



afme/

asifma

sifma

13 August 2012

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

**Re: Comment Letter on the Proposed Interpretive Guidance on the Cross-Border Application of Certain Swaps Provisions of the Commodity Exchange Act (RIN 3038–AD57) and the Proposed Exemptive Order Regarding Compliance with Certain Swap Regulations (RIN 3038–AD85)**

Dear Mr. Stawick:

The Global Financial Markets Association (**GFMA**)<sup>1</sup> appreciates the opportunity to provide the Commodity Futures Trading Commission (the **Commission**) with comments regarding the Proposed Interpretive Guidance on the Cross-Border Application of Certain Swap Provisions (the **Proposed Interpretive Guidance**)<sup>2</sup> and the Proposed Exemptive Order Regarding Compliance with Certain Swap Provisions (the **Proposed Exemptive Order**,<sup>3</sup> and together with the Proposed Interpretive Guidance, the **Release**).

The GFMA welcomes the Commission's publication of the Release as the first concrete effort by any regulator around the globe to tackle the challenges of regulating the cross-border aspects of the global swaps market. Our members are eager to work with the Commission, as well as other regulators, both within and outside the United States, to help build an international regulatory environment that will support a global swaps market that is safer and more transparent, without being unnecessarily distorted by conflicting or insufficiently coordinated rules. Our members have a variety of comments on the Release, but many of these will be made separately through forthcoming SIFMA comment letters to the Commission or through comment letters submitted by other trade associations. Our focus in this letter will be on those aspects of the Release that are intended to establish a

---

<sup>1</sup> The Global Financial Markets Association (GFMA) brings together three of the world's leading financial trade associations to address the increasingly important global regulatory agenda and to promote coordinated advocacy efforts. The Association for Financial Markets in Europe (AFME) in London and Brussels, the Asia Securities Industry & Financial Markets Association (ASIFMA) in Hong Kong and the Securities Industry and Financial Markets Association (SIFMA) in New York and Washington are, respectively, the European, Asian and North American members of GFMA. For more information, please visit <http://www.gfma.org>.

<sup>2</sup> Cross-Border Application of Certain Swaps Provisions of the Commodity Exchange Act, 77 Fed. Reg. 41,214 (proposed July 12, 2012).

<sup>3</sup> Exemptive Order Regarding Compliance with Certain Swap Regulations, 77 Fed. Reg. 41,110 (proposed July 12, 2012).

process for dealing with overlapping or conflicting regulatory regimes through cooperation between regulators in separate jurisdictions, or, in the words of the Release, the process for establishing "substituted compliance."<sup>4</sup>

We welcome the Commission's acknowledgement, underlying its substituted compliance proposals in the Release, that swap dealers and major swap participants organized outside the United States will, in many cases, be subject to home country regulation that seeks to achieve the same regulatory objectives as Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the **Dodd-Frank Act**)<sup>5</sup> and that, as a result, it will often be more appropriate not to extend the extraterritorial reach of U.S. regulation to such entities. We are concerned, however, that the substituted compliance process set forth in the Release may not be the most effective way to achieve these goals. More specifically, to the extent that the Commission intends for substituted compliance only to be granted where it finds rule-by-rule analogs in the relevant non-U.S. jurisdiction, rather than in cases in which there are common regulatory objectives, its approach will be more likely to create a regime of conflicting, confusing and unnecessarily complex regulations that will add cost and complexity for customers. We are also concerned that neither the Commission nor swaps regulators in other jurisdictions will have the resources to police effectively such extraterritorial rules. Instead, we believe that such equivalence determinations should be based on **regulatory recognition**,<sup>6</sup> meaning a principles-based approach in which one regulator relies on the oversight and supervision of the relevant regulated entity by another regulator pursuing the same regulatory objectives.<sup>7</sup> An approach based on regulatory recognition is more consistent with international comity than a rule-by-rule assessment by the Commission of each relevant jurisdiction's regulations. We also believe it is particularly appropriate in the context of cross-border swaps regulation, in which the G-20 governments have agreed in detail on the goals and objectives for the regulation of the global swaps market.<sup>8</sup>

### **1.1 The Commission's proposed approach to substituted compliance determinations under the Proposed Interpretive Guidance is unclear.**

It is difficult to ascertain with certainty, based on a plain reading of the Proposed Interpretive Guidance, precisely what standard the Commission will apply to substituted compliance determinations. At some points in the Release, it appears that the Commission intends to take a principles-based approach to substituted compliance determinations. The Proposed Interpretive Guidance provides that substituted compliance will be permitted "if the Commission finds that such requirements are comparable to cognate requirements under

---

<sup>4</sup> Specifically, we believe this letter is responsive to Questions 26, 28, 29 and 30 of the Proposed Interpretive Guidance.

