afme/
Finance for Europe

24 August 2012

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

Dear Mr. Stanwick

Comment Letter on the Proposed Interpretive Guidance on the Cross-Border Application of Certain Swaps Provisions of the Commodity Exchange act and the Proposed Exemptive Order Regarding Compliance with Certain Swaps Regulations

The Association for Financial Markets in Europe (**"AFME"**)[2] 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**) and the Proposed Exemptive Order Regarding Compliance with Certain Swap Provisions (the **Proposed Exemptive Order**, together with the Proposed Interpretive Guidance, the **Release**).

We endorse the responses submitted by the Global Financial Markets Association (**"GFMA"**)[3] and by the Securities Industry and Financial Markets Association (**"SIFMA"**)[4], which were submitted on 13 August 2012: AFME, and it's members, worked together with the GFMA and SIFMA on their submissions to the Commission.[1]

AFME 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 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.

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**) and that, as a result, it will often be appropriate not to extend the extraterritorial reach of U.S. regulation to such entities. We are concerned, however, that the actual substituted

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[1] GFMA's submitted comment on both the Proposed Exemptive Order and the Proposed Interpretive Guidance, along with SIFMA's submitted comment on the Proposed Exemptive Order are attached to this letter (SIFMA's comment on the Proposed Exemptive Order will be submitted shortly).

Association for Financial Markets in Europe

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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 substituted compliance only to be granted in the case where it finds rule-by-rule analogs in the relevant non-U.S. jurisdiction, rather than where 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 the equivalence determinations that the Commission has in mind should be based on **regulatory recognition**, this being a principles-based approach in the case where one regulator relies on the oversight and supervision of the relevant regulated entity by another regulator pursuing the same regulatory objectives. 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.

Substituted compliance, if its implementation is 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.

AFME is working with the European Commission and others to ensure that there is consistency on a global basis in relation to the regulatory approach to the global swaps market.

We and our respective members again thank you for the opportunity to write in respect of the Commission's Proposed Interpretive Guidance on the Cross-Border Application of Certain Swap Provisions and the Proposed Exemptive Order Regarding Compliance with Certain Swap Provisions.

Yours sincerely

Peter Beales
Managing Director, Policy

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[2] AFME promotes fair, orderly, and efficient European wholesale capital markets and provides leadership in advancing the interests of all market participants. AFME represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. AFME participates in a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association through the GFMA (Global Financial Markets Association). For more information please visit the AFME website www.afme.eu.

[3] The Global Financial Markets Association (GFMA) represents the common interests of the world's leading financial and capital market participants, and speaks for the industry on the most important global market issues. GFMA's mission is to provide a forum for global systemically important banks to develop policies and strategies on issues of global concern within the regulatory environment.

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.

[4] SIFMA brings together the shared interest of hundreds of securities firms, banks and asset managers. SIFMA's mission is to develop policies and practices which strengthen financial markets and which encourage capital availability, job creation and economic growth while building trust and confidence in the financial industry. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA).

August 13, 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 Exemptive Order Regarding Compliance with Certain Swap Regulations (RIN 3038-AD85)

Dear Mr. Stawick:

The Securities Industry and Financial Markets Association ("**SIFMA**") [1] appreciates the opportunity to provide the Commodity Futures Trading Commission (the "**Commission**") with comments regarding the Proposed Exemptive Order Regarding Compliance with Certain Swap Regulations (the "**Proposed Exemptive Order**").[2]

SIFMA believes that it is necessary and appropriate for the Commission to provide market participants with temporary relief from cross-border compliance with Title VII regulations, as the Commission has generally proposed in the Proposed Exemptive Order. We believe that doing so is critically important to an orderly and successful phase-in of the new swaps regulatory regime, as discussed in greater detail in our previous comment letters to the Commission.[3] In this letter, we note a number of

[1] SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association. For more information, visit www.sifma.org.

[2] Exemptive Order Regarding Compliance with Certain Swap Regulations, 77 Fed. Reg. 41,110 (proposed July 12, 2012).

[3] Letter submitted by SIFMA, the Financial Services Forum, the Futures Industry Association, and the International Swaps Dealers Association to the Commodity Futures Trading Commission and the Securities and Exchange Commission on the subject of the phase-in schedule for requirements for Title VII (May 4, 2011) (*available at* http://www.sifma.org/issues/item.aspx?id=25260); Letter submitted by SIFMA, the Financial Industry Association and the International Swaps and Derivatives Association to the Commodity Futures Trading Commission on the subject of the proposed compliance and implementation schedules for clearing, trading execution, documentation and margin (Nov. 4, 2011) (*available at* http://www.sifma.org/issues/item.aspx?id=8589936345); Letter submitted by SIFMA and the International (...continued)

places in which we believe changes should be made to the Proposed Exemptive Order to further this goal.

As a preliminary matter, we note that although the Proposed Exemptive Order relies heavily on and cross-references frequently to the Proposed Interpretive Guidance on Cross-Border Application of Certain Swaps Provisions (the "**Proposed Interpretive Guidance**"),[4] the two documents have been presented as functionally separate, with two separate comment letter deadlines and a likelihood of being finalized and published in the *Federal Register* on two different dates.[5] Although, given the interrelationship between the two documents, we would have preferred to comment on both in a single letter, the difference in comment letter deadlines, the compressed timing and the rejection of our request for an extension of the deadline[6] made it impossible to cover all comments in a single letter. Consequently, we intend to submit a longer and more thorough analysis of our concerns with the Proposed Interpretive Guidance before its comment deadline. In this letter we will refer to and comment on the Proposed Interpretive Guidance only as necessary for the purposes of responding to the Proposed Exemptive Order.

