

August 8, 2013

Secretary  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21st Street, N.W.  
Washington, DC 20581

**Re: Exemptive Order regarding Compliance with Certain Swap Regulations (RIN 3038-AE05)**

The International Swaps and Derivatives Association, Inc. (“**ISDA**”) appreciates the opportunity to provide the Commodity Futures Trading Commission (the “**Commission**”) with comments and recommendations regarding the exemptive order (the “**Exemptive Order**”)¹ described above.

Since 1985, ISDA has worked to make the global over-the-counter (OTC) derivatives markets safer and more efficient. Today, ISDA has over 800 member institutions from 60 countries. These members include a broad range of OTC derivatives market participants including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure including exchanges, clearinghouses and repositories, as well as law firms, accounting firms and other service providers.²

Our comments focus on the need for longer and internally better-aligned implementation periods and the importance of a transparent and participatory substituted compliance determination process. The phase-in periods provided in (or in some cases missing from) the Exemptive Order underestimate the scale of the market-wide efforts needed to implement the Cross-Border Guidance.³ Instead of the 75-day period applicable under many provisions of the Exemptive Order, ISDA recommends that the Commission adopt a more realistic, but still aspirational, phase-in period through December 21, coupled with a willingness to make further adjustments as the industry progresses toward implementation. So as not to preempt the substituted compliance process, the duration of relief from the clearing requirement should be aligned with the period for all other transaction-level requirements for which substituted compliance is potentially available.

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¹ 78 Fed. Reg. 43785 (July 22, 2013)

² Additional information about ISDA and its activities is available on the Association's web site: [www.isda.org](http://www.isda.org).

³ Interpretive Guidance and Policy Statement Regarding Compliance with Certain Swap Regulations, 78 Fed. Reg. 45292 (July 26, 2013) (“Cross-Border Guidance”).

Phase-in periods should be provided for large trader reporting and recordkeeping obligations upon which relief from SDR reporting for non-US registrants is conditioned, and application of the new criteria for “foreign branch” transactions. The currently imposed September 30 effective date for real-time reporting should be extended to December 21, and additional time should be provided for SDR reporting of Part 46 historical swaps and swaps entered into prior to July 12, 2013 that have become reportable by virtue of the Cross-Border Guidance.

A transparent and participatory substituted compliance determination process is essential to provide planning certainty to firms, ensure that the determinations take into account concerns regarding their effects on competitive parity, and tap the practical knowledge of market participants. ISDA suggests that a 90-day phase-in period for substituted compliance determinations is appropriate, with further staging of compliance dates by category of market participant to be considered. A phase-in period is also necessary following a denial of substituted compliance with respect to a jurisdiction, and following such denial US registrants with foreign branches in that jurisdiction should be permitted to comply with local transaction-level requirements in lieu of the Commission’s in accordance with the 5%-of-aggregate-notional-value exception provided in the Cross-Border Guidance.

## I. Phase-in periods

### A. 75-Day Period is Insufficient.

The 75-day phase-in period provided under the Exemptive Order<sup>4</sup> is insufficient for the market-wide adjustments to operational and compliance systems needed to implement the Cross-border Guidance. This implementation burden falls on market participants of every kind – from swap dealers, to investment funds to non-financial corporate end-users. The Cross-Border Guidance requires market participants to make myriad “facts and circumstances” determinations, amplifying the difficulty and time needed to formulate and obtain counterparty representations and conduct the self-diligence necessary in order to give representations. Some examples follow:

- The new US person definition:
  - adds new intricacies to determining the principal place of business for investment funds;
  - requires collective investment vehicles and unlimited liability entities to monitor for US person majority-ownership; and
  - introduces a vague penumbra of coverage through its “including but not limited to” introductory clause.
- An entity’s status as an “affiliate conduit” requires a facts and circumstances analysis, and “guaranteed affiliate” determinations must incorporate new interpretive gloss on the types of arrangements that may constitute guarantees.
- De minimis exemption from SD status:<sup>5</sup> Non-US persons applying the de minimis test must now ascertain a much broader array of counterparty

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<sup>4</sup> The 75-day time period applies to Exemptive Order paragraphs 1, 2, 3, 4, 8, 10, 12, 14 and 15.

