

July 18, 2016

***Submitted Electronically***

Mr. Christopher Kirkpatrick  
Secretary of the Commission  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21<sup>st</sup> Street NW  
Washington, DC 201581

**Re: Clearing Requirement Determination Under Section 2(h) of the CEA for Interest Rate Swaps (RIN 3038-AE20)**

Dear Mr. Kirkpatrick:

The International Swaps and Derivatives Association, Inc. (“**ISDA**”)<sup>1</sup> appreciates the opportunity to comment on the above-referenced notice of proposed rulemaking (the “**Proposal**”) published by the Commodity Futures Trading Commission (the “**CFTC**”), which would expand upon the CFTC’s existing clearing mandate to cover additional interest rate products that are, or are expected to be, subject to clearing mandates implemented by non-U.S. regulators. In the Proposal, the CFTC states its desire to harmonize its clearing mandate with those of its counterparts in other jurisdictions.

As a core part of its work to make derivatives markets safer and more efficient, ISDA and its members strongly support derivatives clearing to reduce systemic risk and promote market liquidity, both in the United States and globally. Clearing of swaps such as those covered by the Proposal is consistent with the 2009 G20 commitment to clear all standardized over-the-counter (“**OTC**”) derivatives. It is also consistent with the intent of U.S. Congress in Section 723 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. ISDA and its members also strongly support efforts to harmonize derivatives regulation across jurisdictions. Such

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<sup>1</sup> Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has over 850 member institutions from 67 countries. These members comprise a broad range of 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, such as exchanges, intermediaries, clearing houses and depositories, as well as law firms, accounting firms and other service providers. Additional information on ISDA is available at [www.isda.org](http://www.isda.org).

harmonization is crucial to effective and efficient implementation of all of the G20 derivatives reforms.

ISDA commends the CFTC for its efforts in the areas of derivatives clearing and global harmonization of derivatives regulation, both of which are advanced by the Proposal. In order to ensure that the Proposal is implemented in a manner that enhances market liquidity, reduces risk and fosters financial stability, ISDA urges the CFTC to consider the following in any final rulemakings, each of which is discussed in greater detail below:

- In response to the Proposal's request for feedback regarding implementation timing, ISDA and its members strongly support an implementation schedule that follows the effective date of corresponding non-U.S. clearing mandates. Such implementation should also provide an additional phase-in period based on the implementation schedule in CFTC Reg. §50.25.
- Given the low threshold for mandatory trading determinations once a product is subject to mandatory clearing under the CFTC's regulatory framework and the broad application of the CFTC's cross-border guidance, ISDA urges the CFTC to consider issues that ISDA has separately raised in connection with certain aspects of the CFTC's mandatory trading determinations.
- The CFTC should ensure that it has appropriate and adequate data regarding the impact that any expansion of its clearing mandate would have on market participants on both a global and regional basis in order to inform its analysis of the factors in Section 2(h) of the Commodity Exchange Act ("CEA").
- As it works to harmonize its clearing mandate with those of its counterparts in other jurisdictions, we urge the CFTC to consider all aspects of clearing mandates, which include both product scope *and* entity scope.

## **Implementation Timing**

The Proposal provides two alternatives for implementation timing and asks for industry input regarding which alternative should apply if the Proposal is finalized. Under the first alternative, the extended mandate would take effect for market participants subject to the CFTC's clearing mandate 60 days after a final CFTC rule is published in the Federal Register, regardless of whether analogous clearing mandates have taken effect in non-US jurisdictions (this is the so-called "simultaneous effective date"). Under the second alternative, for each product covered by the extended mandate, clearing would be required on the earlier of: (a) 60 days after the effective date of an analogous clearing mandate in the corresponding non-U.S. jurisdiction (*provided that*, in no event would such date be earlier than 60 days after a final CFTC rule is published in the Federal Register); and (b) two years after a final CFTC rule is published in the Federal Register (so-called "alternative compliance dates to coordinate implementation with non-U.S. jurisdictions").

ISDA strongly prefers compliance dates that correspond with the effectiveness of clearing mandates in non-U.S. jurisdictions. This alternative is consistent with the CFTC's objective of global harmonization and also consistent with maximizing liquidity and reducing risk associated with cleared OTC derivatives.