Because the Proposed Exemptive Order could be finalized and published in the *Federal Register* before the Proposed Interpretive Guidance is finalized, we believe that the final version of the exemptive order (the "**Final Exemptive Order**") should not rely on or substantively cross-reference the Proposed Interpretive Guidance in any way. Conditioning the availability of final exemptive relief on the terms of guidance that currently exists only in proposed form presents significant issues relating to how the terms of Final Exemptive Order relief would change once the Proposed Interpretive Guidance is finalized. The Final Exemptive Order will have little practical value if all of its terms are not truly final, including any of those currently incorporated from the

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(continued...)

Swaps and Derivatives Association to the Commodity Futures Trading Commission on the subject of the proposed schedule of CFTC Title VII rulemaking (June 29, 2012) (*available at* http://www.sifma.org/issues/item.aspx?id=8589939400).

[4] Cross-Border Application of Certain Swaps Provisions of the Commodity Exchange Act, 77 Fed. Reg. 41,214 (proposed July 12, 2012).

[5] Separately, we believe that the Proposed Interpretive Guidance is plainly a "rule" under the Administrative Procedure Act and a "regulation" under the Commodity Exchange Act. Accordingly, we believe that in promulgating the Proposed Interpretive Guidance the Commission is required to observe the rule-making procedures contemplated by the Administrative Procedure Act and the Commodity Exchange Act, including the provision of a thorough and detailed cost-benefit analysis. We will discuss this in greater detail in our comment letter on the Proposed Interpretive Guidance.

[6] Letter submitted by SIFMA, the American Bankers Association, The Clearing House, the Financial Services Forum, the Financial Services Round Table, the Futures Industry Association, the Institute of International Bankers, the International Swaps and Derivatives Association, the Investment Company Institute/ICI Global and the Managed Funds Association to the Commodity Futures Trading Commission requesting a comment deadline extension on the Proposed Interpretive Guidance and Proposed Exemptive Order (July 16, 2012) (*available at* http://www.sifma.org/issues/item.aspx?id=8589939524).

Proposed Interpretive Guidance. We therefore believe that the Commission should treat the Order and the Guidance as two wholly separate and self-contained documents. Any terms or concepts that relate to the interpretation or application of the Order should be defined and finalized in the Final Exemptive Order itself. More generally, we believe that market participants should not be required to interrupt registration determinations that are currently underway based on guidance that is merely proposed and not yet final.

We believe that many of the provisions included in the Proposed Exemptive Order require determinations (particularly as to counterparty identity and status) that rely on information not currently available to many swap dealers. This poses several problems. First, given the short time until registration, it is unlikely that market participants will be able to collect and analyze counterparty information prior to the date registration is required, thereby leaving market participants with less relief than the Commission appears to have intended. Perhaps more importantly, attempting to gather this information and build systems to comply with a non-final provision may result in a costly waste of resources and effort, to little effect to the extent that the final provisions do not mirror the proposed provisions closely.

Our specific responses to and suggestions for the Proposed Exemptive Order are explained in more detail below.

I. Interim Relief Based on the Definition of U.S. Person

Our members are concerned that swap dealers and major swap participants ("**MSPs**," and together "**Swap Entities**") may need to comply with Title VII registration and regulatory requirements before the Commission's final definition of "U.S. person" (the "**Final Definition**") has been understood and implemented by market participants. Compliance with those requirements requires an understanding of the use of the term in a number of provisions. Accordingly, we request that the Commission include as part of the Final Exemptive Order a workable definition of U.S. person that would apply until the Final Definition is published.[7] We believe that the interim definition proposed below should be the definition contained in the Final Exemptive Order.

Further, we request that the Commission allow market participants at least 90 days after the Final Definition is published in the *Federal Register* before that definition becomes effective and applicable to Title VII registration and regulatory requirements. This will permit market participants sufficient time to understand the Final Definition and to implement the appropriate systems and compliance processes to identify counterparties based on the Final Definition.

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[7] Separately, we believe that, to avoid confusion and potential unintended consequences, the Commission should state that any definition of U.S. person adopted is solely for Title VII swap regulatory purposes and is not applicable to the futures market or any other Commission purposes.

We believe that, after the Final Definition is published, counterparties should interpret and understand the definition of U.S. person in order to self-report their status to Swap Entities through either representations or information embedded in Legal Entity Identifiers (**"LEIs"**). In the short term, however, it will not be possible for Swap Entities to obtain such information or representations from all counterparties, and the burden of determining a counterparty's status will likely fall to the Swap Entity. Consequently, it is critical that in the period before the Final Definition has been published and 90 days thereafter (the **"Interim Period"**), the definition of "U.S. person" enforced by the Commission be one that can be appropriately observed based on Swap Entities' current recordkeeping and their good-faith attempts to comply.

Observation: During the Interim Period, it would be impossible for our members to employ a definition of "U.S. person" other than one that is based on information already accessible to them.

Recommendation: The Commission should include as part of the Final Exemptive Order a workable, uniform definition of U.S. person for this transitional time period.

Unlike regulation in other markets, swap market regulation has not historically required market participants to determine whether their counterparties are "U.S. persons." As a result, there is no commonly accepted existing definition of "U.S. person" that market participants have incorporated into their operational and compliance systems for swaps. Before a Final Definition is published and has been implemented in the market, it would be impossible for our members to do anything other than rely on their current systems and internal classifications. For most, this would consist of:

- Any natural person who is a resident of the U.S.; and

- Any corporation, partnership, LLC, business or other trust, association, joint-stock company, fund, or any form of enterprise similar to any of the foregoing that is organized or incorporated under the laws of the United States or has its principal place of business in the United States.

For the purposes of this definition (the **"Interim Definition"**), non-U.S. branches of U.S. swap dealers (**"Non-U.S. Branches"**) would not be considered U.S. persons.

