors.²³

In 2000, Congress stepped forward to provide the CFTC with clearer jurisdiction over Retail Forex, while also clarifying that OTC institutional transactions remained outside the scope of CFTC regulation. The Commodity Futures Modernization Act of 2000 (the "CFMA")²⁴ required Retail Forex trades to be conducted through otherwise regulated entities, including futures

commission merchants (“FCMs”), affiliated persons of FCMs satisfying specified recordkeeping requirements, registered broker-dealers, insurance companies and banking institutions.²⁵ OTC Currency Transactions between institutional traders qualifying as ECPs,²⁶ on the other hand, were largely exempted from CFTC jurisdiction by the CFMA.²⁷

The period after the adoption of the CFMA was marked by an increasing number of regulatory enforcement actions involving fraudulent conduct in the Retail Forex market. As of 2005, the CFTC had brought over 70 cases involving allegations of misconduct in the Retail Forex market and had imposed over \$240 million in penalties and claims for restitution.²⁸ The NFA, which had adopted rules in 2003 applicable to NFA members who engaged in Retail Forex transactions²⁹ (often firms that had registered as FCMs solely for the purpose of engaging in Retail Forex),³⁰ also brought a number of enforcement actions against Retail Forex dealers alleging fraudulent conduct.³¹ The ability of the CFTC and NFA to combat fraud in the Retail Forex market, however, was limited by several aspects of the CFMA. The CFMA did not provide the CFTC with rulemaking authority with respect to Retail Forex, and the CFTC had not exercised its general rulemaking authority under Section 8a(5) of the CEA in this area. Further, because the entities that were permitted to engage in Retail Forex transactions included affiliated persons of FCMs,³² many firms formed “shell FCMs” that registered as FCMs but engaged in Retail Forex activities through unregistered affiliates. As a practical matter, these entities were difficult to police because they were not subject to a comprehensive set of rules governing the Retail Forex business.

The CFTC’s ability to regulate Retail Forex was further limited by court decisions that construed the scope of the CFTC’s jurisdiction narrowly. Notably, in *CFTC v. Zelener*,³³ the U.S. Court of Appeals for the Seventh Circuit considered the applicability of the CEA to foreign exchange contracts with retail customers that were documented as “spot” contracts but that were, in practice, rolled on a continuous basis. The market referred to these transactions as “rolling spot.” In *Zelener*, Judge Easterbrook, writing on behalf of the court, interpreted the provision in Section 2(c) of the CEA related to Retail Forex in a limited manner. The court held that the CFTC’s jurisdiction over Retail Forex under Section 2(c) was limited to fungible futures contracts³⁴ and that, although rolling spot transactions provided investors with economic exposure that was similar to the exposure provided by futures contracts, the transactions were not futures contracts, primarily because they were non-standardized and did not provide the customer with a right to execute an offsetting contract.³⁵ As a result, the court held that the CFTC’s jurisdiction over Retail Forex did not include rolling spot transactions.³⁶

Congress addressed the *Zelener* decision in 2008 with adoption of the Commodity Futures Trading Commission Reauthorization Act (“CRA”).³⁷ The CRA provided the CFTC with express authority to regulate entities that engage in rolling spot transactions with non-ECPs. In addition, the CRA expanded CFTC jurisdiction over Retail Forex transactions by (i) subjecting FCM affiliates to CFTC jurisdiction and requiring them to register as retail foreign exchange dealers (“RFEDs”)³⁸ if they did not fall within any other regulated entity type listed in CEA Section 2(c)(2)(B) and (ii) giving the CFTC jurisdic-

tion over foreign exchange contracts offered on a leveraged or margined basis, regardless of whether the contracts are traded on an exchange or considered to be a futures contract.³⁹ The CRA continued to exclude from CFTC jurisdiction bona fide spot contracts that result in an exchange of currencies within two days.⁴⁰

B. Dodd-Frank

In 2010, following the broader financial crisis of 2008, Dodd-Frank was enacted. Title VII of Dodd-Frank⁴¹ implemented sweeping changes to the regulation of derivatives by eliminating the broad exemptions for institutional derivatives created by the CFMA. The new legislation enacted, for the first time, a comprehensive regulatory framework for OTC derivatives, including Currency Transactions. Although the institutional provisions of Title VII of Dodd-Frank were motivated primarily by concerns regarding systemic risk caused by OTC derivatives,⁴² Title VII included provisions that specifically addressed Currency Transactions. In the institutional foreign exchange market, the regulatory regime set out in Dodd-Frank distinguishes between cash-settled and physically-settled Currency Transactions. The regulations define the institutional market for Currency Transactions as comprised of transactions between ECPs. Cash-settled transactions between ECPs were classified as “swaps” and made subject to all of the attendant regulatory requirements. Physically-settled transactions (*i.e.*, Currency Forwards and Physically-Settled FX Swaps) were made eligible for an exclusion from full regulation as swaps, which exclusion was subsequently implemented by the Treasury.⁴³ Dodd-Frank enhanced the CFTC’s anti-fraud and anti-manipulation authority over Currency Transactions and derivatives generally.

In the Retail Forex context, Dodd-Frank amended the CEA to provide that the group of entities permitted to engage in Retail Forex transactions could do so only pursuant to rules adopted by their federal regulators.⁴⁴ As a result, the statute conditioned the ability of an entity to carry out a Retail Forex business on the adoption of comprehensive regulations by its federal regulator(s), many of which had had no experience regulating Retail Forex. Dodd-Frank also made changes to the ECP definition related to Retail Forex, as described below.

C. Other Recent Developments

Since the adoption of Dodd-Frank, enforcement actions and market events have continued to shape the regulatory environment in both the retail and institutional markets. In November 2014, the CFTC settled charges against five large banks for attempted manipulation of global foreign exchange benchmark rates. The CFTC found that foreign exchange traders at the five banks colluded with traders at other banks via private chat rooms to alter trading positions with the aim and result of setting benchmark rates in a way that benefited the traders.⁴⁵ In the chat rooms, the currency traders allegedly shared confidential information regarding client orders, which provided the traders with a more comprehensive view of order flows, and then allegedly colluded to alter their own currency trading positions prior to executing client orders in order to drive the benchmark price up or down at or around the time of the daily “fix.”⁴⁶ The CFTC imposed an aggregate civil penalty of over \$1.4 billion on the banks whose traders were found to be complicit in the wrongdoing and stressed the culpability of the banks themselves, finding that they had failed to implement internal controls and

procedures regarding training and oversight of the foreign exchange traders. Another group of banks pleaded guilty in May 2015 to felony violations of U.S. antitrust laws for similar manipulative behavior affecting foreign currency exchange rates.⁴⁷

Currency Transactions were also a focal point for pension funds and institutional investors as a result of fiduciary breach allegations against major custodial banks. In the spring of 2015, the Bank of New York Mellon (“BNYM”) agreed to settle civil lawsuits and federal investigations in connection with allegations that the bank had engaged in fraudulent foreign exchange trading practices.⁴⁸ According to the allegations, BNYM misled institutional customers participating in BNYM’s “Standing Instruction Program,” which provided a conversion service in connection with the purchase or sale of foreign securities, by representing to customers that they would achieve execution at the “best rates,” in accordance with “best execution standards,” when in reality execution was provided at the highest reported interbank rate of the day (for clients purchasing foreign currency) or at the lowest reported interbank rate of the day (for clients selling foreign currency). BNYM’s practices were also alleged to be materially misleading because statements provided to customers did not disclose how the prices obtained were determined. BNYM settled the actions for \$714 million.

Similar actions were brought against State Street Bank and Trust Company (“State Street”) in connection with currency conversion services, which State Street settled.⁴⁹ State Street was alleged to have misled custodial clients by providing them with conversions at a spread from the prevailing interbank rates, contrary to representa-

tions to such clients. Plaintiffs alleged that State Street traders would execute a transaction for a client at the actual market exchange rate and then later mark the rate up or down to benefit the bank.⁵⁰ According to the complaints, the monthly reports provided to custodial clients by State Street detailed only the marked-up or marked-down exchange rates entered by State Street’s electronic system and not the more favorable rates achieved at the time of the transaction.⁵¹ As part of the settlement, State Street was ordered to distribute price reports to customers regarding spot conversions.