To further promote harmonization, ISDA urges the CFTC to phase-in implementation by counterparty type after the initial 60-day period if the corresponding non-U.S. clearing mandate either (i) applies to a materially narrower set of entities than the CFTC's clearing mandate or (ii) is subject to phased-in implementation based on entity type. Specifically, after the initial 60-day period, a CFTC clearing mandate should be phased in based on the 270-day implementation schedule in CFTC Reg. §50.25, which was used to implement the CFTC's existing clearing mandate. Market participants subject to the CFTC's clearing mandate are familiar with these entity classifications. A longer phase-in is appropriate in these situations to allow entities that are not currently subject to, or preparing to be subject to, a corresponding clearing mandate to address legal, documentation, operational and other considerations prior to a move to clearing.

**Annex A** to this letter sets forth the entity scope (or expected entity scope) of applicable non-U.S. clearing mandates and any applicable phase-in periods. Based on this information, ISDA believes that the additional phase-in time would be appropriate for products subject to clearing mandates in all of the jurisdictions covered by the Proposal (*i.e.*, Australia, Canada, the European Union, Hong Kong, Mexico, Singapore and Switzerland).

### **Link with CFTC's Mandatory Trading Determinations**

ISDA and its members are concerned that the expanded clearing mandate could lead to more mandatory trading determinations for products that may not have the necessary trading liquidity to be executed on a swap execution facility. Under the CFTC's current framework, once a product is subject to the CFTC's clearing mandate, the threshold for whether it is "made available to trade," and therefore subject to mandatory trading requirements, is very low.

The Proposal covers products that are transacted in relatively high volumes outside of the United States. The CFTC should consider the impact that a clearing mandate for these products and any subsequent "made available to trade" determination could have on market liquidity in relevant non-U.S. markets. ISDA believes that as a result of the broad definition of "U.S. person" under the CFTC's cross-border guidance, combined with the current lack of a substituted compliance framework for trade execution platforms, a mandatory trading determination for products covered by the Proposal would have a detrimental impact on trading liquidity and could result in potentially irreversible market fragmentation.

ISDA urges the CFTC to be mindful of the link between a clearing mandate and a mandatory trading determination in any final rules expanding upon its existing clearing mandate. ISDA has separately suggested modifications to the CFTC's mandatory trading requirements, including with respect to the cross-border impacts of such requirements and determinations of when a

product is “made available to trade” under the requirements.<sup>2</sup> In light of these issues, ISDA urges the CFTC to take any available steps (e.g., suspension of self-certification of the “made available to trade” determination under CFTC Reg. §40.6 or no-action relief) in connection with an expansion of its clearing mandate to ensure that only contracts that have sufficient trading liquidity are subject to the mandatory trading requirements.

### **Relevant Data and Analysis**

The data in *Table 17* in the Proposal sets forth percentages of interest rate swap products covered by the Proposal that were cleared in the second quarter of 2015 based on the CFTC’s Part 45 data. However, it is difficult to determine the impact that the Proposal would have on market participants based on this data (*i.e.*, it is difficult to extract and analyze the volume of transactions entered into by entities subject to the CFTC’s clearing mandate that currently enter into transactions covered by the Proposal on an uncleared basis).

It is particularly difficult to determine the impact that the Proposal would have on market participants in an individual jurisdiction. To facilitate a better understanding of such impact, ISDA urges the CFTC to publish the data in *Table 17* on a jurisdiction-by-jurisdiction basis for each of the jurisdictions covered by the Proposal. Additionally, ISDA would welcome the opportunity to work with the CFTC to gather additional data, which could enhance the CFTC’s analysis of the factors in Section 2(h) of the CEA and better inform both the CFTC and the market regarding whether the products covered by the Proposal are suitable for *mandatory* clearing.

ISDA believes that a fulsome understanding of the impact that the Proposal would have on market participants, and of whether the Proposal would have a disparate impact in any of the covered jurisdictions, is necessary to fully analyze whether the CFTC’s clearing mandate should apply to each of the products covered by the Proposal. Such data would also inform the analysis of the effect that mandatory clearing for a product would have on competition under Section 2(h)(2)(D)(ii)(IV).

