



U.S. COMMODITY FUTURES TRADING COMMISSION

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CFTC Letter No. 17-31
No-Action
June 30, 2017
Division of Clearing and Risk
Division of Market Oversight

Re: No-Action Relief from Commission Regulations 38.8(b), 38.10, 38.951 (in part) and 39.20(b)(2) and Parts 43 and 45 for Binary Options and Spread Contracts Traded on or Pursuant to the Rules of, and Cleared by, the North American Derivatives Exchange, Inc. (“Nadex”)

Introduction

The Division of Market Oversight (“DMO”) and the Division of Clearing and Risk (“DCR”) and, together with DMO, the “Divisions”) of the Commodity Futures Trading Commission (“CFTC” or “Commission”) are issuing this letter in response to a request from Nadex (“Request”).¹ Nadex is both a designated contract market (“DCM”) and a registered derivatives clearing organization (“DCO”). Nadex requested relief, for itself and its market participants, as applicable, from various swap data reporting requirements of Parts 43 and 45 of the CFTC’s regulations (collectively, the “Specified Regulations”) with respect to binary options and spread contracts traded on or pursuant to the rules of, and cleared by, Nadex (collectively, “Nadex Contracts”). The Divisions have considered the Request and are granting no-action relief subject to conditions, as described below.

Background

Nadex characterized its market as a short duration (most contracts expire intraday) retail market with very little open interest at the end of the trading day, eliminating long-term exposure for Nadex members. Nadex characterized the Nadex Contracts as having most of the characteristics of exchange traded futures or options thereon (fungibility, offset, exchange traded with standardized terms) with few of the indicia of traditional swaps (bilateral, traded over-the-counter and customized). Notwithstanding the foregoing, Nadex stated in the Request that the Nadex Contracts are swaps. Nadex requested relief from the Specified Regulations for the Nadex Contracts, which they described as fully collateralized, traded on a DCM and cleared through a DCO that clears only fully collateralized contracts.

¹ December 29, 2016 letter from Timothy G. McDermott, Nadex’s CEO, to then-DMO Director Vince McGonagle and then-DCR Acting Director Jeff Bandman.

The Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”)² amended the CEA by adding a definition of “swap.”³ The Dodd-Frank Act required the Commission and the Securities and Exchange Commission to further define jointly the term “swap.” In 2012, the Commissions jointly adopted such further definition.⁴ Nadex notes in the Request that “the instruments listed by Nadex have been classified as swaps pursuant to the Commodity Exchange Act, as amended”

Pursuant to the Dodd-Frank Act, the Commission promulgated various regulations applicable to swaps, including the Specified Regulations. The Specified Regulations impose swap reporting and recordkeeping obligations from which Nadex has requested relief.

Relief Requested

Nadex requested that the Divisions not recommend that the Commission take enforcement action against Nadex or its participants for failure to report Nadex Contracts to a swap data repository (“SDR”) or to fulfill any of the other requirements of the Specified Regulations. In support of its position, Nadex stated or represented, among other things, that:

- the Nadex Contracts are required to be fully collateralized;⁵
- Nadex will continue to comply with its end-of-day reporting requirements pursuant to Parts 16 and 39 of the Commission’s regulations;
- Nadex publishes its time and sales data, as well as a Daily Bulletin on the Nadex website in compliance with Parts 16, 38 and 39 of the Commission’s regulations;⁶ and
- Nadex could, with a minimal amount of work, publish the prices and quantities of transactions in Nadex Contracts on its website.

No-Action Relief and Related Conditions

The Divisions have decided to grant the requested relief, subject to certain conditions described below. Thus, the Divisions will not recommend that the Commission initiate an enforcement action against Nadex or its participants for failure to comply with Commission Regulations 38.8(b), 38.10, 38.951 (only to the extent it requires compliance with Part 45 of the Commission’s regulations) and 39.20(b)(2) and Parts 43 and 45 of the Commission’s regulations (the “Relevant Regulations”), or the related CEA provisions pursuant to which the Relevant

² Public Law 111–203, 124 Stat. 1376 (2010).

³ CEA § 1a(47), 7 U.S.C. § 1a(47).

⁴ Further Definition of “Swap,” “Security-Based Swap,” and “Security-Based Swap Agreement”; Mixed Swaps; Security-Based Swap Agreement Recordkeeping, 77 FR 48207, 48236 (Aug. 13, 2012).

⁵ In this regard, the Request states that each Nadex member is “fully aware of, and must fund, his or her maximum exposure at the time the order is placed.” Request at 4.

⁶ Nadex currently publishes time and sales data at https://www.nadex.com/sites/default/files/pdf/time-and-sales/20170608_timeandsales.pdf?0.7875418365690652 within 15 minutes of execution and a Daily Bulletin at <https://www.nadex.com/market-data>.