We believe that the Interim Definition is appropriate to capture "core" U.S. persons and would capture a large portion of entities that would be U.S. persons under the Final Definition. However, such a definition would allow most of our members to identify those counterparties that are U.S. persons during the Interim Period without the necessity of building new, interim systems that might have to be changed when a Final Definition is adopted. Adopting such an Interim Definition has the additional benefits of effectively phasing in Title VII requirements by targeting these core U.S. persons and being conceptually similar to existing definitions of U.S. person in other contexts, such as Regulation S.

An Interim Period that lasts at least 90 days following the publication of the Final Definition is critical to a smooth transition into full Title VII compliance. Incorporating a new definition of "U.S. person," particularly a definition as complicated and unprecedented as the one proposed in the Proposed Interpretive Guidance and Proposed Exemptive Order, will be a time-consuming and burdensome task that cannot be done quickly after the Final Definition is published.[8] Further, if the Final Exemptive Order is published in the *Federal Register* before the Final Definition, we believe that the Final Exemptive Order should refer to this Interim Definition rather than the proposed definition in the Proposed Interpretive Guidance. Otherwise, regulated entities will be required to make registration and other compliance decisions based on a complex definition that is subject to change.

We emphasize that our members intend to interpret the concept of "U.S. person" based solely on information already tracked by or readily available to them. As we will argue more completely in our response to the Proposed Interpretive Guidance, we believe that the ultimate responsibility of counterparty classification should fall to the counterparties themselves, who are clearly the best positioned to analyze and interpret the application of the Final Definition to them. To the extent that counterparties make representations to regulated entities during the Interim Period, those representations should govern the U.S. person interpretation. However, as stated above, it will be nearly impossible to obtain representations from all counterparties in the short time allotted prior to the required registration date. Thus, in the absence of representations from counterparties, our members will interpret the Interim Definition using a good-faith standard based on available information.

We note that different members will have different information available to them during the Interim Period,[9] which may lead to different status determinations with respect to the same counterparties. Although this result is not ideal, we believe that it is a consequence of the extremely short timeline provided to determine whether counterparties are U.S. persons. We note that any inconsistency with respect to counterparty status across our members, as a result of their varying operational capacities with respect to the Interim Definition, would persist only so long as the Interim Definition is in effect.

Recommendation: During the Interim Period, the Commission should base registration requirements on the Interim Definition. Additional registration requirements arising from the Proposed Interpretive Guidance should not become effective until sufficient time after the Guidance is finalized.

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[8] In addition to its novelty, this definition is not final, and it contains a number of problematic elements and ambiguities that we plan to comment on separately in our comment letter to the Commission on the Proposed Interpretive Guidance.

[9] Indeed, some members have indicated that they do not currently track a counterparty's principal place of business.

We believe that, during the Interim Period, swap dealer and MSP registration should be based on the Interim Definition. Specifically, we believe that only those entities that engage in swap dealing activities above the *de minimis* threshold with U.S. persons meeting the Interim Definition should be required to register with the Commission as swap dealers or MSPs during the Interim Period.

We also believe that entities should not have to register as swap dealers or MSPs based on the Proposed Interpretive Guidance until sufficient time has passed after the Final Interpretive Guidance has been published. Specifically, guarantees of non-U.S. persons by U.S. persons and interaffiliate swap relationships—concepts newly introduced in the Proposed Interpretive Guidance—should not require entities to register as swap dealers until at least 90 days following the publication of the Final Interpretive Guidance.[10] Without such relief, entities would be required to register based on rules that may change from the Proposed Interpretive Guidance to the final and thus may not be fully ascertainable at the time registration is required. In addition, these concepts require entities to collect information that may not be readily available, and that may require them to create new or modify existing systems to process this information, all of which will require sufficient time to be implemented smoothly and successfully.

Recommendation: Any *de minimis* threshold aggregation requirements should not apply until sufficient time after the Final Interpretive Guidance has been published in the *Federal Register.*[11]

We request similar relief from the *de minimis* threshold aggregation requirement. Specifically, we request that entities be allowed to conduct the swap dealer *de minimis* analysis on a legal entity basis for a period of time. We make this request for several reasons. First, the Proposed Interpretive Guidance includes provisions relating to the scope of the aggregation requirement. Entities will not be able to rely on these statements until the Final Interpretive Guidance is published. Second, aggregation may require many smaller affiliates and subsidiaries of swap dealers to register as swap dealers by virtue of the swap dealing activities of their larger affiliates. Because of the relatively late introduction of the aggregation requirement, these entities have had a very short amount of time to prepare for swap dealer registration and regulation. Finally, relief on the aggregation requirement would have the practical benefit of phasing in the effectiveness of Title VII requirements starting with the swap dealers with the most

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[10] We note that we do not believe registration should be required for central booking entities whose exposure to the swaps markets arises only by virtue of interaffiliate swaps. In addition, we believe that a non-U.S. entity should not have to register solely as a result of being guaranteed by a U.S. person. These issues will be addressed more completely in our comment letter to the Commission in response to the Proposed Interpretive Guidance.

[11] We separately note that we believe the aggregation requirement is generally inappropriate. We will address this topic in our comment letter to the Commission in response to the Proposed Interpretive Guidance and Proposed Order.

significant nexus to the United States and, later, possibly expanding the scope of swap dealer registration more broadly.

At a minimum, the Commission should not require non-registered entities to aggregate their swap dealing activity with that of registered swap dealer affiliates. As we will discuss more completely in our letter commenting on the Proposed Interpretive Guidance, we believe that entities should not be required to aggregate swap dealing positions with any registered Swap Entity affiliates. If all non-U.S. entities under common control are required to aggregate their swap activities, the determination that any single entity in the group of affiliates is required to register effectively operates as a mandate that *all* such affiliates register. This would have the effect of requiring a number of smaller, internationally-based entities to register, even if they operate completely independently of their larger affiliate entities, by virtue of the affiliation. This result seems unnecessarily burdensome for these smaller entities and appears to be beyond the scope of Title VII's extraterritorial reach, as these entities will likely not have a direct and significant connection with United States commerce.