The Retail Forex market experienced a major shock in January 2015 when the Swiss National Bank ended its policy of capping the Swiss franc at 1.20 francs per Euro. The change in policy caused the price of the Swiss franc to increase almost 30% in value against the Euro⁵² and resulted in significant losses to market participants.⁵³ These events caused NFA to tighten margin requirements for Retail Forex transactions involving specified foreign currencies⁵⁴ and prompted calls for the CFTC to consider increased requirements for Retail Forex.⁵⁵ The CFTC ultimately approved rule amendments that (i) increased capital requirements for Retail Forex dealers registered as Forex Dealer Members (“FDMs”),⁵⁶ (ii) required FDMs to collect security deposits for off-exchange foreign exchange transactions from ECP counterparties in addition to retail counterparties, (iii) required FDMs to adopt and implement rigorous risk management programs, and (iv) required FDMs to provide additional market disclosures and firm-specific information on their websites to permit current and potential counterparties to better assess the risks of engaging in off-exchange FX transactions and conducting business with a

particular FDM.⁵⁷ NFA has continued to respond to volatility in the foreign exchange markets by changing its minimum security deposit requirements for affected currencies.⁵⁸

In February 2017, the CFTC brought an enforcement action against Forex Capital Markets, LLC (“FXCM”), a registered FCM and RFED that was previously the largest Retail Forex broker in the United States,⁵⁹ and two of its principals for alleged fraudulent conduct in connection with FXCM’s Retail Forex platform.⁶⁰ The CFTC’s settlement order alleged that FXCM had represented to customers that it executed customer trades through its “No Dealing Desk” on strictly an agency or riskless principal basis through external market makers, thus eliminating the conflict of interest resulting from FXCM taking a principal position opposite its customers. According to the settlement order, however, a significant number of customer trades were actually executed through a related high frequency trading firm (“HFT Co”) that had been founded by FXCM. Although HFT Co had been spun off by FXCM and was owned by a former FXCM employee rather than FXCM during the period in question, FXCM and HFT Co maintained a number of significant ongoing ties, including sharing employees. FXCM also provided HFT Co with priority order routing, and HFT Co made order flow payments to FXCM that were found to be profit-sharing payments related to HFT Co’s execution of trades in respect to FXCM’s customers. The CFTC alleged that FXCM misled customers as well as NFA examination staff about this relationship with HFT Co. The CFTC found that FXCM violated Section 4b(a)(2) of the CEA and CFTC Rule 5.2(b) and that both FXCM and the two principals violated Section 9(a)(4) of the CEA. FXCM and the two principals were fined

\$7 million and were permanently barred from acting in any capacity requiring registration with the CFTC or exemption from registration or associating with any firm registered with the CFTC or exempt from registration with the CFTC.

The CFTC, other regulators and prosecutors continue to bring actions against participants in both the retail and institutional markets.⁶¹

The Bank for International Settlement (“BIS”), an organization of 60 central banks, is in the process of finalizing a Global Code of Conduct for the foreign exchange market that is intended to promote integrity and effective functioning of the foreign exchange market. BIS published an initial draft of the Global Code of Conduct in 2016 that set forth standards regarding ethics, governance, information sharing, execution, risk management and compliance and confirmation and settlement processes. The Global Code of Conduct will be a voluntary code and will not have the force of regulation, but BIS and the working group responsible for the Code are working to promote widespread adoption of the Code, including among buy-side firms, sell-side firms and other foreign exchange market participants.⁶² Although BIS is expected to finalize the Global Code of Conduct in May 2017, it remains to be seen how quickly and broadly the Code will be adopted.

II. Current State of the Regulation of OTC Currency Transactions

A. Currency Transactions Regulated as Swaps

Dodd-Frank established a comprehensive regulatory regime for those derivatives that fall within the definition of “swap” under Section 1a(47) of the CEA. The definition of “swap” is broad and includes most OTC Currency Transac-

tions other than spot transactions. The following Currency Transactions would be included in the definition when executed between ECPs:

- *NDFs*. An NDF is a forward contract in foreign exchange⁶³ that is settled through a net payment of a single currency at maturity (in contrast to a Currency Forward, which is settled through an exchange of two currencies at maturity).⁶⁴ The CFTC and SEC (which share rulemaking authority over the swap definition) have classified NDFs as swaps.⁶⁵ Several industry associations petitioned the CFTC to provide relief under CEA Section 4(c) to permit NDFs to be regulated as Currency Forwards⁶⁶ arguing that they are economically equivalent to Currency Forwards and are often used by market participants for transactions involving currencies that are restricted from delivery. To date, the CFTC has not responded to the petition.
- *Foreign Currency Options*. The swap definition includes any agreement, contract, or transaction that “is a put, call, cap, floor, collar, or similar option of any kind that is for the purchase or sale, or based on the value of, 1 or more . . . currencies.” Thus, foreign currency options (but not foreign currency options traded on a securities exchange), fall within the swap definition and have been interpreted by the CFTC and SEC to constitute “swaps.”⁶⁷
- *Currency Swaps and Cross-Currency Swaps*. Currency swaps and cross-currency swaps can generally be described as swaps in which the fixed legs or floating legs based on various interest rates are ex-

changed in different currencies.⁶⁸ Currency swaps are expressly included within the statutory swap definition.⁶⁹

- *Window forwards*. A foreign exchange window forward (also called “window FX forward,” or “window contract”) is a contract that counterparties enter into to physically exchange two currencies at a price agreed upon upfront on one or more dates during an agreed time period (“window”). These contracts involve the exchange of currency on one or more dates within the window.⁷⁰ The optionality as to the timing of the delivery of the currency means that foreign exchange window forwards generally do not constitute “foreign exchange forwards” under the CEA (defined as “Currency Forwards” in this article),⁷¹ which are exempt from the swap definition.⁷²

Currency Transactions that fall within the swap definition (“Currency Swap Transactions”) are subject to the full range of transactional requirements applicable to swaps, if no exclusion or exemption is available, including: (i) mandatory clearing (if designated for clearing),⁷³ (ii) mandatory execution on a SEF or DCM (if designated for clearing and made available for trading on a SEF or DCM),⁷⁴ (iii) reporting, including public real-time reporting, of swaps to swap data repositories (“SDRs”),⁷⁵ (iv) margin requirements for uncleared swaps,⁷⁶ (v) business conduct standards⁷⁷ and swap trading documentation requirements⁷⁸ for swap dealers and major swap participants,⁷⁹ and (vi) recordkeeping requirements.⁸⁰ Counterparties that are not ECPs are prohibited from entering into Currency Swap Transactions,⁸¹ unless those transactions are entered into on or subject to the rules of a DCM

or can be executed in accordance with the Retail Forex rules.

From an operational and cost perspective, the most significant requirements imposed by Dodd-Frank are the clearing, trade execution, and margin requirements. While the CFTC has implemented clearing requirements for a number of interest rate swaps and index credit default swaps, no foreign exchange or currency products are currently subject to mandatory clearing or to the trading requirement. The CFTC staff has, as recently as October 2014, considered issuing a clearing determination applicable to NDFs.⁸² However, the CFTC has not yet taken action on such a proposal.⁸³

Notwithstanding the lack of a regulatory mandate, market participants have been voluntarily clearing some currency products.⁸⁴ Some of the contracts are also voluntarily traded on SEFs or DCMs.⁸⁵ Market participants that trade on a DCM or SEF on a voluntary basis are subject to the rules and jurisdiction of the applicable DCM or SEF.

Swap dealers that enter into uncleared Currency Swap Transactions are subject to the uncleared swap margin rules adopted by the CFTC or federal prudential regulators, as applicable. The margin regulations require swap dealers to post and collect margin for swaps with financial end users, such as funds, although swap dealers are generally not required to post or collect variation margin for swaps with non-financial end users⁸⁶ or entities eligible for an exception from clearing.⁸⁷ As a result, financial end users that trade with such swap dealers are also generally required to post and collect margin on their Currency Swap Transactions. These margin require-

ments are being phased in. Initial margin requirements for swaps between registered swap dealers and financial end users whose swap exposures exceed applicable thresholds are being phased in from September 2016 through September 1, 2020. Variation margin requirements for swaps between registered swap dealers and financial end users went into effect on March 1, 2017.⁸⁸ The CFTC issued limited relief from compliance with these variation margin requirements until September 1, 2017, subject to a swap dealer using best efforts to implement compliance and other conditions.⁸⁹ Separately, the applicable federal prudential regulators provided guidance indicating that swap dealers subject to their supervision must comply with the variation margin requirements as of March 1, 2017 for counterparties that present significant exposures and, with respect to other counterparties, must undertake good faith efforts to comply with the requirements as soon as possible, and in no case later than September 1, 2017.⁹⁰

The business conduct standards and swap trading documentation rules under Dodd-Frank apply only to swap dealers. However, these rules indirectly affect other market participants that trade Currency Swap Transactions, as swap dealers generally require their counterparties to enter into agreements and protocols, such as the Dodd-Frank protocols published by the International Swaps and Derivatives Association (“ISDA”), in order to facilitate compliance by the dealers with the rules. The swap trading documentation rules require swap dealers that enter into Currency Swap Transactions to document such transactions under written relationship documentation, such as the ISDA Master Agreement, that meet the requirements of those rules.⁹¹ Prior to Dodd-Frank, many Currency Transactions were not

documented under master relationship documentation.⁹²

B. Currency Forwards and Physically-Settled FX Swaps

The swap definition includes an exclusion for Currency Forwards and Physically-Settled FX Swaps from a number of the regulatory requirements for swaps⁹³ that was implemented by the Treasury Determination in 2012.⁹⁴ As a result, Currency Forwards, which involve the exchange of currencies on a specific future date at an agreed rate,⁹⁵ and Physically-Settled FX Swaps, which involve an exchange of two different currencies on a specific date, at a fixed rate and a reverse exchange of the two currencies at a later date at a fixed rate, are not subject to the clearing, trading and margin requirements otherwise applicable to swaps under Dodd-Frank. Currency Forwards and Physically-Settled FX Swaps are, however, subject to (i) the business conduct standards⁹⁶ and swap trading documentation rules⁹⁷ for swap dealers and major swap participants, (ii) the SDR reporting requirements (but not the real-time reporting requirements),⁹⁸ and (iii) with respect to Currency Forwards and Physically-Settled FX Swaps listed and traded on or subject to the rules of a DCM or SEF, or cleared by a DCO, those provisions of the CEA and Dodd-Frank prohibiting fraud or manipulation.⁹⁹

Because Currency Forwards and Physically-Settled FX Swaps are subject to the business conduct standards, swap trading documentation rules, and most of the reporting requirements for swaps, market participants that trade Currency Forwards and Physically-Settled FX Swaps with registered swap dealers are required to complete the same documentation that is required for market participants trading swaps, including ISDA

Master Agreements and the ISDA Dodd-Frank protocols. A significant benefit to trading Currency Forwards and Physically-Settled FX Swaps, however, is that these transactions were exempted, through the Treasury Determination,¹⁰⁰ from the margin requirements for swaps adopted by the CFTC and prudential regulators.¹⁰¹ A supervisory letter issued by the Federal Reserve in 2013, however, could be interpreted multiple ways, which creates ambiguity regarding applicability of the margin requirements.¹⁰² The letter suggests that banks subject to the Federal Reserve's jurisdiction should collect and post variation margin on physically-settled foreign exchange transactions with "financial institution" counterparties. The term "financial institution," however, is not specifically defined in the letter. As a result, the application of the guidance remains unclear.