### **Exempt DCOs**

Several of the products covered by the Proposal are cleared in relatively high volumes on derivatives clearing organizations (“DCOs”) that are exempt from registration instead of registered with the CFTC. By CFTC order, these DCOs may clear for US proprietary accounts but not for US customers. ISDA urges the CFTC to consider the effect that the Proposal’s requirements for certain interest rate swaps denominated in Hong Kong dollars and Australia

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<sup>2</sup> See ISDA Research Note *Cross-Border Fragmentation of Global Interest Rate Derivatives; Second Half 2015 Update* (May 2016), available at <https://www2.isda.org/functional-areas/research/research-notes/>; ISDA *Principles for US/EU Trading Platform Recognition* (February 2016), available at <http://www2.isda.org/functional-areas/public-policy/united-states/>; *Petition for Rulemaking to Amend Parts 1 (General Regulations under the Commodity Exchange Act), 37 (Swap Execution Facilities) and 43 (Real-Time Public Reporting) of the Commodity Futures Trading Commission Regulations* from ISDA to the CFTC, dated June 15, 2015, available at <http://www2.isda.org/functional-areas/public-policy/united-states/>.

dollars could have on clearing such products at OTC Clearing Hong Kong Ltd. and ASX Clear (Futures) Pty Ltd. ISDA also urges the CFTC to further consider the effect that mandatory clearing for products that clear in relatively high volumes on these exempt DCOs would have on competition in the relevant jurisdictions.

In the preamble to the Proposal, the CFTC notes that it considered and was informed by the work of its non-U.S. counterparts. However, ISDA notes that the determinations by regulators in Hong Kong and Australia to require clearing for certain interest rate products denominated in Hong Kong dollars and Australian dollars were likely based in part on an assumption that entities subject to the relevant clearing mandates would be able to clear such products on OTC Clearing Hong Kong Ltd. and ASX Clear (Futures) Pty Ltd., respectively. ISDA urges the CFTC to consider this potential discrepancy.

## **Harmonization Generally**

As noted above, ISDA supports the CFTC's efforts to harmonize its clearing mandate with non-U.S. clearing mandates. Additionally, subject to the modifications discussed above, ISDA supports the extension of the CFTC's clearing mandate in accordance with the Proposal as a step towards achieving such harmonization.

Notwithstanding the foregoing, ISDA would also like to stress the importance of conducting independent analysis regarding whether a particular product is appropriate for mandatory clearing within the CFTC's framework. As discussed above, the CFTC's clearing mandate applies to a different set of entities than the clearing mandates of its non-U.S. counterparts. Perhaps even more importantly, the CFTC is subject to statutory requirements in Section 2(h) of the Commodity Exchange Act when determining whether a swap should be subject to mandatory clearing, which may differ from requirements that apply to regulators in non-U.S. jurisdictions.

ISDA commends the CFTC for conducting an independent analysis in the preamble to the Proposal, subject to the comments above regarding additional issues that the CFTC may want to consider in advance of issuing any final rules. ISDA nonetheless cautions the CFTC from prioritizing harmonization of clearing mandates over a thorough analysis of the impacts that a CFTC clearing mandate may have on liquidity and risk management for a particular product, as well as on the safety and soundness of the U.S. and global derivatives markets.

Instances, including those raised above for certain of the products covered by the Proposal, could arise in which it would not be appropriate for the CFTC's clearing mandate to apply to products covered by non-U.S. clearing mandates due to differences in the framework for the CFTC's clearing mandate or for other reasons particular to the U.S. derivatives markets.<sup>3</sup> Separately, the CFTC does not have any control over the clearing mandates of its counterparts in non-U.S. jurisdictions and therefore should continue to conduct full and robust independent analysis prior to implementing any clearing mandates.

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<sup>3</sup> ISDA notes that if finalized the Proposal would be the first clearing mandate to cover interest rate products settled in currencies other than G4 currencies or the applicable local currency.

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ISDA appreciates the opportunity to provide these comments. If we may provide further information, please do not hesitate to contact the undersigned or other ISDA staff.

Sincerely,

A handwritten signature in black ink, appearing to read "Steven Kennedy". The signature is fluid and cursive, with a long horizontal stroke extending to the right.