<sup>5</sup> Exemptive Order paragraphs 3, 4 and 5.

characteristics, most of which will be within the unique knowledge of the counterparty. For example, in order to exclude transactions with a non-US counterparty whose obligations under a swap are guaranteed, the non-US person applying the de minimis test must satisfy itself that the guarantor is either a non-US person or a US non-financial entity, or else that the US-guaranteed counterparty is a swap dealer (“SD”) or SD affiliate engaged in de minimis dealing.<sup>6</sup>

The premise of the SD de minimis test is that an entity, by limiting its dealing activity, may have control over the decision of whether to register as an SD. This is evidenced in the use of an activity-based test that looks to notional amounts “entered into” after the October 12 effective date of the product definitions. Determining the US person status of counterparties and guarantors will require outreach, counterparty response, and integration of changed status into compliance systems. Imposing use of new definitions before this anticipatory re-classification exercise can be completed and before, if necessary, transactional relationships can be reassigned to a registered SD within an affiliated group, is inconsistent with the principle of volitional registration.

- Non-US person, non-registrants include end-user entities, who will need more time than institutions active in the swap market to comply with the non-registrant requirements (i.e., clearing or establishing the end-user exemption, trade execution, real-time reporting, SDR reporting and recordkeeping, large trader reporting), which may apply in transactions where the non-US person’s counterparty is a US person (or where each of the parties is a guaranteed affiliate or conduit affiliate).

#### B. Recommended Implementation Period.

Onboarding of “new” US persons must follow from the information collection and characterization process. This process will involve outreach to counterparties, counterparty familiarization with and analysis of the new US person attributes and other interpretive categories, collection and review of responses, and their integration into compliance systems. Only after this classification phase is completed can counterparties familiarize themselves with newly applicable requirements and enter into arrangements to comply. For example, non-registrant requirements will impose clearing and SDR reporting on non-US persons not previously subject to such requirements. Such parties will require additional time to establish clearing relationships (or end-user exemptions) and provide consents to reporting. New US persons will be newly within the scope of the business conduct rules, and first-time adherence to ISDA protocols or equivalent documentation must occur.

ISDA recommends that the 75-day period be extended to December 21, the date specified in the Exemptive Order as the end date for relief from most of the requirements for which substituted compliance is available. Having a uniform target date for changes to operational and compliance systems will enhance efficiency and allow such systems to be constructed as

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<sup>6</sup> Cross-Border Guidance at 45326.

an integrated whole. This December 21 target date is still an ambitious one. As noted above, the market must engage in a two-stage compliance effort (i.e., an information collection and analysis stage, and an implementation stage), and a substantial part of the compliance effort can commence only after the initial information intake and characterization is completed. ISDA hopes that the Commission and its staff will be open to adjustments of this schedule as the industry works toward implementation and appraises the Commission of any obstacles encountered.

### C. Clearing.

The duration of the relief available from the clearing requirements under paragraphs (8) and (12) of the Exemptive Order should be aligned with the period for all other Transaction-Level Requirements for which substituted compliance is potentially available. The current lack of alignment leads to the possibility that the Commission's clearing mandate could become applicable while a substituted compliance determination (or local clearinghouse registration application) is pending. Undesirable consequences would follow from this outcome. First, forced use of an out-of-jurisdiction Commission-registered DCO (or one that may avail itself of no-action relief) during the interim period, followed by use of the local DCO when made possible, would split netting pools. Furthermore, application of the clearing mandate during this interim period would create an uneven playing field between foreign branches of US SD/MSPs and non-US SD/MSPs with respect to transactions with non-US persons that are not guaranteed or conduit affiliates of US persons, as such persons' transactions with non-US SD/MSPs are not subject to the Commission's clearing mandate.

### D. Reporting.

The condition in paragraph (6) of the Exemptive Order that non-US SDs and MSPs comply with Commission recordkeeping requirements where no swap data reporting requirements have been implemented in their home jurisdictions has been imposed without a phase-in period. Similarly, no phase-in period was provided for the elimination of Part 20 large trader reporting as an Entity-Level Requirement.<sup>7</sup> ISDA recommends that the same phase-in period as applies to other Entity-Level Requirements (i.e., December 21, 2013, subject to earlier issuance of a substituted compliance determination) should apply to Commission recordkeeping requirements and to large trader reporting. Until that date, SDs and MSPs should be able to satisfy the recordkeeping condition of paragraph (6) by keeping records in accordance with local requirements. For the reporting of "historical" swaps under Part 46 and swaps entered into prior to July 12, 2013 that have become reportable by virtue of the Cross-Border Guidance, an additional 30-day period of relief should be provided beyond that available for Part 45 reporting.

For Part 43 reporting by non-US SDs or foreign branches of US SDs transacting with guaranteed affiliates of US persons,<sup>8</sup> ISDA suggests that a compliance date of December 21, 2013 is appropriate. The problem of identifying guaranteed affiliates requires the same

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<sup>7</sup> The expired January Exemptive Order included Part 20 among the entity-level requirements for which relief was available. 78 Fed. Reg. 858, footnote 156.

<sup>8</sup> Exemptive Order paragraphs 9 and 13.

information collection effort as these other aspects of the Cross-border Guidance, making the currently imposed September 30 compliance date impracticable.