C. Investment Funds

The ECP definition, as amended by Dodd-Frank, provides that a commodity pool that enters into OTC Currency Transactions described in the Retail Forex rules¹⁰³ (an "FX Pool") is not an ECP for the purposes of such transactions if the FX Pool has one or more investors that are not ECPs.¹⁰⁴ This look-through requirement could have had the disruptive effect of subjecting many investment funds, which generally do not screen investors for ECP status, to the Retail Forex rules.¹⁰⁵ However, the CFTC adopted a safe harbor from the look-through requirement that has provided important relief to the currency markets. The safe harbor exempts from the look-through requirement an FX Pool that (i) was not formed for the purpose of evading the Retail Forex requirements under the CEA or any related CFTC rules, regulations or orders, (ii) has total

assets exceeding \$10 million and (iii) was formed and is operated by a registered commodity pool operator (“CPO”) or by a CPO that is exempt from registration under CFTC Rule 4.13(a)(3).¹⁰⁶ The CFTC also indicated that the look-through rule does not apply to investors that are themselves investment funds.¹⁰⁷

D. Spot Transactions

The CFTC has indicated that a bona fide spot transaction that is settled through delivery of the relevant currencies within two business days is not a swap or Currency Forward.¹⁰⁸ A Currency Transaction with a longer settlement period concluding with the actual delivery of the relevant currencies may also be considered a bona fide spot transaction if it is settled on the customary timeline of the relevant spot market.¹⁰⁹ The CFTC and SEC have stated that they will consider securities conversion transactions¹¹⁰ to be bona fide spot transactions,¹¹¹ which are generally exempt from regulation.¹¹² Although the CFTC does not have substantive regulatory jurisdiction over spot transactions, the CFTC has anti-manipulation authority that would be applicable to spot transactions because it covers the manipulation of “any commodity in interstate commerce.”¹¹³ The cases against the custodial banks regarding their spot mark-up practices should also serve as a warning that, although spot transactions are not subject to direct substantive regulations, they do not fall outside of regulation for fraud.

E. Retail Forex

Retail Forex transactions are defined under the CEA and regulators’ Retail Forex rules to consist of any account, agreement, contract or transaction in foreign currency that is entered into by a

permitted counterparty with a person that is not an ECP and that is (i) a contract of sale of a commodity for future delivery (or an option on such contract) or an option that is not executed or traded on a securities exchange,¹¹⁴ or (ii) offered on a leveraged, margined or financed basis.¹¹⁵ Retail Forex transactions exclude (i) spot transactions that result in actual delivery within two days,¹¹⁶ (ii) forward-like contracts that create an enforceable obligation to make or take delivery,¹¹⁷ (iii) options that are executed or traded on a securities exchange,¹¹⁸ and (iv) securities conversion transactions.¹¹⁹

The CEA provides that only registered FCMs and RFEDs, registered broker-dealers, and banking entities are permitted to engage in Retail Forex transactions, and they may only do so pursuant to rules adopted by their applicable federal regulator.¹²⁰ The CFTC has adopted Retail Forex rules that apply to registered FCMs (but not FCMs that are dually registered as broker-dealers) and RFEDs,¹²¹ and the FDIC,¹²² OCC,¹²³ and the Federal Reserve¹²⁴ have adopted Retail Forex rules that apply to banking entities. Notably, the SEC had adopted interim rules that permitted registered broker-dealers to engage in Retail Forex transactions,¹²⁵ but the SEC allowed those rules to expire as of July 31, 2016,¹²⁶ after previously expressing concerns about the risks associated with Retail Forex.¹²⁷ As a result, Retail Forex may not be offered through broker-dealers (including broker-dealers dually registered as FCMs).

The Retail Forex rules adopted by the CFTC and banking regulators are not identical, but both sets of regulations establish requirements regarding disclosure,¹²⁸ margin,¹²⁹ statements and confirmations.¹³⁰ The regulations also include

anti-fraud provisions.¹³¹ FCMs and RFEDs that enter into Retail Forex transactions are regulated by NFA as FDMs and are subject to NFA's Retail Forex rules.¹³²

F. Anti-Fraud and Anti-Manipulation

While the substantive regulation of Currency Transactions differs depending upon the product, the CFTC's anti-fraud and anti-manipulation authority under the CEA generally applies broadly across products regulated by the CFTC, including futures contracts, swaps and Retail Forex transactions. The CFTC's anti-fraud and anti-manipulation authority also potentially extends to products that otherwise do not fall within the CFTC's rulemaking authority, including potentially to Currency Transactions that are not substantively regulated, such as spot transactions.

The CEA contains a number of anti-fraud and anti-manipulation provisions that may be applied to Currency Transactions. Section 4b of the CEA is a broad anti-fraud provision that makes it unlawful for a party to a futures contract or swap to cheat or defraud, make false reports or statements to, or willfully deceive, such person's counterparty (or attempt any of the foregoing).¹³³ Section 2(c)(2)(C)(iv) of the CEA extends this anti-fraud authority under Section 4b to leveraged Retail Forex transactions (including rolling spot transactions), regardless of whether they qualify as futures contracts.¹³⁴ Section 4c of the CEA proscribes various forms of fraudulent and manipulative activity. Section 4c(a)(2) applies to any futures contract (or option on a futures contract) or swap and prohibits wash sales, fictitious sales and transactions resulting in false price reporting.¹³⁵ Section 4c(a)(5) prevents any person from engaging in trading or other conduct

on or subject to the rules of a registered entity (a SEF or DCM) that violates bids or offers, intentionally or recklessly disregards orderly execution of transactions during the closing period, or would be considered "spoofing" (bidding or offering with an intent to cancel prior to execution).¹³⁶ Section 4c(a)(7) makes it unlawful for any person to knowingly or recklessly enter into a swap where such person's counterparty will use the swap to defraud a third party.¹³⁷ Section 9(a)(2) of the CEA provides that any manipulation or attempted manipulation of the price of any swap or any commodity in interstate commerce, or for future delivery on or subject to the rules of any registered entity, is a felony punishable by up to \$1,000,000 in fines and/or ten years imprisonment, along with the costs of prosecution.¹³⁸

Section 753 of Dodd-Frank further expanded the CFTC's anti-fraud and anti-manipulation authority by amending Section 6(c) of the CEA. New CEA Section 6(c)(1) and CFTC Rule 180.1 (which was adopted pursuant to Section 6(c)(1))¹³⁹ prohibits various forms of fraudulent and manipulative conduct and, significantly, applies to conduct that is merely "reckless," which is lower than the scienter standard under Section 9(a)(2).¹⁴⁰ Section 6(c)(1) and Rule 180.1 also have a broad reach to "all manipulative or deceptive conduct *in connection with* the purchase, sale, solicitation, execution, pendency, or termination of any swap, or contract of sale of any commodity in interstate commerce, or for future delivery on or subject to the rules of any registered entity."¹⁴¹ New Section 6(c)(3) of the CEA and CFTC Rule 180.2 (which was adopted pursuant to Section 6(c)(3)) prohibit the manipulation, or attempted manipulation, of the price of any swap, or contract of sale of any commodity

in interstate commerce, or for future delivery on or subject to the rules of any registered entity. CEA Section 6(c)(3) and CFTC Rule 180.2 do not require proof of fraud, but do require proof of specific intent to manipulate, whether directly or indirectly.¹⁴² The CEA and the CFTC's rules do not define manipulation, but courts have generally utilized the following four-prong test for establishing manipulation: (i) the accused had the ability to influence market prices; (ii) the accused specifically intended to create or effect a price or prices trend that does not reflect legitimate sources of supply and demand; (iii) artificial prices existed; and (iv) the accused caused the artificial prices.¹⁴³ Although the CFTC has generally acknowledged the validity of this test,¹⁴⁴ in a recent case in which a defendant had acknowledged engaging in conduct with an intent to affect market prices, the CFTC moved for summary judgment on the basis that manipulation could be established merely by the "intent to affect market prices."¹⁴⁵ The court ultimately rejected the CFTC's motion for summary judgment and upheld the four-prong test, stating that there is "no manipulation without intent to cause artificial prices."¹⁴⁶

The broad provisions in CEA Sections 6(c)(1) and 6(c)(3) and CFTC Rules 180.1 and 180.2 apply to fraudulent conduct that is in connection with or that attempts to manipulate the price of any "commodity in interstate commerce," and arguably provide the CFTC with enforcement authority over otherwise unregulated Currency Transactions. This authority may extend to spot transactions, for example, depending on the circumstances of the relevant conduct.