<sup>5</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act, Public Law 111-203 (July 21, 2010).

<sup>6</sup> Regulatory recognition is an approach supported by the EU-US Coalition on Financial Regulation. *See* the report on Inter-jurisdictional Regulatory Recognition: Facilitating Recovery and Streamlining Regulation, issued by the EU-US Coalition on Financial Regulation in June 2012.

<sup>7</sup> We believe this section is responsive to Question 26 of the Proposed Interpretive Guidance.

<sup>8</sup> G-20 Leaders' Statement, The Pittsburgh Summit, Sep. 25, 2009, available at: <http://www.g20.utoronto.ca/2009/2009communique0925.html> (the **G-20 Framework**).

the [Commodity Exchange Act (**CEA**)] and Commission regulations." <sup>9</sup> Choosing comparability as the standard, instead of equivalence, would support the sort of principles-based approach that we endorse. Helpfully, the Proposed Interpretive Guidance spells out that "comparable does not necessarily mean identical."<sup>10</sup> As further support, the Proposed Interpretive Guidance specifically provides that there can be a positive substituted compliance determination even if the regulations of the foreign regime are not identical to those of the U.S. regulatory regime and highlights that the determination can include a consideration of the objectives of the foreign regulatory regime,<sup>11</sup> which is part of a principles-based review. The description in the Proposed Interpretive Guidance of the Commission's intended scope of review<sup>12</sup> of the foreign regulatory regime also appears to be consistent with a principles-based approach.

However, the Proposed Interpretive Guidance also provides for substituted compliance determinations to be made on an "individual requirements basis,"<sup>13</sup> rather than an assessment of the foreign regime in its entirety, which would seem closer to a rule-by-rule approach to substituted compliance determinations. Another indication that a rule-by-rule approach may be contemplated is that the Proposed Interpretive Guidance requires an applicant seeking a substituted compliance determination to "state with specificity the factual basis for requesting that the Commission recognize comparability with respect to a particular Dodd-Frank Act requirement...and include with specificity all applicable legislation, rules and policies."<sup>14</sup>

At the same time, there are indications that the Commission is considering a hybrid approach, which would begin with a principles-based approach and only move closer to a rule-by-rule analysis if a positive substituted compliance determination could not be made following a principles-based review. Specifically, the Proposed Interpretive Guidance provides that where the foreign regulatory regime does not meet the objectives of the Dodd-Frank Act, substituted compliance would only be recognized in areas that are comparable and comprehensive when compared against the CEA and Commission regulations.<sup>15</sup> Thus, it is unclear what standard the Commission will apply when conducting a review of a foreign jurisdiction's regulations as compared to the U.S. regulations.

We believe that a strict equivalence standard – or even a hybrid approach as discussed above, if applied, will encounter many challenges given the necessary differences in the laws of separate jurisdictions, even where those jurisdictions have agreed on the same principles of swaps regulation. We note that some non-U.S. regulators have already begun

---

<sup>9</sup> Proposed Interpretive Guidance at 41,229.

<sup>10</sup> *Id.* at 41,233.

<sup>11</sup> *Id.* at 41,232-41,233.

<sup>12</sup> The Commission's review will include, but not be limited to the scope and objectives of the relevant non-U.S. regulatory regime, the comprehensiveness of those requirements, the comprehensiveness of the relevant non-U.S. regulator's supervisory compliance program, and the authority of the relevant non-U.S. regulator to support and enforce its oversight of the non-U.S. swap dealer. *Id.* at 41,233.

<sup>13</sup> *Id.* at 41,229.

<sup>14</sup> *Id.* at 41,233.

<sup>15</sup> *Id.*

raising concerns with respect to the Proposed Interpretive Guidance.<sup>16</sup> We understand that the kinds of concerns that foreign regulators are considering include:

- the belief that the application of U.S. rules to institutions organized outside the United States may impede the ability of non-U.S. regulators to set standards their own jurisdictions;
- the potential for conflicts or duplication with home country regulations;
- the challenges of accommodating potential extraterritorial enforcement efforts by U.S. regulators;
- the potential that required compliance with U.S. rules may lead to violations of local law;
- the complexity of applying more than one regulatory framework in the context of the failure or insolvency of a local swap dealing entity; and
- the failure to leverage off global efforts already in process.

We advocate instead, therefore, that the Commission clarify that its proposed approach will be consistent with principles-based regulatory recognition, rather than rule-by-rule substituted compliance.