Steven Kennedy  
Global Head of Public Policy

**Annex A**

***Entity Scope of Relevant Non-U.S. Clearing Mandates***

	<b>European Union<sup>4</sup></b>	<b>Switzerland</b>	<b>Canada<sup>5</sup></b>	<b>Mexico<sup>6</sup></b>
<b>Entity Scope</b>	Financial counterparties (FC); Non-financial counterparties that exceed the clearing threshold (NFC+); and Third country entities (TCE) that would be an FC or NFC+ if established in EU where (i) dealing with an FC or NFC+ or (ii) dealing with another TCE that would be an FC or NFC+ in certain circumstances.	Financial counterparties that exceed a CHF 8 billion notional-based threshold (FC+); and Non-financial counterparties that exceed the clearing threshold (NFC+).	<b>PROPOSAL:</b> A local counterparty to a transaction in a mandatory clearable derivative if it itself, and the other counterparty, are one or more of the following: (i) a participant subscribing to the services of a regulated clearing agency for a mandatory clearable derivative; (ii) an affiliated entity of a participant described in (i); (iii) a local counterparty that, together with its local affiliated entities, has an aggregate gross notional amount of more than CAD 500 billion in outstanding derivatives as specified under the applicable regulations, after excluding intragroup transactions.	All banks and brokerage firms that trade (i) among themselves or with domestic institutional investors and (ii) with foreign financial institutions or foreign institutional investors (for example, hedge funds); plus any market participants trading non-cleared OTC derivatives now subject to the mandate.
<b>Effectiveness and Phase-In</b>	Expected to enter into force for products covered by the Proposal in August, 2016. Category 1 (Clearing Members) – six months after entry into force. Category 2 (FCs whose group’s aggregate month-end average notional of uncleared derivatives for January, February and March 2016 is above €8billion) – 12 months after entry into force. Category 3 – (all other FCs) – 18 months after entry into force. Category 4 – (NFC+s not in Cat 1, 2, 3) – 36 months after entry into force.	<b>EXPECTED:</b> Phase-in by entity type.	<b>PROPOSAL:</b> No phase-in.	Currently in effect. Phase-in by entity type.

<sup>4</sup> See [http://ec.europa.eu/finance/financial-markets/docs/derivatives/160610-delegated-regulation\\_en.pdf](http://ec.europa.eu/finance/financial-markets/docs/derivatives/160610-delegated-regulation_en.pdf).

<sup>5</sup> See **PROPOSAL** at [http://www.osc.gov.on.ca/documents/en/Securities-Category9/csa\\_20160224\\_94-101\\_roc-derivatives.pdf](http://www.osc.gov.on.ca/documents/en/Securities-Category9/csa_20160224_94-101_roc-derivatives.pdf).

<sup>6</sup> See <http://www.banxico.org.mx/disposiciones/circulares/%7b9EA848A6-2376-3AB8-A8D8-45943278029C%7d.pdf>.

	Hong Kong <sup>7</sup>	Singapore <sup>8</sup>	Australia <sup>9</sup>
<b>Entity Scope</b>	Authorized Financial Institutions (AFIs), Approved Money Brokers (AMBs) and Licensed Corporations (LCs), both local and foreign-incorporated (together, “prescribed persons”), with average local total positions of USD 20 B or more over a 3-month calculation period. <u>Both</u> counterparties must fall within these categories and thresholds for the trade to be required to be cleared. HKMA/SFC has designated a specific list of “Financial Services Providers” (FSPs). A trade between a prescribed person and an FSP is required to be cleared.	<b>PROPOSAL:</b> Banks in Singapore licensed under the Banking Act with aggregate outstanding notional amount of derivatives booked in Singapore exceeding SGD 20 billion on the last day of each of the last 4 quarters. <u>Both</u> counterparties must fall within the above category and threshold for the trade to be required to be cleared.	Australian or foreign financial entities which are Australian Authorized Deposit-Taking Entities (ADIs), Australian financial services licensees (AFS licensees) or exempt foreign licensees (as applicable) with gross notional outstanding positions of AUD 100 billion or more on two consecutive quarterly calculation dates and any other entities which wish to opt-in (Clearing Entities) are subject to mandatory clearing when trading with (i) another Clearing Entity or (ii) a Foreign Internationally Active Dealer ( <i>e.g.</i> , CFTC SDs, SEC SBSDs) (subject to certain conditions when the Clearing Entity is a Foreign Clearing Entity). For trades involving two Clearing Entities, both counterparties must fall within those categories and thresholds for the trade to be required to be cleared.
<b>Effectiveness and Phase-In</b>	Will take effect July 1, 2017. No phase-in.	<b>PROPOSAL:</b> No phase-in.	Currently in effect ( <i>except for</i> AUD FRAs and AUD OIS). AUD FRAs in effect from April 2018. AUD OIS in effect from October 2016.

<sup>7</sup> See <http://www.gld.gov.hk/egazette/pdf/20162005/es22016200528.pdf>.

<sup>8</sup> See **PROPOSAL** at <http://www.mas.gov.sg/~media/MAS/News%20and%20Publications/Consultation%20Papers/Consultation%20Paper%20on%20Draft%20Regulations%20for%20Mandatory%20Clearing%20of%20Derivatives%20Contracts.pdf>.

<sup>9</sup> See <https://www.legislation.gov.au/Details/F2015L01960>.