III. Current Issues

A. Treatment of Offsetting Currency Forwards

The current regulatory framework distinguishes between NDFs and Currency Forwards, with the former being subject to full regulation as "swaps" and the latter being subject to lighter regulation. While this distinction has been in place for several years, there continues to be uncertainty regarding whether transactions that are documented as Currency Forwards could be recharacterized as swaps because they are settled through entry into an offsetting Currency Forward or spot transaction.¹⁴⁷ In many cases, offsetting transactions provide the most efficient way to close out a Currency Forward. If these offsetting transactions were to cause the Currency Forwards to be deemed to be "cash-settled," then the Currency Transactions could be deemed to be swaps and the counterparties could be found to have failed to comply with the requirements applicable to swaps.

Regulatory guidance regarding characterization of offsetting Currency Transactions is ambiguous. The Swap Adopting Release states that transactions that are initially "styled as or intended to be" Currency Forwards but are subsequently "modified" to be settled in a single reference currency will be treated as swaps, and this language could be read to say that reliance on an offsetting transaction to settle a Currency Forward causes the transaction to become a swap.¹⁴⁸ Another reading of this language is that it is limited to situations in which the terms of a transaction itself are modified (*e.g.*, the written confirmation of a Currency Forward is amended to provide for cash settlement) and does not apply to situations in which parties execute a separate

offsetting transaction (*e.g.*, execute a separate written confirmation for a new Currency Forward). Guidance from the CFTC in the context of commodity forwards could support the reading that the execution of an offsetting Currency Forward does not result in recharacterization of the Currency Forward as a swap. Specifically, the CFTC has interpreted the exclusion from regulation as a futures contract applicable to nonfinancial commodity forwards to apply to contracts that allow the parties to “book-out” the forward to avoid delivery.¹⁴⁹ Although the exclusion depends, among other factors, on the parties’ intention to make and accept physical delivery, in the context of nonfinancial forwards, the CFTC reasoned that the forward exclusion should still apply to contracts having a “book-out” feature because no party would be under any obligation to execute a book-out and each party could unilaterally require settlement through physical delivery.¹⁵⁰ In the Swap Adopting Release, the CFTC indicated that this guidance would apply to forwards in all nonfinancial commodities.¹⁵¹ Although the CFTC did not extend the guidance to financial derivatives, the underlying rationale—that a transaction should not be recharacterized because of a subsequent action that the parties are not obligated to take—arguably applies equally to offsetting Currency Forwards.

B. Margin Requirements for Physically-Settled Foreign Exchange Products

Although the uncleared swap margin rules adopted by the CFTC and the prudential regulators do not apply to Currency Forwards and Physically-Settled FX Swaps,¹⁵² in 2013, the Federal Reserve issued a Supervision and Regu-

lation Letter (“SR 13-24”),¹⁵³ which incorporated guidelines issued by the Basel Committee on Banking Supervision (the “BCBS Guidelines”). The BCBS Guidelines apply to “banking institutions”¹⁵⁴ and provide for collection and posting of variation margin on physically-settled foreign exchange transactions¹⁵⁵ with “financial institutions and systemically important non-financial entities.”¹⁵⁶ Because the largest swap dealers are generally subject to the Federal Reserve’s jurisdiction, it is possible that SR 13-24 could be interpreted to negate the plain language in the swap margin regulations that excludes Currency Forwards and Physically-Settled FX Swaps. Given that variation margin has historically not been collected on many Currency Forwards and Physically-Settled FX Swaps, if SR 13-24 were applied as a regulatory requirement (notwithstanding that the guidance was not subjected to notice and comments), the application could create material operational and financial obligations for both dealers and end users that are deemed to be “financial institutions” for purposes of the guidance. SR 13-24 and the BCBS Guidelines also state that spot transactions fall under the guidance.

SR 13-24 has also been a source of confusion among both banking institutions and their non-bank counterparties because of the lack of formal guidance provided by the Federal Reserve regarding the scope or details of the margin requirements. It is unclear why the Federal Reserve adopted these requirements through a Supervision and Regulation Letter rather than a formal rulemaking, particularly given that it adopted detailed margin rules for other derivatives. Among the details that are addressed specifically in the Prudential Regulator Margin Rules but that are left unanswered in SR 13-24

are: (i) the definition of the term “financial institutions,” with whom the banking institutions are required to post and collect variation margin,¹⁵⁷ (ii) the minimum transfer amount that will apply to margin transfers,¹⁵⁸ (iii) the types of collateral that are permitted as variation margin, and what haircuts may apply to such collateral,¹⁵⁹ and (iv) the effective date of the requirements.

C. Shifting ECP Status

As discussed above, Currency Transactions entered into with non-ECPs are subject to the Retail Forex rules, and Currency Transactions between ECPs are subject to the swap rules unless, in either case, the applicable transaction is excluded from regulation. There are several prongs of the ECP definition through which a person can qualify as an ECP; however, a natural person (other than floor brokers or associated persons of broker-dealers) will qualify as an ECP only if he or she has assets invested on a discretionary basis in excess of \$10,000,000, or in excess of \$5,000,000 if he or she is using the transactions to manage risk associated with his or her assets or liabilities.¹⁶⁰ Because ECP status generally depends upon the amount of a person’s assets, a person’s status can shift over time, and a financial institution transacting with such a person would be required to change which rules they are complying with depending on the person’s ECP status. Due to the significant differences between the requirements of the rules applicable to Retail Forex transactions and those applicable to swaps, financial institutions use different systems, documentation and legal entities to comply with the two sets of rules. Retail Forex transactions are generally executed on separate platforms, pursuant to separate documentation and customer reporting and different margining systems from

Currency Transactions conducted with ECPs (including swap transactions). Thus, there are significant legal and operational obstacles to switching between compliance with the two different rule sets. Further, if a dealer entered into a Currency Transaction with a person when the person was an ECP, but that person later became a retail investor, there is uncertainty as to whether or how the dealer could subsequently amend or close out that transaction. While the CFTC has confirmed that a party’s ECP status only needs to be confirmed prior the execution of a swap and not throughout the life of the swap,¹⁶¹ the CFTC has not specifically addressed whether the close out or amendment of a swap could be deemed to be a new “swap” that requires both parties to be ECPs at the time of such close out or amendment.¹⁶²

Some market participants have suggested that a financial institution should have the right to opt-in to the Retail Forex rules rather than the swaps rules for transactions with ECPs.¹⁶³ On this point, the Federal Reserve has indicated that a banking institution subject to its jurisdiction may comply with its Retail Forex rules when transacting with a Retail Forex customer who later becomes an ECP,¹⁶⁴ but the CFTC has not provided additional guidance on this point.

Conclusion

The regulation of Currency Transactions is one of the most nuanced areas of financial regulation and has evolved substantially in recent years. Given continued instances of abuses in currency trading, including claims of undisclosed markups by custodial banks, large-scale losses by retail investors and retail currency trading firms, and manipulation of exchange rates, it would seem likely that, notwithstanding the new administra-

tion's potential focus on paring back unwieldy regulation, Currency Transactions will remain subject to significant regulatory oversight in the United States. We also believe, however, that there are useful areas within the current framework of regulations, which we have highlighted in this article, that could be rationalized in order to provide greater certainty to the currency markets.

ENDNOTES:

*David Aron was one of the principal draftsmen of the joint CFTC-Securities and Exchange Commission ("SEC") rulemaking further defining the term swap (Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping, 77 Fed. Reg. 48,207 (Aug. 13, 2012) ("Swap Adopting Release")), including the foreign exchange and currency sections thereof. Mr. Aron was also the principal draftsman of the joint CFTC-SEC rulemaking further defining the term "eligible contract participant." See Further Definition of "Swap Dealer," "Security-Based Swap Dealer," "Major Swap Participant," "Major Security-Based Swap Participant" and "Eligible Contract Participant," 77 Fed. Reg. 30,596 (May 23, 2012) ("Swap Entity Definition Release"). The research for this paper conducted by Mr. Aron was done in his personal capacity and not in his official capacity as an employee of the CFTC. The analyses and the conclusions expressed in this paper are those of Mr. Aron, and do not reflect the views of other DMO employees, other CFTC staff, the CFTC itself, or the United States government. P. Georgia Bullitt and Jed Doench assisted in the preparation of this article and in formulating the conclusions. The authors would like to thank Annie Fox, an associate at Willkie Farr & Gallagher LLP, whose research efforts were invaluable.

¹Wall Street Transparency and Accountability Act of 2010, Pub. L. No. 111-203, 124 Stat. 1641.

²Generally, foreign exchange and currency derivatives entered into with institutional investors that qualify as eligible contract participants ("ECPs") under Section 1a(18) of the CEA are regulated as swaps subject to the jurisdiction of the CFTC, whereas foreign exchange and currency derivatives entered into with retail customers that do not qualify as ECPs are subject to a separate set of rules applicable to retail foreign exchange. While the retail foreign exchange rules all originate from the CEA, jurisdiction over retail foreign exchange transactions varies depending on the financial institution trading with the retail counterparty, as discussed later in this article.

³FX options that are listed on a national securities exchange registered under Section 6(a) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), are regulated as securities under the Exchange Act and are subject to the jurisdiction of the SEC, whereas foreign exchange futures products listed on designated contract markets are subject to the jurisdiction of the CFTC under the CEA. Over-the-counter foreign exchange transactions executed between ECPs are generally subject to the jurisdiction of the CFTC.