We note that, even with the relief suggested above, the novel nature of the Title VII regime and the rapid timeline on which it is being implemented will give rise to significant complications. As a result, while our members intend to comply with registration and other regulatory requirements, including any aggregation requirements that are in place, firms may need to request no-action relief where additional time is needed for compliance.

Recommendation: Title VII compliance requirements, in addition to the registration requirement, should employ the Interim Definition proposed above during the Interim Period.

We believe that Title VII compliance requirements, in addition to the registration requirement, should employ the Interim Definition proposed above during the Interim Period. As a result, during the Interim Period, swap dealers would apply Title VII requirements only to transactions between swap dealers and U.S. persons as defined under the Interim Definition. Otherwise, non-U.S. swap dealers would need to divide their counterparties into U.S. persons and non-U.S. persons during the Interim Period, raising the precise problems the Interim Definition is meant to ameliorate.

Our most pressing concern in this regard relates to the application of reporting requirements to non-U.S. Swap Entities. The Commission's Proposed Exemptive Order would generally provide non-U.S. Swap Entities 12 months to comply with the Commission's Entity-Level Requirements, including swap data repository reporting ("**SDR Reporting**"), and Transaction-Level Requirements, including real-time reporting. However, this relief would not extend to transactions between a non-U.S. Swap Entity and a counterparty that is a "U.S. person." As a result, if the Exemptive Order were adopted as proposed, non-U.S. Swap Entities would need to be able to divide their counterparties into U.S. persons and non-U.S. persons by the date on which they register in order to take advantage of this relief. As discussed above, it will be difficult, if not

impossible, for Swap Entities to collect sufficient data to analyze their counterparties and program their systems in time, thereby significantly reducing the usefulness of the Proposed Exemptive Order's relief. Similarly, to ensure competitive equality among entities operating in the United States, we ask that such relief be extended to transactions between U.S. Swap Entities and non-U.S. persons during the period of exemptive relief.

II. Entity-Level and Transaction-Level Requirements

The Proposed Exemptive Order conditions its relief on the division between Entity-Level and Transaction-Level Requirements in the Proposed Interpretive Guidance. As mentioned above, we believe that any concepts related to the relief available through the Exemptive Order should be contained in the Final Exemptive Order itself. Because the Proposed Exemptive Order specifically "incorporates the proposed categories of Entity-Level and Transaction-Level Requirements, as set forth in the Cross-Border Interpretive Guidance,"[12] for the purpose of commenting on the scope of available relief, we must necessarily refer to the concepts currently embodied only in the Proposed Interpretive Guidance.

A. Division into Entity-Level and Transaction-Level Requirements

Recommendation: All forms of swap reporting, including SDR Reporting and large trader reporting, should be categorized as Transaction-Level Requirements and thereby be eligible for Transaction-Level relief under the Exemptive Order.

Under the Proposed Interpretive Guidance, SDR Reporting and large trader reporting are classified as Entity-Level Requirements.[13] Real-time reporting, however, is classified as a Transaction-Level Requirement. We believe it is appropriate for all reporting requirements to be treated as Transaction-Level Requirements, and thereby be eligible for Transaction-Level relief under the Final Exemptive Order, since all operate on a transaction-by-transaction basis.

SDR Reporting is done on a swap-by-swap basis at the time the transaction is first initiated and throughout the life of the swap. Since both the application and the enforcement of the SDR Reporting requirement will be addressed on the transaction level, we believe this requirement is more appropriately categorized as a Transaction-Level Requirement. Further, SDR Reporting is conceptually more aligned with the Commission's expressed view of Transaction-Level Requirements. Transaction-Level Requirements "relate to both risk mitigation and market transparency."[14] All forms of swap reporting both increase market transparency and serve risk mitigating functions, but we believe that swap reporting is "less closely connected to risk mitigation of the firm as

[12] Proposed Exemptive Order at 41,114.

[13] Proposed Interpretive Guidance at 41,224.

[14] *Id.* at 41,225.

a whole and thus more appropriately applied on a transaction-by-transaction basis."[15] Real-time public reporting is designed to increase regulatory transparency and "support the fairness and efficiency of markets."[16] Like real-time public reporting, which is categorized as a Transaction-Level Requirement,[17] swap data recordkeeping and the reporting and recordkeeping requirements set forth in Parts 45 and 46 of the Commission's regulations provide a means to increased market transparency.

Recommendation: The relief in the Exemptive Order should apply to certain business conduct requirements, specifically swap data recordkeeping and internal conflict of interest requirements, for U.S. swap dealers for trades with non-U.S. counterparties.

During the term of the Exemptive Order, U.S. swap dealers should be provided relief for swap data recordkeeping and internal conflicts requirements for transactions with non-U.S. counterparties similar to that provided to non-U.S. swap dealers. These requirements are transactional in nature, foreign client protection oriented, or depend on local trading practices.[18] This treatment would increase parity between U.S. and non-U.S. swap dealers and is consistent with our general request to avoid penalizing or rewarding swap dealers based on the organization of their entities.

Recommendation: Position limits and anti-manipulation rules should be categorized as Transaction-Level Requirements and thereby be eligible for Transaction-Level relief.

The Proposed Interpretive Guidance does not categorize position limits and anti-manipulation rules as either Entity-Level or Transaction-Level Requirements. Although these rules are part of the Title VII compliance requirements more generally, the Commission has not described their relationship to the rest of the Title VII regulatory regime. This creates uncertainty as to their application during the period of exemptive relief.

Position limits and anti-manipulation rules "have a closer nexus to the transparency goals of the Dodd-Frank Act, as opposed to addressing the risk of a firm's failure."[19] Since both position limits specifically and anti-manipulation rules more broadly represent the Commission's efforts "to diminish, eliminate, or prevent excessive speculation and market manipulation"[20] and to enhance market stability and transparency, they satisfy the

[15] *Id.*

[16] *Id.* at 41,227.