Regulations were promulgated, with respect to current or future Nadex Contracts, subject to the following conditions:⁷

- (1) Nadex continues to require all Nadex Contracts to be fully collateralized;⁸
- (2) Nadex continues to clear all of the Nadex Contracts and clears only Nadex Contracts;
- (3) commencing on October 31, 2017, Nadex publishes on its website the following time and sales data for all Nadex Contracts transactions promptly after execution thereof—business date, execution time, instrument type, periodicity, display name, expiration date, price (in USD), and volume;
- (4) Nadex continues to publish within 2 hours after the close of trading each trading day a Daily Bulletin with the following:
 - a. summary information for Nadex Contracts executed that day: date; instrument type; resource class (*i.e.*, commodities, currencies, equity indices, events); resource description (*i.e.*, specific commodity underlying the Nadex Contract); and volume; and
 - b. detailed information for Nadex Contracts executed that day (or, with respect to open interest, as of that day): date; name; type; period; volume; open interest; first trade; high trade; low trade; last trade; exp. value; buyer payout; and seller payout;⁹
- (5) Nadex continues to comply with all swap reporting and recordkeeping requirements of the CEA and Commission regulations applicable to it in its respective capacities as a DCM and a DCO, other than the Relevant Regulations, including, but not limited to, providing DMO with transactional information as described in Commission Regulation 16.02 and complying with the applicable requirements of Parts 38 and 39 of the CFTC’s regulations; provided, however, that Nadex can continue to rely on any

⁷ Some of these conditions regarding no-action relief would constitute a collection of information, as that term is defined in the Paperwork Reduction Act, 44 U.S.C. §§ 3501 *et. seq.* The Office of Management and Budget (“OMB”)—in accordance with 44 U.S.C. § 3507(d) and 5 C.F.R. §§ 1320.8 and 1320.10—has approved collection—3038-0049—entitled “Procedural requirements for requests for interpretative, no-action and exemptive letters,” for such purposes. This collection would encompass collections made as part of exemptive or no-action relief from the Commission. The public is not required to respond to a collection of information that does not have a valid OMB control number.

⁸ Condition (2) of Nadex’s DCO Registration Order states that “Nadex is permitted to clear, in its capacity as a DCO, fully collateralized . . . swaps.” For purposes of this relief, and as set forth in condition (3) of Nadex’s DCO Registration Order, “[a] [Nadex] [C]ontract . . . will be considered ‘fully collateralized’ [i]f Nadex holds, at all times, funds sufficient to cover the maximum possible loss that may be sustained upon liquidation of the [Nadex] [C]ontract.”

⁹ Nadex currently publishes a Daily Bulletin, which contains the information described above, by 5:30 p.m. Central Time.

previous Commission or staff relief from the swap reporting and recordkeeping requirements of the CEA and Commission regulations applicable to Nadex in its respective capacities as a DCM and a DCO, including, but not limited to, the relief provided in Nadex's DCM Registration Order, as amended, CFTC Staff Exemptive Letter 14-04 and CFTC Staff No-Action Letter Nos. 14-05 and 16-32 (the records required to be retained by this condition (5) are referred to below as the "Required Records");

- (6) no Nadex market participant clears a Nadex Contract through a third party clearing member; and
- (7) Nadex shall keep the Required Records open to inspection upon request by any representative of the Commission, the United States Department of Justice, or the Securities and Exchange Commission, or by any representative of a prudential regulator as authorized by the Commission. Copies of all such records shall be provided, at Nadex's expense, to any representative of the Commission upon request. Nadex shall provide copies of the Required Records either by electronic means, in hard copy, or both, as requested by the Commission, with the sole exception that copies of records originally created and exclusively maintained in paper form may be provided in hard copy only.

This letter expresses a staff position with respect to enforcement only and does not purport to state any legal conclusion regarding Nadex Contracts or the conduct of any person covered by the no-action relief provided herein. This letter and the no-action position taken herein represent the views of the Divisions only, and do not necessarily represent the positions or views of the Commission or of any other Commission division or office. This letter and the no-action position taken herein also are not binding on the Commission.¹⁰ Except as explicitly provided in this letter, the no-action positions taken herein do not excuse persons from compliance with any applicable requirements of the CEA or Commission regulations. Further, this letter, and the no-action position contained herein, is based upon the representations made to the Divisions. Any different, changed, or omitted material facts or circumstances might render this letter void. As with all no-action letters, the Divisions retain the authority to, in their discretion, further condition, modify, suspend, terminate or otherwise restrict the terms of the no-action relief provided herein. The Divisions expect to periodically review the relief provided and the associated conditions.

¹⁰ See Commission Regulation 140.99(a)(2) (stating that "[a] no-action letter binds only the issuing Division . . . and not the Commission or other Commission staff.").

If you have any questions concerning this letter, please contact: Dan Bucsa, Deputy Director, DMO—Data and Reporting Branch (“DAR”) at (202) 418-5435 or dbucsa@cftc.gov; David E. Aron, Special Counsel, DMO—DAR at (202) 418-6621 or daron@cftc.gov; Philip W. Raimondi, Special Counsel, DMO—Office of the Chief Counsel at (202) 418-5717 or praimondi@cftc.gov; or Andrea Musalem, Special Counsel, DCR at (202) 418-5167 or amusalem@cftc.gov.

Sincerely,

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John C. Lawton
Acting Director
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