## **1.2 We advocate a regulatory recognition approach based on dialogue between regulators.**

The key components of a regulatory recognition approach are:

- (i) shared values between the two regimes and commonality of objectives designed to be achieved (viewing the relevant regimes in their entirety, and treating common statutory or regulatory principles, such as participation in the G-20 Framework, as strong evidence of the existence of such shared values);
- (ii) direct dialogue between the relevant regulators to determine whether a positive regulatory recognition determination should be granted;
- (iii) agreement on a Memorandum of Understanding (or expansion of an existing Memorandum of Understanding) between the two jurisdictions to allow ongoing dialogue between regulators as well as sharing of information as needed, including with respect to enforcement; and
- (iv) retention by the Commission of an ability to revoke or revise the scope of regulatory recognition following adequate public notice and comment.<sup>17</sup>

---

<sup>16</sup> See, e.g., Swiss Financial Market Supervisory Authority FINMA letter to the Commission dated July 5, 2012.

<sup>17</sup> We believe this section is responsive to Question 28 of the Proposed Interpretive Guidance.

Under this approach, regulators would coordinate with each other bilaterally to make regulatory recognition determinations based on a common description of outcomes,<sup>18</sup> assuming comparability of supervision and enforcement authority. The comparability analysis would focus on the objectives of the relevant regime in the aggregate, not on a rule-by-rule basis. Regulators would then forge an acceptable Memorandum of Understanding between themselves to allow for the sharing of information and cooperation in enforcement and supervision. As these regulatory recognition determinations and agreements would be made on a bilateral basis, the Commission should retain the flexibility to vary these determinations from one jurisdiction to another, as it deems necessary in keeping with the goal of achieving shared regulatory objectives in the aggregate.

### **1.3 A regulatory recognition approach would have several benefits.**

A regulatory recognition approach has many benefits for both regulators and market participants that we do not believe are effectively achieved by a more granular rule-by-rule comparison of regulations. First and foremost, a regulatory recognition approach acknowledges the global nature of the swaps market, respecting principles of international comity and legitimate interests of both jurisdictions. It avoids the politically unpalatable result of having the Commission unilaterally review the regulatory regimes of foreign jurisdictions and promotes a coordinated approach between the Commission and the relevant regulator. Such an approach would tend to encourage reciprocity where jurisdictions outside of the United States face similar questions regarding the extraterritoriality of their own laws. It would also result in a more cost-effective use of regulatory resources, allowing regulators to leverage each other's regimes. A regulatory recognition approach also avoids costs and inefficiencies of subjecting market participants to duplicative and conflicting requirements that would be a by-product of a rule-by-rule approach.

Of particular importance, a regulatory recognition approach remains flexible over time as laws evolve since regulatory coordination will be ongoing (including with respect to supervision and enforcement).<sup>19</sup> Providing for flexibility over time is a key component of the regulatory recognition approach and one that we believe is critical to success, allowing each regime to develop in a way that its regulator believes is appropriate, while maintaining a coordinated and transparent framework to achieve consistent objectives with the U.S. regulatory framework. It is important to note that, while it is often helpful for rules applicable to market actors to be consistently applied over time, a regulatory coordination process undertaken between regulators who share a commitment to the same regulatory principles should allow for flexibility and dialogue, as it will allow both regulators to adjust their oversight and supervision of the markets as they evolve. Furthermore, direct dialogue between regulators will result in a more efficient and streamlined approach to making

---

<sup>18</sup> See, e.g., IOSCO Objectives and Principles of Securities Regulation.

<sup>19</sup> We believe this section is responsive to Question 30 of the Proposed Interpretive Guidance.

regulatory recognition determinations as contrasted with the potential for multiple individual applications, as contemplated by the Proposed Interpretive Guidance.<sup>20</sup>

If a jurisdiction has taken a reasoned approach to the implementation of its regulations (and, where relevant, the implementation of the G-20 Framework) and the key elements of regulatory recognition are present, its rules should be respected and a positive regulatory recognition determination should be made, even where the scope of the regulations differs in certain areas. In Asia, for example, regulators in several key financial hubs have carefully considered, but do not currently have plans to implement, rules mandating swap execution on organized trading facilities.<sup>21</sup> In such cases, we believe it would not be appropriate for the Commission to require application of its own rules in this area, thereby overruling the policy judgments of local regulators. It is worth noting that if other jurisdictions were to apply their own regimes on a rule-by-rule basis, U.S. regulators could, in certain cases, find their own judgments being effectively overruled when applied to swap dealing entities organized outside the U.S. but doing business within it, as the requirements of a foreign jurisdiction may be more extensive than those of the U.S. in certain cases. For example, if U.S. regulators determine that certain swaps should not be subjected to a clearing mandate, but regulators in another jurisdiction do promulgate such a mandate, such non-U.S. regulations might, without appropriate regulatory recognition, force the relevant transactions on to clearinghouses despite the considered judgment of U.S. officials that such a requirement would not be warranted. As the first major regulator to tackle these global coordination issues, the Commission will need to design a system for regulatory recognition that is flexible enough to avoid such unintended outcomes.