#### E. Foreign branches of US SD/MSPs.

ISDA recommends a phase-in period through December 21, 2013 for the application of the “foreign branch characteristics” and “with a foreign branch” interpretations under the Cross-Border Guidance.<sup>9</sup> Under the January Order, the application of additional factors was required only for transactions between foreign branches of non-US registrants. As non-registrant counterparties will now be affected (through application of the Transaction-Level Requirements), additional time is needed for the provision of information to counterparties regarding the foreign branch’s status under the new interpretations. In some cases, changes in procedures regarding the location of employees allowed to participate in negotiating a transaction and changes in documentation may need to be put in place in order to contend with the “with a foreign branch” criteria. Unless counterparties can have this reassurance, the market may witness a pull back from transacting with foreign branches.<sup>10</sup>

## II. Lack of Transparency in the Substituted Compliance Determination Process<sup>11</sup>

Lack of information about how substituted compliance determinations are progressing prior to the December 21 expiration date of the Exemptive Order leaves market participants uncertain regarding what preparations they need to undertake at this stage. The result of this uncertainty will be either that firms have insufficient phase-in time (as will happen if substituted compliance is not granted in some or all rule categories and firms’ compliance planning was based on overestimated expectations regarding the prospects for substituted compliance success), or else that preparatory efforts will have been unnecessary and wasted, to the extent those efforts were directed at regulatory provisions for which a substituted compliance determination is ultimately issued. The resulting costs and inefficiencies are ones that the substituted compliance process was intended to prevent.

The substituted compliance application process should be transparent and participatory for market participants: Transparent, so that market participants can understand likely outcomes and the Commission can ensure that the determinations preserve a level playing field, both within and across jurisdictions, as the Commission strives to address differently- regulated entities in the same jurisdiction and jurisdiction-specific “alternative approaches.” Participatory, so that market participants can share their practical viewpoints with regulators and so reach perhaps clearly better, or better-informed, outcomes. The Commission recognizes that additional transitional relief may be needed following a substituted compliance determination.<sup>12</sup> Gauging the need for further transitional relief and the

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<sup>9</sup> See Cross-Border Guidance at 45329-30.

<sup>10</sup> Footnote 43 states that “[f]or purposes of this Exemptive Order, market participants” must apply the “foreign branch” and “with a foreign branch” interpretations in the Cross-border Guidance. From the placement of this footnote in the discussion of SD/MSP requirements, we infer that the Commission did not intend the statement to apply to non-SD/MSPs performing SD de minimis and MSP threshold computations. ISDA requests that the Commission clarify this in its final exemptive order.

<sup>11</sup> Exemptive Order paragraphs 6,7 and 11.

<sup>12</sup> 78 Fed. Reg. 43788, footnote 41.

appropriate time periods will require industry input. The views of market participants, and their greater knowledge of operational practicalities, should be tapped.

Even positive substituted compliance determinations could impose “means by which substituted compliance is achieved”, recordkeeping and documentation requirements, and summary compliance and risk reporting to the Commission.<sup>13</sup> For this reason, as well as the planning difficulties described above resulting from a non-transparent determination process, a 30-day period following the issuance of a substituted compliance determination may not be an adequate phase-in period. In the interest of uniformity among jurisdictions and providing planning certainty for market participants, ISDA suggests that the Commission adopt a period of at least 90 days for the phase-in of substituted compliance after issuance of a determination. An additional phase-in by counterparty type, similar to that based on the Category 1, 2 and 3 classifications used for the phase-in of the clearing mandate, should be considered for particular Transaction-Level Requirements, such as clearing.

When a substituted compliance application is not granted, a phase-in period to implement the Commission’s requirements is needed. Given the inherent situational difficulties, the appropriate time period should be greater than phase-in period available for positive substituted compliance determinations. For foreign branches of US SDs and MSPs, if substituted compliance is not granted for some of all Transaction-Level Requirements, the US SD or MSP should be entitled to comply with local law requirements in the jurisdiction of the branch (to the extent required by such jurisdiction) in lieu of Transaction-Level Requirements, provided that it includes its activities in such jurisdiction for purposes of the 5% aggregate notional value limitation, as provided in the Cross-Border Guidance with respect to jurisdictions other than Australia, Canada, the European Union, Switzerland, Hong Kong and Japan.<sup>14</sup>

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ISDA appreciates the opportunity to provide its comments on the Exemptive Order. Please feel free to contact me or ISDA’s staff at your convenience.

Sincerely,



Robert G. Pickel  
Chief Executive Officer

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<sup>13</sup> Cross-Border Guidance at 45344.

<sup>14</sup> Cross-Border Guidance at 45351.