[17] *Id.*

[18] Specifically, we refer to §§ 23.201(a)(1), (a)(2), (a)(3) (transaction and position records); § 23.201(b)(3) (complaints); § 23.201(b)(4) (marketing and sales materials); § 23.201(d) (records of real-time reporting data); and § 23.605 (conflicts of interest related to clearing) of Commission regulations.

[19] Proposed Interpretive Guidance at 41,226.

[20] Position Limits for Futures and Swaps, 76 Fed. Reg. 71,626, 71,627 (Nov. 18, 2011) (to be codified at 17 C.F.R. pts. 1, 150 and 151).

market-transparency goals of the Transaction-Level category. Further, like clearing and margin requirements, which are categorized as Transaction-Level, anti-manipulation rules can be best enforced on a transaction-by-transaction basis. To the extent that position limits speak to firm-oriented risk mitigation efforts, they are more similar to the Transaction-Level Requirements of clearing and margining than to Entity-Level Requirements such as capital adequacy and chief compliance officer requirements. Therefore, we believe that both position limits and anti-manipulation rules should be categorized in the Final Exemptive Order (and later in the Final Interpretive Guidance) as Transaction-Level Requirements and therefore eligible for exemptive relief.

B. Application of Transaction-Level Requirements

Recommendation: U.S. swap dealers should be entitled to relief from Transaction-Level Requirements to the same extent as non-U.S. swap dealers and Non-U.S. Branches.

The Proposed Exemptive Order permits non-U.S. swap dealers operating in the United States, and Non-U.S. Branches operating outside the United States, to postpone compliance with Transaction-Level Requirements for swaps with non-U.S. counterparties.[21] The Order does not, however, extend that relief to U.S. swap dealers transacting with the same non-U.S. persons. We believe that treatment of U.S. swap dealers and non-U.S. swap dealers operating in the U.S. should be the same when transacting with non-U.S. counterparties—transactions undertaken between U.S. swap dealers and non-U.S. counterparties should be exempt from Transaction-Level Requirement compliance just as non-U.S. swap dealers operating in the U.S. are exempt. Permitting non-U.S. swap dealers operating in the U.S. to delay compliance with Transaction-Level Requirements in some circumstances while requiring U.S. swap dealers to comply in those same circumstances would put U.S. swap dealers at a competitive disadvantage. Compliance with Transaction-Level Requirements when transacting with non-U.S. counterparties will create similar operational difficulties for both U.S. swap dealers and non-U.S. swap dealers operating in the United States. Consequently, to mitigate the competitive inequalities that result from disparate treatment of entities operating out of the United States depending on whether they are U.S.- or foreign-based, we believe that the Final Exemptive Order should clarify that both U.S. swap dealers and non-U.S. swap dealers operating in the U.S. should be able to benefit from the availability of Transaction-Level relief during the term of the Exemptive Order when transacting with non-U.S. counterparties.

Recommendation: The Commission should clarify that the Exemptive Order's exemptive relief applies to swaps with a Non-U.S. Branch as a counterparty.

The Proposed Exemptive Order makes clear that a Non-U.S. Branch is eligible for exemptive relief with respect to Transaction-Level Requirements for trades with non-U.S.

[21] Proposed Exemptive Order at 41,112.

persons.[22] The technical language is not as clear that the opposite is true—that a non-U.S. swap dealer entering into a swap with a Non-U.S. Branch is eligible for the same relief. The definition of "U.S. person" contained in the Proposed Interpretive Guidance would include Non-U.S. Branches in the definition of U.S. persons.[23] While adoption of the Interim Definition would solve this issue for the Interim Period, for purposes of increased clarity and to solve the same problem in the time between the Interim Period and the expiration of the exemptive relief, we ask that the Commission clarify in the Final Exemptive Order that exemptive relief from compliance with Title VII Transaction-Level Requirements is available to counterparties to Non-U.S. Branches to the extent those counterparties would have relief for their transactions with non-U.S. persons.

C. Application of Entity-Level Requirements

Recommendation: The Final Exemptive Order should delay Part 46 historical swap reporting requirements for a particular reporting counterparty and asset class until 120 days after Part 45 reporting requirements are effective for that reporting counterparty and asset class.

The Proposed Exemptive Order categorizes the Commission's Part 45 and Part 46 reporting requirements as Entity-Level Requirements for which no relief is available to U.S. swap dealers and for which relief is only available to non-U.S. swap dealers for swaps with non-U.S. person counterparties.[24] Part 45 sets out the Commission's recordkeeping and reporting requirements (other than real-time reporting requirements) for swap transactions entered into on or after its effective date.[25] Part 46 establishes the applicability of recordkeeping and reporting requirements with respect to swaps entered into before that date.[26] Compliance with both sets of requirements will necessitate significant efforts, along with the creation of new systems and procedures, for regulated entities.

Implementing both new swap reporting and historical swap reporting on the same day would subject swap reporting infrastructure to the greatest volume of reporting (and consequently its greatest stresses) on the very first day that such infrastructure is live. Before a significant amount of historical swap data is uploaded to swap data repositories,

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[22] Proposed Exemptive Order at 41,112.

[23] We note that the divergent treatment of Non-U.S. Branches throughout the Proposed Interpretive Guidance is emblematic of the numerous problems with the definition of U.S. person, as proposed. We intend to comment on the treatment of Non-U.S. Branches more completely in our response to the Proposed Interpretive Guidance.

[24] Proposed Exemptive Order at 41,115. Part 46 is implicated in both Swap Data Recordkeeping and Swap Data Reporting. Part 45 is mentioned only in the context of Swap Data Reporting.

[25] *See* Swap Data Recordkeeping and Reporting Requirements, 77 Fed. Reg. 2136 (Jan. 13, 2012) (to be codified at 17 C.F.R. pt 45).