⁴In this article, we use the term "physically-settled" to describe foreign exchange and currency transactions that are settled via an exchange of two settlement payments, each in a different currency. Such transactions are also referred to in the market as "deliverable" transactions and are distinguished from "non-deliverable" transactions that are settled via one payment in a single currency. References to physical settlement in this article do not relate to a transaction's eligibility for the forward contract exclusion for futures and swaps pursuant to CEA Sections 1a(27) and 1a(47)(B)(ii), respectively, which are separate exclusions that incorporate concepts of physical settlement or delivery.

⁵Certain exclusions and exemptions from some of these requirements are available.

⁶See Determination of Foreign Exchange Swaps and Foreign Exchange Forwards Under the Commodity Exchange Act, 77 Fed. Reg.

69,694 (Nov. 20, 2012) (“Treasury Determination”) (issued pursuant to Section 1a(47)(E) of the CEA).

⁷CEA § 1a(24).

⁸CEA § 1a(25).

⁹See CEA § 2(c)(2)(C)(i)(II)(bb)(AA).

¹⁰Retail Forex transactions includes “rolling spot” transactions, which are Currency Transactions that are nominally booked as spot transactions but that are continually rolled over, and thus are economically similar to forward or futures transactions.

¹¹Securities exchanges that list currency options include NASDAQ PHLX LLC and International Securities Exchange, LLC.

¹²CEA §§ 2(c)(2)(A)(i) and (iii).

¹³CEA § 2(c)(2)(E)(iii)(I).

¹⁴See Letter from Donald L. E. Ritger, Acting General Counsel, Department of the Treasury, to the Hon. Herman E. Talmadge (July 30, 1974), reprinted in 1974 U.S.C.C.A.N. 5843, 5887-88 (“The Department feels strongly that foreign currency futures trading, other than on organized exchanges, should not be regulated by the new agency. Virtually all futures trading in foreign currencies in the United States is carried out through an informal network of banks and dealers. . . . The participants in this market are sophisticated and informed institutions, unlike the participants on *organized* exchanges, which, in some cases, include individuals and small traders who may need to be protected by some form of governmental regulation. . . . Where the need for regulation of transactions on other than organized exchanges does exist, this should be done through strengthening existing regulatory responsibilities now lodged in the Comptroller of the Currency and the Federal Reserve.”).

¹⁵The Treasury Amendment provided: “Nothing in this Act shall be deemed to govern or in any way be applicable to transactions in foreign currency . . . unless such transactions involve the sale thereof for future delivery conducted on a board of trade.” 88 Stat. 1395, 7 U.S.C. § 2(ii).

¹⁶See Trading in Foreign Currencies for Fu-

ture Delivery, 50 Fed. Reg. 42,983, 42,984 (Oct. 23, 1985) (“The [CFTC] has, since its creation, consistently been of the view that the Treasury Amendment which, as more fully discussed below, excludes from the [CFTC’s] exclusive jurisdiction over futures contracts, certain off-exchange transactions in foreign currencies and other enumerated financial instruments, applies only when such transactions are entered into by and between banks and certain other sophisticated and informed institutional participants.”) (internal citations omitted).

¹⁷*Id.*; *CFTC Fraud Advisories: Foreign Currency Trading (Forex) Fraud*, CFTC, http://www.cftc.gov/ConsumerProtection/FraudAwarenessPrevention/CFTCFraudAdvisories/fraudadv_forex (last visited Dec. 5, 2016).

¹⁸See Exemption for Certain Swap Agreements, 58 Fed. Reg. 5587 (Jan. 22, 1993) (adopting Part 35 of the CFTC’s regulations, which implemented a safe harbor from regulation for certain swap agreements (including FX swap agreements) between “eligible swap participants”).

¹⁹See, e.g., *CFTC v. Baragosh*, 278 F.3d 319 (4th Cir. 2002) (“Transactions in foreign currency were not subject to [CFTC] jurisdiction in the period at issue in this case if they were ‘large-scale, customized, negotiated, bilateral transactions between sophisticated financial professionals.’ But they were subject to its jurisdiction if they were small, standardized, offered as-is, and mass marketed to individuals.”) (internal citations omitted); *CFTC v. Standard Forex*, No. cv-93-0088, 1993 WL 809966 (E.D.N.Y. 1993) (deferring to the interpretation of the CFTC that the Treasury Amendment does not limit the CFTC’s jurisdiction over off-exchange foreign currency transactions to the general public). See also *Salomon Forex, Inc. v. Tauber*, 8 F.3d 966, 978 (4th Cir. 1993) (“We hold *only* that individually-negotiated foreign currency option and futures transactions between sophisticated, large-scale foreign currency traders fall within the Treasury Amendment’s exclusion from CEA coverage.”) (emphasis added).

²⁰*Dunn v. CFTC*, 519 U.S. 465 (1997).

²¹*See id.* at 473.

²²*CFTC v. Frankwell Bullion Ltd.*, 99 F.3d 299, 305 (9th Cir. 1996) (“We hold, as the legislative history indicates, that Congress intended the Treasury Amendment to exempt all off-exchange transactions in foreign currency.”).

²³*See* The President’s Working Group on Financial Markets, *Over-the-Counter Derivatives and the Commodity Exchange Act (1999)* (“PWG Report”) at 26-27.

²⁴Pub. L. No. 106-554, 114 Stat. 2763.

²⁵CEA § 2(c)(2)(B)(ii) (2001) (amended 2008 and 2010).

²⁶The CFMA added a definition of an ECP in Section 1a(12) of the CEA (subsequently renumbered as 1a(18) by Dodd-Frank). The definition is very similar to the current definition and contained a list of different persons qualifying as ECPs including, among others, financial institutions, regulated insurance companies, registered investment companies, commodity pools with total assets exceeding \$5,000,000 and operated by a person subject to regulation by the CFTC or a similar foreign regulator, entities and individuals with total assets exceeding \$10,000,000, employee benefit plans subject to the Employee Retirement Income Security Act of 1974 with total assets exceeding \$5,000,000 or managed by a registered investment adviser, governmental entities, registered broker-dealers and registered FCMs.

²⁷Prior to the adoption of the CFMA, there had been concerns that OTC derivatives, including OTC currency derivatives, could be deemed illegal off-exchange futures contracts. *See* PWG Report at 10-13. Section 102 of the CFMA revised Section 2(c) of the CEA to exclude from the CEA foreign currency transactions, other than transactions conducted on an “organized exchange” or securities exchange, where organized exchange was defined to include a trading facility that permits trading by persons who are not ECPs. CFMA Section 103 added Section 2(d) to the CEA, which generally provided that the CEA would not govern any transaction in an excluded commodity (which was defined to include any exchange rate or currency) entered into between

ECPs and that is not executed on a trading facility. CFMA Section 105 added a broader exclusion to Section 2(g) of the CEA, which generally excluded from regulation under the CEA any swap transactions that were entered into between ECPs, subject to individual negotiation, and not executed or traded on a trading facility.

²⁸*See Testimony of Sharon Brown-Hruska, Acting Chairman CFTC, Before the House Subcommittee on General Farm Commodities and Risk Management Committee on Agriculture, U.S. House of Representatives, CFTC* (Mar. 3, 2005), <http://www.cftc.gov/opa/speeches05/opabrown-hruska-27.htm>.

²⁹*See NFA Notice I-03-14, New Forex Rules Will Become Effective on December 1, 2003*, Nat. Futures Ass’n (Oct. 2, 2003), <https://www.nfa.futures.org/news/newsNotice.asp?ArticleID=1169> (announcing CFTC approval of NFA Compliance Rule 2-36, Sections 11 and 12 of the NFA Financial Requirements, NFA Interpretive Notice 9053, and related rules regarding Retail Forex that are applicable to “Forex Dealer Members”).

³⁰*The Commodity Futures Modernization Act of 2000 and Recent Market Developments: Hearing Before the Comm. On Banking, Housing, and Urban Affairs*, 109th Cong. 1 (2005) (prepared statement of Daniel J. Roth, President and Chief Executive Officer, National Futures Association) (“Since passage of the CFMA, a number of firms—that do not engage in any other regulated business—have nonetheless registered as FCMs to qualify to be an otherwise regulated entity and have become NFA Forex Dealer Members for the sole purpose of acting as counterparties to retail customers in these transactions.”).

³¹*Id.* (“Though less than 1 percent of our member firms, forex dealers have accounted for 50 percent of our emergency enforcement actions and over 10 percent of our arbitration docket.”).

³²CEA § 2(c)(2)(B)(ii)(III) (prior to subsequent amendments).

³³*CFTC v. Zelener*, 373 F.3d 861 (7th Cir. 2004). *See also CFTC v. Erskine*, 512 F.3d 309 (6th Cir. 2008).

³⁴*Zelener*, 373 F.3d at 867-68 (“Our decision

in *Nagel* observed that in the great majority of situations even opinions emphasizing ‘the totality of the circumstances’ boil down to whether trading has occurred in fungible contracts.”).

³⁵*Id.* at 868.

³⁶*Id.* at 868-69.

³⁷Food, Conservation, and Energy Act of 2008, Public Law 110-246, 122 Stat. 1651, 2189-2204 (2008).

³⁸See CEA § 2(c)(2)(B)(i)(II). The CRA also created a \$20 million minimum capital requirement for FCMs and RFEDs that offer Retail Forex.

³⁹CEA § 2(c)(2)(C)(i)(I)(bb).

⁴⁰CEA § 2(c)(2)(C)(i)(II)(bb)(AA).

⁴¹Wall Street Transparency and Accountability Act of 2010 (“Title VII”).

⁴²See S. Rep. No. 111-176 (2010) at 29-35.