Coordination of timelines is another critical component of a regulatory recognition approach. Failure to account for the different stages of global derivatives reform implementation will significantly undermine the ability to rely on substituted compliance as a means of addressing cross-border issues. If timing is not coordinated, market participants will have no choice but to build out systems for compliance with two regulatory regimes (home country and U.S.) so that they can comply with the U.S. regulatory regime until their own regulatory regime is finalized and a substituted compliance determination can be made. We do not believe this was the intent of legislators, particularly with respect to countries that have signed onto the G-20 Framework. Regulatory recognition could resolve these differences in timing, ultimately allowing regulators in each country to permit the other to use substituted compliance where the key elements of regulatory recognition are present.

---

<sup>20</sup> We look forward to further discussion with the Commission regarding the process for filing substituted compliance plans in order to ensure that this process is as rational and efficient as possible.

<sup>21</sup> See, e.g., Joint Consultation Conclusions on the Proposed Regulatory Regime for the Over-the-Counter Derivatives Market in Hong Kong, issued by the Hong Kong Monetary Authority and the Securities and Futures Commission in July 2012; the Consultation Paper on the Proposed Regulation of Derivatives issued by the Monetary Authority of Singapore in February 2012; the final report on OTC Derivative Market Reform Considerations, issued by the Australian Council of Financial Regulators in March 2012; and the Consultation Paper on Implementation of a Framework for Australia's G20 Over-the-Counter Derivative Commitments, issued by the Australian Federal Treasury in April 2012.

We note that the Commission will also need to coordinate its efforts on cross-border issues with the Securities and Exchange Commission (the **SEC**) and U.S. prudential regulators. The Commission should consider issuing a joint rule with the SEC and the prudential regulators on cross-border issues with respect to margin and capital requirements. The rules clarifying the cross-border impact of Title VII of the Dodd-Frank Act are effectively part of the "swap" and "swap dealer" definitional rules that Congress explicitly required to be issued by the Commission and the SEC jointly.<sup>22</sup> Furthermore, the impact of disparate regulatory actions could be profound. For example, if the SEC similarly requires its swap data reporting rule to apply to transactions between non-U.S. security-based swap dealers and U.S. persons, but defines U.S. persons differently than the Commission has, non-U.S. security-based swap dealers that are also swap dealers would be required to construct and maintain two separate reporting systems. In other cases where regulations conflict, swaps entities may have to comply with the most stringent regulation and effectively be deprived of any comparative relief considered appropriate by the other regulator.

#### **1.4 A rule-by-rule approach could cause conflicts.**

A rule-by-rule approach to substituted compliance determinations may result in conflicting and duplicative requirements for market participants under U.S. and foreign regulatory regimes, particularly in jurisdictions where the regime does not closely parallel that of the United States. In some jurisdictions, concepts central to the U.S. regime simply are not present, making it difficult to find rule-by-rule analogs. For example, the internal business conduct rule (the **Internal Business Conduct Rule**)<sup>23</sup> includes certain prohibitions on a swap dealer's exercise of influence over an affiliate that would have the effect of limiting access to clearing services. Such an objective would need to be implemented differently in a regulatory environment in which the clearing member firm and the swap dealing entity are one and the same entity, as is the case in most jurisdictions outside of the United States. Requiring adherence to U.S. rules in such a circumstance would likely lead to confusion and would force the Commission to spend its resources to determine how its rules should be applied in a regulatory structure different from the one for which the rule was designed.

In addition, certain regulatory regimes are, by design, more principles-based than the relatively prescriptive regime the Commission has developed to implement Title VII of the Dodd-Frank Act. For example, the Internal Business Conduct Rule contains very specific requirements with respect to the appointment of a chief compliance officer and the implementation of specific risk management procedures by a swap dealer. For Canadian banks, however, key risk management objectives consistent with those in the U.S. swap dealer regulations are to be achieved by application of risk management frameworks in the context of prudential oversight by the Canadian bank regulators. In the European Union,

---

<sup>22</sup> See Section 712 of the Dodd-Frank Act.

