



STATE STREET

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Via: <http://comments.cftc.gov>

Ms. Melissa Jurgens  
Secretary of the Commission  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21st Street, NW  
Washington, DC 20581

**Re: Further Proposed Guidance Regarding Compliance with Certain Swap Regulations  
Final Exemptive Order Regarding Compliance with Certain Swap Regulations  
(RIN 3038-AD85)**

Dear Ms. Jurgens:

State Street Corporation (“State Street”) appreciates the Commodity Futures Trading Commission’s (“the Commission’s”) ongoing efforts to clarify the cross-border application of the Commission’s new regulatory regime for swaps.

U.S. swap dealers, including State Street, often enter into transactions with non-U.S. persons through non-U.S. branches. We support earlier Commission proposed guidance which would allow “substituted compliance” for most transaction level requirements, and which would defer oversight of sales practices to local jurisdictions, by excluding such transactions from the Commission’s External Business Conduct Standards.<sup>1</sup>

Our comments today, however, relate to specific criteria recently suggested by the Commission for identifying swaps that will qualify for this proposed approach to foreign branches. As an internationally active, U.S.-registered swap dealer, State Street supports additional Commission guidance on this issue,

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<sup>1</sup> Cross-Border Application of Certain Swaps Provisions of the Commodity Exchange Act; Propose Rules. See 77 FR 41229-30.

particularly with respect to the highly liquid, transparent and around-the-clock foreign exchange markets in which all of State Street’s swap dealing activity takes place.

We believe the simplest, most relevant, test for whether a swap is “with a foreign branch” is whether the branch is the legal counterparty to the swap, and whether the swap is booked to the branch. Nevertheless, we understand the Commission’s interest in avoiding evasion of its U.S. rules, and, while the Commission’s anti-evasion powers should suffice to avoid inappropriate actions by U.S. swap dealers, establishing some guidelines for identifying *bona fide* non-U.S. branch transactions could be helpful.

Specifically, in the preamble to the “Final Exemptive Order Regarding Compliance with Certain Swap Regulations<sup>2</sup>,” the Commission suggests four possible criteria which could be used to determine when a swap is with a foreign branch of a U.S. person:

- i. That the foreign branch is the location of employment of the employees negotiating the swap for the U.S. person or, if the swap is executed electronically, the employees managing the execution of the swap;
- ii. That the U.S. person treats the swap as a swap of the foreign branch for tax purposes;
- iii. That the foreign branch operates for valid business reasons and is not only a representative office of the U.S. person; and
- iv. That the branch is engaged in the business of banking or financing and is subject to substantive regulation in the jurisdiction where it is located.

While we urge the Commission to not be overly prescriptive, and establish these criteria as principles subject to interpretation based on individual facts and circumstances, we do not strongly object to three of the four criteria: that the swap is treated as a swap of the foreign branch for tax purposes, that the branch operates for valid business reasons and is not only a representative office, and that the branch is engaged in banking or financing and subject to substantive local regulation. While each of these, particularly the tax-related criteria, may be challenging to properly define and evaluate, we do not disagree that these could be reasonable indicia of a *bona fide* non-U.S. branch of a U.S. swap dealer.

We have significant concerns, however, with the first prong of the proposed criteria: “that the foreign branch is the location of the employees negotiating the swap for the U.S. person, or, if the swap is executed electronically, the employee managing the execution of the swap.” We urge the Commission to eliminate this criteria from any further guidance issued on this subject.

In many cases, non-U.S. counterparties prefer to book trades with branches of U.S. dealers, which provides the benefits of dealing with a strong, well-regulated U.S. firm within the context of the local market. The location of the employee negotiating, agreeing to, or executing a swap is, in our view, irrelevant to the determination of whether a swap is “with a foreign branch.”

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<sup>2</sup> 78 FR 873

In today's global economy, foreign exchange swaps are negotiated 24 hours a day, by parties located in a wide variety of locations. The physical location of the employees negotiating the swaps has little connection to the legal jurisdiction of the branch in which the swaps are booked. The determination of which branch will be the counterparty to a swap is influenced by a number of factors, including the convenience of the swap counterparty and agreements between counterparties to book swaps to mutually agreeable and preferred locations.

Limiting the ability to book transactions to a foreign branch solely to traders physically located in the branch would be particularly inappropriate for U.S. dealers in foreign exchange, such as State Street, because of the way such dealers interact with investment managers. These investment managers typically negotiate foreign exchange transactions in large blocks, which combine the orders of a variety of asset owners (such as pension funds or other collective investment pools), and which can include U.S. persons, non-U.S. persons, or both. Once negotiated and executed, such blocks are allocated to the various asset owners, and booked to the location preferred by the asset owner. In many cases, some portions of the block will be booked to the dealer's non-U.S. branch.

This block trading approach has several advantages for investment managers. It allows such managers to trade foreign exchange more efficiently, using a single point of dealer contact, and ensures that all asset owners on whose behalf they are trading receive the same price.

A dealer providing such services, however, needs sufficient flexibility to accommodate the needs of the investment manager. Most importantly, dealers must be able to book trades to the branch preferred by asset owners, and must be able to accommodate requests to book allocations from a block to different locations world-wide. In addition, dealers need to have the ability to negotiate transactions on a 24-hour basis. In both of these cases, traders may need to be located in different locations than the location where the trade is ultimately booked.

The first prong of the Commission's suggested criteria would interfere with this well established and successful business model, to the disadvantage of investment managers, asset owners, and U.S.-based foreign exchange dealers. In addition to seeking the convenience of booking trades to their preferred locations, many non-U.S. asset owners are unwilling to enter into transactions that would subject them to U.S. regulatory requirements, such as the Commission's External Business Conduct rules. Since, as a result, the block would need to be broken up pre-execution, and negotiated and executed with personnel in different locations, investment managers and their asset owner clients may elect not to utilize the highly efficient block trading services provided by U.S. dealers. As a result, U.S. dealers who rely on non-U.S. branch structures will be significantly disadvantaged in competing with non-U.S. based dealers.

This competitive disadvantage would be particularly acute if U.S.-based employees of non-U.S. based swap dealers are permitted to avoid compliance with all of the Commission's transaction-level

requirements by booking trades to a non-U.S. location, as appears to be the case under the guidance proposed by the Commission in July, 2012<sup>3</sup>.

In summary, we believe there are compelling policy, convenience, and competitive reasons for not imposing a requirement that only traders physically located at a foreign branch of a U.S. dealer may book trades to that branch. We urge the Commission to refrain from adopting such a requirement, and to provide guidance establishing indicia for determining which trades are “with a foreign branch”, focusing on the remaining three proposed prongs of its suggested approach.

Sincerely,

A handwritten signature in black ink, appearing to read 'Stefan M. Gavell', written in a cursive style.

Stefan M. Gavell

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<sup>3</sup> 77 FR 41214