⁴³See Treasury Determination.

⁴⁴See CEA § 2(c)(2)(E)(ii)-(iii) (requiring disclosure, recordkeeping, capital and margin, reporting, business conduct, documentation and other standards).

⁴⁵See CFTC Release PR7056-14, CFTC Orders Five Banks to Pay over \$1.4 Billion in Penalties for Attempted Manipulation of Foreign Exchange Benchmark Rates (Nov. 12, 2014), <http://www.cftc.gov/PressRoom/PressReleases/pr7056-14>. See also *In re Citibank, N.A.*, CFTC Docket No. 15-03 (Nov. 11, 2014); *In re JPMorgan Chase Bank, N.A.*, CFTC Docket No. 15-04 (Nov. 11, 2014); *In re The Royal Bank of Scotland plc*, CFTC Docket No. 15-05 (Nov. 11, 2014); *In re UBS AG*, CFTC Docket No. 15-06 (Nov. 11, 2014); *In re HSBC Bank plc*, CFTC Docket No. 15-07 (Nov. 11, 2014).

⁴⁶See Daniel Schäfer, Alice Ross and Delphine Strauss, *Foreign Exchange: The Big Fix*, Financial Times (Nov. 12, 2013), <https://www.ft.com/content/7a9b85b4-4af8-11e3-8c4c-00144feabdc0>.

⁴⁷See Plea Agreement, *U.S. v. Barclays PLC*, Case No. 3:15-cr-00077 (D. Conn. 2015); Plea Agreement, *U.S. v. Citicorp*, Case No. 3:15-cr-

00078 (D. Conn. 2015); Plea Agreement, *U.S. v. JPMorgan Chase & Co.*, Case No. 3:15-cr-00079 (D. Conn. 2015); *U.S. v. The Royal Bank of Scotland PLC*, Case No. 3:15-cr-00080 (D. Conn. 2015). See also Five Major Banks Agree to Parent-Level Guilty Pleas, Dep’t of Just. (May 20, 2015), <https://www.justice.gov/opa/pr/five-major-banks-agree-parent-level-guilty-pleas>.

⁴⁸ *Manhattan U.S. Attorney and New York State Attorney General Announce \$714 Million Proposed Settlement with the Bank of New York Mellon Over Fraudulent Foreign Exchange Trading Practices*, Dep’t of Just. U.S. Att’y’s Off. S.D.N.Y. (Mar. 19, 2015), <https://www.justice.gov/usao-sdny/pr/manhattan-us-attorney-and-new-york-state-attorney-general-announce-714-million-proposed>. See also *In the Matter of The Bank of New York Mellon*, Investment Company Act Release No. 32151 (June 13, 2016) (The SEC concluded that BNYM willfully violated Section 34(b) of the Investment Company Act, which prohibits both untrue statements of material facts and fraudulent omission of material facts in documents such as registration statements, applications, reports and accounts. The SEC also concluded that BNYM violated Section 31(a) of the Investment Company Act and the corresponding Rule 31a-1(b), both of which specify that registered investment companies must keep records of certain transaction information.).

⁴⁹See *State Street Bank to Pay \$382 Million to Settle Allegations of Fraudulent Foreign Currency Exchange Practices*, Dep’t of Just. (July 26, 2016), <https://www.justice.gov/opa/pr/state-street-bank-pay-382-million-settle-allegations-fraudulent-foreign-currency-exchange>. See also *In the Matter of State Street Bank and Trust Company*, Investment Company Act Release No. 32390 (Dec. 12, 2016).

⁵⁰*Hill. v. State Street Corporation*, Fed. Sec. L. Rep. (CCH) ¶ 96,504 (D. Mass. 2011).

⁵¹*Id.*

⁵²Patrick Graham, *Swiss Franc Jumps 30 Percent After Swiss National Bank Dumps Euro Ceiling*, Reuters (Jan. 15, 2015), <http://www.reuters.com/article/us-markets-franc-idUSKBN0K016Y20150115>.

⁵³Ira Iosebashvili, Andrew Ackerman and Alexandra Wexler, *Surge of Swiss Franc Triggers Hundreds of Millions in Losses*, Wall St. J. (Jan. 16, 2015), <http://www.wsj.com/articles/swiss-franc-move-cripples-currency-brokers-1421371654>.

⁵⁴See NFA Notice I-16-27 (Jan. 21, 2015) (increasing the security deposit requirements under Section 12 of the NFA Financial Requirements for transactions for Retail Forex transactions in the Swiss franc, Swedish krona and Norwegian krone).

⁵⁵Andrew Ackerman, *CFTC Reviews Retail Forex Trading Rule Following FXCM Debacle*, Wall St. J. (Jan. 16, 2015), <http://www.wsj.com/articles/cftc-reviewing-retail-forex-trading-rules-following-fxcm-debacle-1423673421>.

⁵⁶A Forex Dealer Member is defined in NFA Bylaw 306 as any NFA member that enters into Retail Forex transactions, and generally includes RFEDs as well as FCMs that enter into Retail Forex transactions but that are not required to register as RFEDs.

⁵⁷See CFTC Release PR7219-15, CFTC Approves National Futures Association Rules Enhancing Protections for Retail Forex Customers (Aug. 27, 2015), <http://www.cftc.gov/PressRoom/PressReleases/pr7219-15>.

⁵⁸See NFA Notice I-15-04 (Jan. 21, 2015) (increasing the security deposit requirements under Section 12 of the NFA Financial Requirements for transactions for Retail Forex transactions in the Mexican peso, Japanese yen and New Zealand dollar).

⁵⁹See Lananh Nguyen, *Gain Capital Is Set to Become the Biggest U.S. Retail FX Provider*, Bloomberg (Feb. 24, 2017), <https://www.bloomberg.com/news/articles/2017-02-24/gain-capital-take-top-slot-in-u-s-retail-fx-as-fxcm-exits>.

⁶⁰Forex Capital Markets, LLC, CFTC Docket No. 17-09 (Feb. 6, 2017).

⁶¹Recently, two former currency traders at two large banks pleaded guilty to engaging in criminal violations of U.S. antitrust law by conspiring to manipulate foreign currency transactions. See Plea Agreement, *U.S. v. Cummins*,

Case No. 1:17-cr-00026 (S.D.N.Y. 2017); Plea Agreement, *U.S. v. Katz*, Case No. 1:17-cr-00003 (S.D.N.Y. 2017).

⁶²FX Global Code Public Update on Adherence (May 2016), http://www.bis.org/mktc/fxwg/am_may16.pdf.

⁶³In this context, the term “forward contract” is not intended to connote any connection to the forward contract exclusion from the swap definition in Section 1a(47)(B)(ii) of the CEA, which is not available for foreign exchange transactions, or to Section 1a(27) of the CEA, which, as noted above, incorporates concepts of physical settlement or delivery.

⁶⁴NDFs were described in greater detail by the CFTC as follows: “An NDF generally is similar to a forward foreign exchange contract, except that at maturity, the NDF does not require physical delivery of currencies and is typically settled in U.S. dollars. The other currency, usually an emerging market currency subject to capital controls, is therefore said to be ‘non-deliverable.’ If the spot market exchange rate on the settlement date is greater (in foreign currency per dollar terms) than the previously agreed forward exchange rate, the party to the contract that is long the emerging market currency must pay its counterparty the difference between the contracted forward price and the spot market rate, multiplied by the notional amount.” Further Definition of “Swap,” “Security-Based Swap,” and “Security-Based Swap Agreement”; Mixed Swaps; Security-Based Swap Agreement Record-keeping, 76 Fed. Reg. 29,818, 29,836 (May 23, 2011) (citations omitted).

⁶⁵See CFTC Rule 1.3(xxx)(2)(i)(F) and Exchange Act Rule 3a69-2(b)(1)(vi) (2016); Swap Adopting Release at 48,254-56. The Swap Adopting Release indicated that NDFs are swaps pursuant to Section 1a(47)(A)(iii) of the CEA because they provide for a future payment based on an exchange rate, which is an “interest or other [rate]” within the meaning of clause (A)(iii).

⁶⁶See Petition from the Investment Company Institute, ICI Global, ABA Securities Association, and American Bankers Association, Petition for Exemptive Relief for Non-Deliverable For-

eign Exchange Forwards to CFTC (Feb. 26, 2013), <https://www.aba.com/Advocacy/LetterstoCongress/Documents/2-26-13PetitionforExemptiveRelief.pdf>.

⁶⁷CFTC Rule 1.3(xxx)(2)(i)(B) and Exchange Act Rule 3a69-2(b)(1)(ii) (2016); Swap Adopting Release at 48,254.

⁶⁸See Swap Adopting Release at 48,256.

⁶⁹CEA § 1a(47)(A)(iii)(VII).

⁷⁰FX window forwards are used when parties to the contract do not know the specific date on which they will need the currency (for example, because they do not know when, within a certain date range, a foreign supplier will ship a particular shipment). See, e.g., *Window Forward Contracts*, California Bank & Trust, <https://www.calbanktrust.com/business-banking/international-banking/foreign-exchange-services/window-forward-contracts.html> (last visited Dec. 6, 2016) (noting that “it’s often challenging to determine exactly when a payment will take place. Production or shipment dates, the conclusion of legal matters, and invoice discounting all can impact when payments are released.”).

⁷¹See CEA § 1a(19) (defining a foreign exchange forward as “a transaction that *solely* involves the exchange of 2 different currencies on a specific future date at a fixed rate agreed upon on the inception of the contract covering the exchange”) (emphasis added).