[26] *See* Swap Data Recordkeeping and Reporting Requirements: Pre-Enactment and Transition Swaps, 77 Fed. Reg. 35,200 (June 12, 2012) (to be codified at 17 C.F.R. pt 46).

we believe there should be time for issues that arise in reporting new Part 45 trades to be worked out. Further, as we have argued elsewhere, we believe that phasing in reporting requirements is the best and most effective way to bring these provisions into effect.[27]

Consequently, we believe that the Commission should grant to all market participants in the Final Exemptive Order a delay of 120 days for reporting of historical swap information. In particular, compliance with the historical swap recordkeeping and reporting requirements for a given reporting counterparty and asset class should be required 120 days after Part 45 reporting begins for that reporting counterparty and asset class.[28]

III. Technical Aspects of the Exemptive Order and Compliance Plan Draft

A. Availability of Relief

Recommendation: Non-swap dealers/MSPs should be entitled to the same relief as swap dealers and MSPs.

Certain Title VII requirements, including SDR Reporting and large trader reporting, apply to swap counterparties that are not swap dealers or MSPs. However, the Proposed Exemptive Order would not extend relief to these counterparties equivalent to the relief provided to non-U.S. swap dealers or Non-U.S. Branches. This leads to a particularly problematic result with respect to SDR Reporting: a swap between a non-U.S. person and a non-U.S. branch of a registered swap dealer or MSP will be eligible for exemptive relief, whereas the same non-U.S. person engaging in a transaction with a non-U.S. branch of a U.S. bank that is not a registered swap dealer or MSP will not be eligible. To avoid this anomalous result, we ask the Commission to clarify that non-swap dealer/MSP entities are eligible for exemptive relief to the same extent as registered swap dealers and MSPs.

[27] *See supra* note 3.

[28] The three classes of transactions addressed in Part 45, in order of their required reporting dates are: 1) credit default swaps and interest rate swaps with a swap dealer as the reporting counterparty, 2) all other swaps with a swap dealer as the reporting counterparty (90 days later), and 3) all swaps not covered in the first two categories (90 days later). Swap Data Recordkeeping and Reporting Requirements, 77 Fed. Reg. 2136 (Jan. 13, 2012) (to be codified at 17 C.F.R. pt. 45).

B. SDR and Large Trader Reporting Requirements

Recommendation: The relief granted to non-U.S. Swap Entities with respect to SDR Reporting and large trader reporting for swaps with non-U.S. counterparties should be available regardless of whether the non-U.S. Swap Entity is affiliated with a U.S. swap dealer.

The Proposed Exemptive Order provides that, during the pendency of the order, non-U.S. Swap Entities that are not affiliates or subsidiaries of a U.S. swap dealer may delay compliance with the SDR Reporting and large trader reporting requirements for swaps with non-U.S. counterparties.[29] However, this relief is not available to non-U.S. Swap Entities that are affiliated with U.S. swap dealers. At a minimum, the existing proposed relief for non-U.S. Swap Entities should apply regardless of whether the non-U.S. Swap Entity in question has an affiliate that is a U.S. swap dealer. If the U.S. affiliates of non-U.S. Swap Entities are considered in determining the availability of exemptive relief, non-U.S. subsidiaries or affiliates of similarly situated parent firms may be subject to different regulatory treatment, even in a situation where the home-jurisdiction swap activities are comparable. Further, the presence of a U.S. affiliate in the larger corporate structure that includes a non-U.S. swap dealer does not suggest that the non-U.S. swap dealer will be any better equipped or prepared to comply with SDR Reporting and large trader reporting. Different legal entities, in many cases, use different technology systems to satisfy different sets of local requirements.

Because SDR Reporting and large trader reporting will have to be satisfied with respect to individual transactions, these requirements likely cannot be satisfied with a single firm-wide solution. Rather, each individual entity will have to come into compliance individually. Thus, the fact that a non-U.S. swap dealer has a U.S.-registered swap dealer affiliate that will have to comply with SDR Reporting and large trader reporting does not suggest that implementation of the requirement will be smoother for such non-U.S. swap dealer.[30] We therefore request that the Commission clarify in the Final Exemptive Order that the reporting relief currently proposed is available to all non-U.S. Swap Entities, regardless of their affiliation with U.S. swap dealers.

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[29] Proposed Exemptive Order at 41,119.

[30] Moreover, the fact that a non-U.S. Swap Entity has a U.S. affiliate does not mean that these entities are part of a "U.S.-based affiliated group." *Id.* at 41,112. The Commission's stated goal is its "supervisory interest in data related to the swap activities of non-U.S. swap dealers and non-U.S. MSPs that are part of a U.S.-based affiliated group." *Id.* It is incorrect to assume that all non-U.S. Swap Entities that happen to have a U.S. affiliate are part of a U.S.-based affiliated group. Making such an assumption will deny certain non-U.S. Swap Entities the benefit of appropriate exemptive relief.

Recommendation: The Commission should take into account the issue of foreign jurisdictions' privacy laws.

Additional time is needed for the Commission and market participants to address concerns arising from client confidentiality requirements under the local law of certain non-U.S. jurisdictions, some of which may even apply to transactions with U.S. persons. This is a complicated issue that requires consultation with local regulators. 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 an information-sharing treaty or agreement in place with the local regulator, some of which cannot be satisfied by counterparty consent. One solution could be to mask client identities, consistent with the approach taken in the OTC Derivatives Supervisors Group global trade repository.

As this delicate issue requires more time for the Commission to consider and to develop possible alternative solutions, we suggest that during the term of the Exemptive Order, swap dealers should be permitted to mask client information from SDR Reporting, provided that the failure to do so would violate non-U.S. legal requirements. During this time, the Commission should work with foreign regulators to address these problems. To the extent that these problems are not solved before reporting is required for U.S. persons, market participants may need to ask for additional relief from specific reporting requirements, such as for historical swaps.