<sup>23</sup> Swap Dealer and Major Swap Participant Recordkeeping, Reporting, and Duties Rules; Futures Commission Merchant and Introducing Broker Conflicts of Interest Rules; and Chief Compliance Officer Rules for Swap Dealers, Major Swap Participants, and Futures Commission Merchants, 77 Fed. Reg. 20128 (Apr. 3, 2012) (to be codified at 17 C.F.R. pts. 1, 3 and 23).

on the other hand, risk management and compliance responsibilities are assigned under the Markets in Financial Instruments Directive<sup>24</sup> to swap dealing firms at the level of the board, to be carried out by the company's officers. In both jurisdictions, regulators and legislators are seeking to achieve similar goals through regulatory structures or approaches that are different from those of the U.S. There is no evidence to suggest that Congress intended to alter the structure of foreign regulatory regimes such as these. However, if a broader regulatory recognition standard is not adopted, it may be necessary for market participants to comply with both regimes (in whole or part), even where regulations conflict or overlap.

Finally, it may not be possible for non-U.S. market participants to comply with Dodd-Frank Act regulations without violating laws or regulations in their home jurisdiction. For example, the Internal Business Conduct Rule obligation to record telephone conversations regarding pre-execution trade information gives rise to legal issues in foreign jurisdictions such as Germany<sup>25</sup> and China,<sup>26</sup> where all participants on a call must be notified that a particular telephone line is being recorded and/or where principals must give their affirmative consent prior to a conversation being recorded. In addition, at least two dozen jurisdictions have been identified where local law prohibits the disclosure of client names to non-local regulators that do not currently have any information sharing treaty or agreement in place with the local regulator, resulting in a conflict with the swap data reporting requirements applicable to trades with both U.S. and non-U.S. counterparties.<sup>27</sup> These are issues that could be resolved by a regulatory recognition determination.

### **1.5 Regulatory recognition should be applied to a wider variety of rules beyond those enumerated in the Release.**

As proposed, the Release provides for the potential for substituted compliance only in respect of certain enumerated entity-level or transaction-level requirements. It is important, however that the flexibility inherent in a robust regulatory recognition approach also be extended to other aspects of the Commission's regulatory framework, to the extent that the Commission and the relevant non-U.S. regulator can agree on a sensible accommodation. For example, if the relevant U.S. rule requires background checks to be performed on principals of a non-U.S. swap dealer, and there is a similar requirement imposed upon the swap dealing entity under some other foreign regulatory framework (such as banking regulation), the Commission should consider recognizing compliance with the foreign requirement instead of the relevant Commission rule, even if such rule does not fall

---

<sup>24</sup> Directive no. 2004/39/EC, Official Journal L 145 (Apr. 30, 2004), available at: <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:32004L0039:EN:HTML>.

<sup>25</sup> See Bundesdatenschutzgesetz [Federal Data Protection Act], Sep. 1, 2009 BGBL 1 at 2814, § 4 (F.R.G.), available at: [http://www.bfdi.bund.de/EN/DataProtectionActs/Artikel/BDSG\\_idFv01092009.pdf?\\_\\_blob=publicationFile](http://www.bfdi.bund.de/EN/DataProtectionActs/Artikel/BDSG_idFv01092009.pdf?__blob=publicationFile).

<sup>26</sup> See Law of the People's Republic of China on Penalties for Administration of Public Security (17th Meeting of the Standing Committee of the Tenth National People's Congress of the People's Republic of China), Aug. 25, 2005, art. 42 § 6 (P.R.C.), available at: [http://www.china.org.cn/china/LegislationsForm2001-2010/2011-02/11/content\\_21899252.htm](http://www.china.org.cn/china/LegislationsForm2001-2010/2011-02/11/content_21899252.htm).

<sup>27</sup> See Swap Data Recordkeeping and Reporting Requirements, 77 Fed. Reg. 2136 (Jan. 13, 2012) (to be codified at 17 C.F.R. pt. 45).



within the enumerated entity-level or transaction-level requirements enumerated in the Release.

### **Conclusion**

Substituted compliance, if it is implemented based on a regulatory recognition approach, will adequately address many cross-border concerns with respect to the implementation of global derivatives regulations. Shared objectives, together with comparable supervisory and enforcement regimes and acceptable arrangements for sharing and coordination of information between the relevant jurisdictions are the building blocks needed for a positive substituted compliance determination. We hereby request that the Commission clarify that it intends to adopt this principles-based approach for substituted compliance.

Yours sincerely,

A handwritten signature in black ink, appearing to read "Simon Lewis". The signature is written in a cursive style with a large, sweeping initial "S".

Simon Lewis, CEO  
GFMA