⁷²See Treasury Determination (issued pursuant to Section 1a(47)(E) of the CEA).

⁷³CEA § 2(h).

⁷⁴CEA § 2(h)(8).

⁷⁵17 C.F.R. Parts 43, 45 and 46 (2016).

⁷⁶17 C.F.R. §§ 23.150-23.161 (2016); 12 C.F.R. Part 45 (2016) (Office of the Comptroller of the Currency (“OCC”) Rules); 12 C.F.R. Part 237 (2016) (Federal Reserve Rules); 12 C.F.R. Part 349 (2016) (Federal Deposit Insurance Corporation (“FDIC”) Rules); 12 C.F.R. Part 624 (2016) (Farm Credit Administration Rules); 12 C.F.R. Part 1221 (2016) (Federal Housing Finance Agency Rules). We refer to the OCC, Federal Reserve, FDIC, Farm Credit Administra-

tion and Federal Housing Finance Agency margin rules, which are nearly identical, as the “Prudential Regulator Margin Rules” and cite generically to the subsections of the rules (e.g., § —.1).

⁷⁷CFTC Rules 23.400 through 23.451.

⁷⁸CFTC Rules 23.500 through 23.506.

⁷⁹Swaps dealers and major swap participants are generally subject to the same requirements under Dodd-Frank. Because there are not any major swap participants currently registered with the CFTC, for brevity we will just refer to swap dealers.

⁸⁰CFTC Rule 45.2.

⁸¹See CEA § 2(e) (“It shall be unlawful for any person, other than an eligible contract participant, to enter into a swap unless the swap is entered into on, or subject to the rules of, a board of trade designated as a contract market under section 5.”).

⁸²The CFTC’s Global Markets Advisory Committee (“GMAC”) held a meeting to discuss NDF clearing on October 9, 2014. At that meeting, Brian O’Keefe, then a Deputy Director in the CFTC’s Division of Clearing and Risk, said that the staff is evaluating a request for mandatory clearing for cash-settled non-deliverable forwards in 12 currency pairs with tenors of up to two years. *FIA Special Report: CFTC Examines FX Clearing Mandate*, <https://fia.org/articles/fia-special-report-cftc-examines-fx-clearing-mandate>.

⁸³After the October 9, 2014 GMAC meeting, GMAC’s FX Markets Subcommittee provided GMAC a memorandum essentially advocating a “go slow” approach. See Memorandum from the Foreign Exchange Markets Subcomm. on Response to Request for Recommendation on an FX NDF Mandate to Global Markets Advisory Comm. (Dec. 5, 2014) (on file with CFTC), http://www.cftc.gov/idc/groups/public/@aboutcftc/documents/file/gmac_fxndfmandate122214.pdf.

⁸⁴See Chris Barnes, *NDF Volumes—It’s all about Clearing*, Clarus Financial Technology (Dec. 21, 2016), <https://www.clarusft.com/ndf-volumes-its-all-about-clearing/>.

⁸⁵The SEFs that offer foreign exchange and

currency products include ICAP SEF (US) LLC, BGC Derivatives Markets, L.P., tpSEF Inc., GFI Swaps Exchange LLC and Tradition SEF, Inc., among others. The Futures Industry Association (“FIA”) has made available an interactive online tool that provides detailed information about SEF trading activity. *SEF Tracker Overview*, FIA, <http://fia.org/sef-tracker-overview>.

⁸⁶See CFTC Rules 23.153 and 23.154; Prudential Regulator Margin Rules §§ _____.3 and _____.4.

⁸⁷CEA § 4s(e)(4) (2015).

⁸⁸CFTC 23.161(a)(2); Prudential Regulator Margin Rules § _____.1.

⁸⁹See CFTC Letter No. 17-11 (Feb. 13, 2017).

⁹⁰See Initial Examinations for Compliance with Minimum Variation Margin Requirements for Non-Cleared Swaps and Non-Cleared Security Based Swaps, SR 17-3 (Feb. 22, 2017); Initial Examinations for Compliance With Final Rule Establishing Margin Requirements for Non-Cleared Swaps and Non-Cleared Security-Based Swaps, OCC Bulletin 2017-12 (Feb. 23, 2017).

⁹¹See CFTC Rules 23.500 through 23.506.

⁹²See Letter from the Global Financial Market Association’s Global Foreign Exchange Division and The Financial Services Roundtable to Gary Barnett, Director, Division of Swap Dealer and Intermediary Oversight, CFTC (June 5, 2013).

⁹³CEA § 1a(47)(E)(i).

⁹⁴See Treasury Determination.

⁹⁵CEA § 1a(24).

⁹⁶CEA § 1a(47)(E)(iv).

⁹⁷Although Section 1a(47)(E)(iv) of the CEA only references Currency Forwards and Physically-Settled FX Swaps being subject to the “business conduct standards,” the CFTC has interpreted this to include its swap trading documentation rules. See Treasury Determination at 69,699 n.51; CFTC Letter No. 13-38 (June 27, 2013).

⁹⁸*Id.* § 1a(47)(E)(iii).

⁹⁹*Id.* § 1a(47)(F)(i). See also CEA § 1b(c).

¹⁰⁰Treasury Determination at 69,695 n.8 (“Thus, as a result of this determination pursuant to sections 1a(47)(E) and 1b of the CEA, foreign exchange swaps and forwards would not be subject to margin requirements under the CEA.”).

¹⁰¹See Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 81 Fed. Reg. 636, 638 (Jan. 6, 2016) (to be codified at 17 C.F.R. pts. 23 and 140) (“CFTC Margin Adopting Release”); Margin and Capital Requirements for Covered Swap Entities, 80 Fed. Reg. 74,840, 74,842 (Nov. 30, 2015) (to be codified at 12 C.F.R. pts. 45, 237, 349, 624 and 1221). Nevertheless, both the CFTC’s and the prudential regulators’ margin rules take into account Currency Forwards and Physically-Settled FX Swaps for the purposes of certain thresholds within the rules. For example, the compliance dates for the initial margin requirements within the rules depend upon the size of a counterparty’s positions, and include Currency Forward and Physically-Settled FX Swap positions in this calculation. See CFTC Margin Adopting Release at 675-76; Prudential Regulator Margin Rules § _____.1(e).

¹⁰²See Managing Foreign Exchange Settlement Risks for Physically Settled Transactions, SR 13-24 (Dec. 23, 2013).

¹⁰³See CEA §§ 2(c)(2)(B)(i) and 2(c)(2)(C)(i) (providing that the Retail Forex provisions of the CEA apply to any agreement, contract, or transaction in foreign currency with a person that is not an ECP that is a contract of sale of a commodity for future delivery (or an option on such contract), an option (other than an option traded on a securities exchange), or entered into on a leveraged, margined or financed basis).

¹⁰⁴CEA § 1a(18)(A)(iv).

¹⁰⁵See, e.g., Comment Letter from Willkie Farr & Gallagher LLP re: Further Definition of “Swap Dealer,” “Security-Based Swap Dealer,” “Major Swap Participant” and “Eligible Contract Participant” (Feb. 22, 2011).

¹⁰⁶See CFTC Rule 1.3(m)(8); Swap Entity Definition Release at 30,659.

¹⁰⁷The rule provides that an FX Pool is not

required to look through to the ECP status of investors in any feeder fund that invests in the FX Pool (an “Investor Pool”), provided that none of the FX Pool, any Investor Pool, or any other pool in which the FX Pool holds a direct or indirect interest was structured to evade the Retail Forex rules by permitting non-ECPs to participate in OTC FX transactions. *See* CFTC Rule § 1.3(m)(5)(ii) (2016); Swap Entity Definition Release at 30,651-52.

¹⁰⁸*See* Swap Adopting Release at 48,256-57.

¹⁰⁹*Id.* at 48,257.

¹¹⁰The CFTC and SEC described a “securities conversion transaction” as an agreement, contract or transaction for the purchase or sale of an amount of foreign currency equal to the price of a foreign security with respect to which (i) the security and related foreign currency transactions are executed contemporaneously in order to effect delivery by the relevant securities settlement deadline and (ii) actual delivery of the foreign security and foreign currency occurs by such deadline. *Id.*

¹¹¹*Id.*

¹¹²*Id.* at 48,256-57.

¹¹³Swap Adopting Release at 48,229 n.226 (citing 7 U.S.C. §§ 6(c), 6(d) and 9(a)(2) and 17 C.F.R. § 180.1).

¹¹⁴CEA § 2(c)(2)(B)(i). *See also* Swap Adopting Release at 48,258.

¹¹⁵CEA § 2(c)(2)(C)(i)(I)(bb).

¹¹⁶CEA § 2(c)(2)(C)(i)(II)(bb)(AA).

¹¹⁷Provided that the seller and buyer must have the ability to deliver and accept delivery, respectively, in connection with their line of business. CEA § 2(c)(2)(C)(i)(II)(bb)(BB).

¹¹⁸CEA § 2(c)(2)(B)(i)(I). Further, Section 2(c)(2)(C)(i)(II)(aa) exempts from the CFTC’s jurisdiction any “security that is not a security futures product.” The definition of security in Section 3(a)(10) of the Exchange Act includes “any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency.” 15 U.S.C. § 78c(a)(10) (2015).

¹¹⁹*See supra* note 110 for a description of securities conversion transactions. *See also* Swap Adopting Release at 48,257.

¹²⁰CEA § 2(c)(2)(B)(i)(II) and 2(c)(2)(E)(ii)(I).