C. Length of Proposed Exemptive Relief

Recommendation: The end of the Proposed Exemptive Order's relief should be tied to publication of the Final Exemptive Order, rather than that of the proposal, in the *Federal Register*.

As proposed, the relief offered by the Exemptive Order would expire 12 months after the publication of the Proposed Exemptive Order in the *Federal Register*.[31] The full scope of the available relief will not become apparent, however, until the relief is finalized and the Final Exemptive Order is published in the *Federal Register*. Consequently, we believe that the expiration of the relief should be determined relative to the publication of the Final Exemptive Order. To the extent that the Final Exemptive Order differs from the Proposed Exemptive Order, affected entities would be deprived of the benefit of a one-year transition period.

Since the full range of exemptive relief will not become evident until the Final Exemptive Order is published, we believe that the transition time provided by the relief can only be meaningful if measured from that final date. The proposed timing could present a scenario in which compliance requirements come into effect only shortly before the exemptive relief expires. An abbreviated exemptive relief period could deprive non-U.S. Swap Entities of the benefits that the proposed exemptive order seeks to provide.

[31] *Id.* at 41,110.

Recommendation: The Commission should develop a process to extend exemptive relief where potentially comparable foreign requirements are proposed but not yet final, or where the Commission has not completed comparability determinations.

The Proposed Exemptive Order provides that exemptive relief for non-U.S. Swap Entities will expire 12 months after it is published in the *Federal Register*. Non-U.S. Swap Entities, however, may intend to apply for substituted compliance but may operate in jurisdictions where final rules have not yet come into effect or for which the Commission has not made a comparability determination. In those circumstances, the non-U.S. Swap Entities may be subject to U.S. regulations for the period of time between the end of relief and the finalization of home-jurisdiction regulations, plus the length of time it takes the Commission to make an accompanying comparability determination.

As a result, we believe that non-U.S. Swap Entities should remain subject to the Final Exemptive Order's relief until substituted compliance is available rather than needing to build the technological, operational and compliance systems required to comply with U.S. law for a short interim period. This should be the case so long as that period of time is anticipated to be reasonably brief and the Commission anticipates a possibility that the finalized regulations will be sufficiently comparable.

Further, we believe that the Commission should provide for an interim process in which non-U.S. Swap Entities may present, as part of their compliance plans, the enacted legislation or regulation regarding swap regulation, along with the anticipated effectiveness dates and scope of home-jurisdiction regulations not yet finalized. Based on these presentations, the Commission could exercise discretionary authority to extend exemptive relief for a reasonable period of time. This extension would allow for smoother transitions, both for regulated entities and for the markets in which they operate. It would also provide for better harmonization among U.S. and non-U.S. swap regulations.

In particular, we propose that the Commission allow a non-U.S. entity, group of entities or a foreign regulator to, at any time, apply to the Commission for a six-month extension during which the non-U.S. entities would remain exempt from Title VII requirements in anticipation of the finalization of home-jurisdiction swap regulations and the requisite comparability analyses. Upon receipt of this application, the Commission would be required to respond within 30 days to notify the applicant of the Commission's determinations. This process would allow the Commission to make reasonable allowances for the transition time required by 1) non-U.S. entities that may be subject to a range of swap regulations internationally, 2) non-U.S. jurisdictions that are beginning to create swap regulatory regimes and 3) the Commission itself, which must evaluate those regimes for comparability as they come into existence.

We recognize that extension of the exemption period will not be appropriate in those instances where no legislation exists and finalization of home-country regulations is too remote. In those circumstances, the expiration of the 12-month relief period should

coincide with the full effectiveness of the U.S. regulations for the affected non-U.S. Swap Entities.

D. Compliance Plans

Recommendation: The Commission should clarify that the initial compliance plans required to apply for Exemptive Order relief need only provide a basic indication of a non-U.S. entity's desire to seek substituted compliance.

The Proposed Exemptive Order conditions exemptive relief on registration and filing, within 60 days of registration, "a compliance plan addressing how [the swap dealer] plans to comply, in good faith, with all applicable requirements under the CEA and related rules and regulations upon the effective date of the Cross-Border Interpretive Guidance."[32] As proposed, the compliance plan would need to contain an indication of whether the non-U.S. Swap Entity intends to seek a comparability determination and, where the entity intends to comply with home-jurisdiction requirements, a description of those requirements.[33] Both of these requirements presuppose a level of development for home-jurisdiction swap regulatory regimes which is likely an unreasonable expectation for the time frame allotted. Most foreign regimes' swap regulations are not as fully formed as are those of the United States, and without a robust and complete foreign regulatory regime, non-U.S. Swap Entities will be effectively unable to provide compliance plans satisfying the Commission's desired level of detail before the appointed deadline.

We therefore request that the Commission clarify the purpose of and its expectation around the compliance plan. We believe that the primary purpose of the compliance plan requirement is to notify the Commission of those provisions for which a swap dealer intends to seek substituted compliance to allow the Commission to begin its comparability analysis wherever possible. Since the compliance plans are separate from the required applications for comparability determinations, we do not interpret the compliance plan requirements to be as detailed or specific as those for comparability determinations, particularly given the short time frame in which compliance plans must be submitted and the fact that many foreign jurisdictions have not yet finalized their swap regulatory regimes. Rather, we interpret the compliance plans to require a more general description of the laws and provisions for which regulated entities plan to seek substituted compliance.

Further, the Commission has indicated that the plans should be updated as new foreign regulatory regimes emerge,[34] further buttressing our view that initial compliance plans need not undertake a detailed analysis of foreign regulatory regimes. We believe

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[32] *Id.* at 41,113.