¹²¹*See* Regulation of Off-Exchange Retail Foreign Exchange Transactions and Intermediaries, 75 Fed. Reg. 55,410 (Sep. 10, 2010); Retail Foreign Exchange Transactions; Conforming Changes to Existing Regulations in Response to the Dodd-Frank Wall Street Reform and Consumer Protection Act, 76 Fed. Reg. 56,103 (Sep. 12, 2011).

¹²²*See* Retail Foreign Exchange Transactions, 76 Fed. Reg. 40,779 (July 12, 2011). The FDIC’s rules apply to FDIC-supervised insured depository institutions, which include state nonmember banks and state savings associations.

¹²³*See* Retail Foreign Exchange Transactions, 76 Fed. Reg. 41,375 (July 14, 2011). The OCC’s rules apply to national banks, federal branches or agencies of foreign banks, and their operating subsidiaries, and federal savings associations.

¹²⁴*See* Retail Foreign Exchange Transactions (Regulation NN), 78 Fed. Reg. 21,019 (Apr. 9, 2013). The Federal Reserve’s rules apply to state member banks, uninsured state-licensed branches of foreign banks, financial holding companies, bank holding companies, savings and loan holding companies, agreement corporations and Edge Act corporations.

¹²⁵*See* Retail Foreign Exchange Transactions, 76 Fed. Reg. 41,676 (July 15, 2011); Retail Foreign Exchange Transactions, 78 Fed. Reg. 42,439 (July 16, 2013).

¹²⁶*See* Retail Foreign Exchange Transactions, 81 Fed. Reg. 33,374 (May 26, 2016).

¹²⁷*See* Retail Foreign Exchange Transactions, 78 Fed. Reg. at 42,439, 42,443 (July 16, 2013) (noting certain “key risks” including the lack of a central marketplace for Retail Forex, uncertainty about transaction costs, and the possibility for investors to lose more than their original investment).

¹²⁸*See* 17 C.F.R. § 5.5 (2016); 12 C.F.R.

§ 349.6 (2016) (FDIC Rule); 12 C.F.R. § 48.6 (2016) (OCC Rule); 12 C.F.R. § 240.6 (2016) (Federal Reserve Rule).

¹²⁹See 17 C.F.R. § 5.9(a) (2016); 12 C.F.R. § 349.9(a) (2016); 12 C.F.R. § 48.9 (2016); 12 C.F.R. § 240.9. NFA Financial Requirements, Section 12.

¹³⁰See 17 C.F.R. § 5.13 (2016); 12 C.F.R. § 349.10 (2016); 12 C.F.R. § 48.10 (2016); 12 C.F.R. § 240.10 (2016).

¹³¹See 17 C.F.R. § 5.2(b) (2016); 12 C.F.R. § 349.3(a) (2016); 12 C.F.R. § 48.3(a) (2016); 12 C.F.R. § 240.3(a) (2016).

¹³²See NFA Compliance Rule 2-36, Sections 11 and 12 to NFA Financial Requirements, and related rules and interpretive materials.

¹³³7 U.S.C. § 6b (2015).

¹³⁴*Id.* § 2(c)(2)(c)(iv).

¹³⁵*Id.* § 6c(a)(2).

¹³⁶*Id.* § 6c(a)(5).

¹³⁷*Id.* § 6c(a)(7).

¹³⁸*Id.* § 13(a)(2).

¹³⁹See Prohibition on the Employment, or Attempted Employment, of Manipulative and Deceptive Devices and Prohibition on Price Manipulation, 76 Fed. Reg. 41,398 (July 14, 2011) (“Rule 180.1 and 180.2 Adopting Release”).

¹⁴⁰*Id.* at 41,404.

¹⁴¹*Id.* at 41,405-06 (emphasis added). The CFTC has stated that it intends to interpret the “in connection with” requirement broadly, rather than restrictively. CFTC Fact Sheet: Anti-Manipulation and Anti-Fraud Final Rules, CFTC Off. of P. Aff., http://www.cftc.gov/idc/groups/public/@newsroom/documents/file/amaf_factsheet_final.pdf.

¹⁴²*Id.* at 41,407-08.

¹⁴³See *In re Amaranth Natural Gas Commodities Litig.*, 730 F.3d 170, 173 (2d Cir. 2013); *DiPlacido v. CFTC*, 364 F. App’x 657, 661 (2d Cir. 2009); *In re Cox*, CFTC No. 75-16, 1987 WL 106879, at *4 (July 15, 1987).

¹⁴⁴See Rule 180.1 and 180.2 Adopting Re-

lease at 41,407 (“In response to the comments received regarding this matter, the Commission reiterates that, in applying final Rule 180.2, it will be guided by the traditional four-part test for manipulation that has developed in case law arising under 6(c) and 9(a)(2). . . .”).

¹⁴⁵CFTC Reply Memorandum in Support of its Motion for Summary Judgment at 4, *CFTC v. Wilson*, No. 13-cv-7884 (S.D.N.Y. Jan. 12, 2016).

¹⁴⁶Memorandum and Order, *CFTC v. Wilson and DRW Investments*, No. 13-cv-7884 (S.D.N.Y. Sept. 30, 2016) at 26 (quoting *In re Amaranth Natural Gas Commodities Litig.*, 730 F.3d 170, 183 (2d Cir. 2013)).

¹⁴⁷For example, on June 1 two parties could execute a Currency Forward in which Party A will pay 100 GBP in exchange for Party B paying 120 USD on July 31. If, on July 15, the expected GBP/USD exchange rate for July 31 has moved to 1.15, the parties could close out the trade by executing an offsetting Currency Forward in which Party B pays 100 GBP and Party A pays 115 USD on July 31. The second Currency Forward would, if documented under a master netting agreement, result in an effective net settlement on July 31 of Party A receiving 5 USD (because Party B receives 100 GBP under the first transaction and pays 100 GBP on second transaction, while Party A receives 120 USD under the first transaction and pays 115 USD under the second transaction).

¹⁴⁸Swap Adopting Release at 48,255 n.539 (“[A] foreign exchange transaction, which initially is styled as or intended to be a ‘[Currency Forward],’ and which is modified so that the parties settle in a reference currency (rather than settle through the exchange of the 2 specified currencies), does not conform with the definition of ‘[Currency Forward]’ in the CEA.”).

¹⁴⁹See Statutory Interpretation Concerning Forward Transactions, 55 Fed. Reg. 39,188, 39,190 (Sep. 25, 1990) (known as the “Brent Interpretation”).

¹⁵⁰*Id.*

¹⁵¹Swap Adopting Release at 48,229.

¹⁵²See *supra* note 94.

¹⁵³See *Managing Foreign Exchange Settlement Risks for Physically Settled Transactions*, SR 13-24 (Dec. 23, 2013).

¹⁵⁴SR 13-24 states that its requirements apply to entities defined in SR letter 12-17 as Large Institution Supervision Coordinating Committee firms, large banking organizations, and U.S. operations of large foreign banking organizations, as well as any other banking organization that engages in significant foreign exchange activities.

¹⁵⁵SR 13-24 states: “The guidance applies to foreign exchange transactions that consist of two settlement payment flows. This includes spot transactions, forwards, swaps, deliverable options and currency swaps involving exchange of principal. It excludes instruments that involve one-way settlement payments, such as non-deliverable forwards, non-deliverable options and contracts for difference.”

¹⁵⁶See Basel Committee on Banking Supervision, *Supervisory Guidance for Managing Risks Associated with the Settlement of Foreign Exchange Transactions* (2013).

¹⁵⁷The prudential regulators’ uncleared swap margin rules contain a detailed definition of a “financial end user,” but it is unclear whether a “financial institution” under SR 13-24 is intended to be synonymous with a financial end user. See Prudential Regulator Margin Rules § —.2.

¹⁵⁸The BCBS Guidelines adopted through SR 13-24 merely provide that margin transfers should be subject to a “low” minimum transfer amount. The prudential regulators’ uncleared swap margin rules provide that a swap dealer is

not required to collect or post margin with a particular counterparty unless and until the combined amount of initial and variation margin that is required to be collected or posted is greater than \$500,000. See Prudential Regulator Margin Rules § —.5(b).

¹⁵⁹The BCBS Guidelines provide that covered firms should have collateral management policies and procedures that address collateral eligibility, collateral substitution, and collateral valuation. The prudential regulators’ margin rules set forth specific types of permitted collateral and haircut rates. See Prudential Regulator Margin Rules § —.8.

¹⁶⁰See CEA § 1a(18)(A)(xi)(I).

¹⁶¹See Business Conduct Standards for Swap Dealers and Major Swap Participants With Counterparties, 77 Fed. Reg. 9734, 9757 (Feb. 17, 2012).

¹⁶²Commenters had requested guidance on this issue, but the CFTC did not specifically address the issue. See *id.* at 9756 n.314 (“[T]he commenter questioned whether the loss of ECP status would limit the counterparty’s ability to terminate, modify or novate the swap.”).

¹⁶³See Letter from Timothy W. Cameron, Managing Director, Asset Mgmt. Group, SIMFA, to Jennifer J. Johnson, Secretary, Board of Governors of the Fed. Res. Sys., John Walsh, Acting Comptroller of the Currency, OCC, and Robert E. Feldman, Exec. Secretary, FDIC (Dec. 20, 2011).

¹⁶⁴See Retail Foreign Exchange Transactions (Regulation NN), 78 Fed. Reg. 21,019, 21,022 (Apr. 9, 2013).