[33] *Id.*

[34] *Id.* n.22.

that these updates should also not undertake a thorough analysis of the specific provisions as finalized, but rather call the Commission's attention to the new availability of these new foreign laws and notify the Commission of a non-U.S. Swap Entity's intent to seek substituted compliance for these provisions. This reading of the compliance plan requirement would allow non-U.S. Swap Entities to meet the required deadlines for filing the necessary documentation to apply for exemptive relief while taking a more realistic view towards the type and quality of information that will be available by the required deadline.

Consequently, we believe that compliance plans should take the form of notice filings in which non-U.S. Swap Entities notify the Commission of their intent to seek comparability determinations as foreign regulators finalize the applicable home-jurisdiction requirements.

IV. Other Issues

Recommendation: The Commission should coordinate its cross-border Title VII regulations with the SEC, including the prudential regulators and foreign regulators.

The regulated entities that will have to comply with both the Final Interpretive Guidance and Final Exemptive Order will likely be subject to other regulators' rules. Without explicit efforts among regulators to harmonize the requirements and compliance timing, affected entities could be subject to three or more different sets of requirements for the same aspects of their swaps business. In addition to being extremely burdensome, there are a number of swap transaction requirements, such as clearing, where only one requirement can practically be satisfied for a given transaction. This means that requirements may conflict or, even where they do not, that the most stringent of the multiple possible regulators will effectively establish the baseline for any given provision, depriving regulated entities of any comparative relief intended by any of their other regulators.

We believe that coordination with the Securities and Exchange Commission (the "**SEC**") is critical. Title VII divides jurisdiction of the over-the-counter derivatives market between the Commission and the SEC. As part of this division of jurisdiction, Congress explicitly requires the Commission and the SEC to consult and coordinate with each other to the extent possible.[35] In addition, Congress required that the Commission and the SEC jointly adopt the foundational Title VII rules, such as those defining "swap" and "swap dealer." In doing so, Congress expressed its intent that any rules governing the regulatory scope of the entities and products subject to Title VII requirements should be defined by these two regulators together.

Rules clarifying the cross-border impact of Title VII are effectively part of the "swap" and "swap dealer" definitional rules in that, like those rules, the clarification of the cross-

[35] *See* Section 712 of the Dodd-Frank Act.

border impact of Title VII defines which entities and transactions are subject to Title VII and which are not. Congress explicitly required that the Commission and the SEC coordinate on these foundational rules that define the scope of Dodd-Frank, yet the Commission has proposed the Proposed Interpretive Guidance and the Proposed Exemptive Order alone. The impact of disparate regulatory actions could be profound: a concept as fundamental as what entities are defined as U.S. persons could be subject to different interpretations by the two regulatory agencies. Thus, we believe that the Commission and the SEC must develop their views of the cross-border application of Title VII jointly.

Coordination with the prudential regulators is similarly critical, as responsibility for swap dealer capital and margin requirements is divided, based on an entity's primary regulator, between the Commission and the prudential regulators. Differing cross-border application of margin and capital rules could thus lead to competitive inequalities between otherwise similarly situated swap dealers.

Finally, because the Proposed Interpretive Guidance and the Proposed Exemptive Order define the extraterritorial effects of the Commission's swaps regulation, direct coordination with international regulators is imperative. Direct communication with foreign regulators will allow both sets of regulators to take full account of the other's perspectives in the regulatory process and will best allow each party to observe the basic principles of comity while protecting their respective jurisdictions from the systemic risks presented by underregulation or misregulation of the global swaps market.

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We thank the Commission for its consideration of our comments. If you have any questions, please do not hesitate to call the undersigned at 202-962-7400.

Sincerely,

Kenneth E. Bentsen, Jr.
Executive Vice President
Public Policy and Advocacy
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**)[1] 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**)[2] and the Proposed Exemptive Order Regarding Compliance with Certain Swap Provisions (the **Proposed Exemptive Order**,[3] 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

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[1] 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.

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

[3] 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."[4]

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**)[5] 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**,[6] 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.[7] 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.[8]

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

[4] Specifically, we believe this letter is responsive to Questions 26, 28, 29 and 30 of the Proposed Interpretive Guidance.

[5] Dodd-Frank Wall Street Reform and Consumer Protection Act, Public Law 111-203 (July 21, 2010).

[6] 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.

[7] We believe this section is responsive to Question 26 of the Proposed Interpretive Guidance.

[8] 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." [9] 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."[10] 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,[11] which is part of a principles-based review. The description in the Proposed Interpretive Guidance of the Commission's intended scope of review[12] 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,"[13] 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."[14]

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.[15] 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

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[9] Proposed Interpretive Guidance at 41,229.
[10] *Id.* at 41,233.
[11] *Id.* at 41,232-41,233.
[12] 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.
[13] *Id.* at 41,229.
[14] *Id.* at 41,233.
[15] *Id.*

raising concerns with respect to the Proposed Interpretive Guidance.[16] 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.[17]

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[16] *See, e.g.,* Swiss Financial Market Supervisory Authority FINMA letter to the Commission dated July 5, 2012.
[17] 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,[18] 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).[19] 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

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[18] *See, e.g.,* IOSCO Objectives and Principles of Securities Regulation.

[19] 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.[20]

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.[21] 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.

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[20] 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.

[21] *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.[22] 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**) [23] 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,

[22] *See* Section 712 of the Dodd-Frank Act.

[23] 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[24] 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[25] and China,[26] 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.[27] 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

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[24] 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.

[25] *See* Bundesdatenschutzgestz [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.

[26] *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.

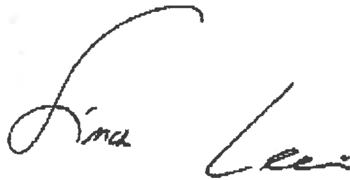
[27] *See* Swap Data Recordkeeping and Reporting Requirements, 77 Fed. Reg. 2136 (Jan. 13, 2012) (to be codified at 17 C.F.R. pt. 45).

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,



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