

November 18, 2019

Mr. Christopher Kirkpatrick
Secretary
U.S. Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

Re: Registration with Alternative Compliance for Non-U.S. Derivatives Clearing Organizations;
Notice of Proposed Rulemaking (RIN 3038-AE87)

Dear Secretary Kirkpatrick:

The International Swaps and Derivatives Association, Inc. (“**ISDA**”)¹ appreciates the opportunity to provide comments to the U.S. Commodity Futures Trading Commission (“**CFTC**” or “**Commission**”) regarding the Commission’s Notice of Proposed Rulemaking: Registration with Alternative Compliance for Non-U.S. Derivatives Clearing Organizations (“**DCO**”) Registration (the “**Proposal**”) published on July 19, 2019.²

ISDA generally supports the Commission’s proposed alternative compliance framework for non-U.S. DCOs and the proposed territorial, risk-based approach to the regulation of central clearing counterparties (“**CCPs**”).³ Market participants and market facilities that operate in global swaps markets are subject to multiple levels of comprehensive regulatory oversight, thus incurring extraordinary compliance costs. The Commission appropriately recognizes that there is no regulatory benefit in subjecting CCPs to additional compliance costs when there is already a primary regulator in charge of conducting oversight and review of essentially the same requirements.

We appreciate that the Proposal relies on foreign regulatory regimes in allowing alternative compliance for non-U.S. CCPs, and encourage the CFTC to continue its dialogue with regulators in the EU and other jurisdictions to ensure that CCP supervision is based on deference to home country regulations. We note that, absent a coordinated approach among regulators that applies

¹ Since 1985, ISDA has worked to make the global derivatives markets safer and more efficient. Today, ISDA has more than 900 member institutions from 70 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 <http://www.isda.org>.

² Registration with Alternative Compliance for Non-U.S. Derivatives Clearing Organizations, Notice of Proposed Rulemaking, 84 Fed. Reg. 34819 (July 19, 2019), <https://www.govinfo.gov/content/pkg/FR-2019-07-19/pdf/2019-15262.pdf>.

³ We believe that the Commission should take a similar territorial, risk-based approach with respect to other aspects of the CFTC’s cross-border regime. Please see ISDA Cross-Border Harmonization White Paper, <https://www.isda.org/a/9SKDE/ISDA-Cross-Border-Harmonization-FINAL2.pdf>, for more details.

principles of deference and outcomes-based comparability, the application of inconsistent and duplicative regulatory frameworks on CCPs will lead to the fragmentation of global cleared derivatives markets.⁴

As we indicated in our response to European Securities and Markets Authority's proposed approach to determining the systemic importance of third country CCPs under the European Market Infrastructure Regulation,⁵ it is important to establish a consistent, global approach to assessing systemically important CCPs that would ensure comparability across jurisdictions and minimize the risk of divergences between various regimes in addressing CCP-related systemic risk concerns.

While we largely agree with the Commission's proposed approach to regulating non-U.S. CCPs, there is one aspect of the Proposal that deserves comment—the proposed test for determining whether a non-U.S. CCP poses significant risk to the U.S. financial system⁶ and therefore would not be permitted to apply for the proposed alternative compliance regime. The test under the Proposal is that: (1) the DCO must not hold 20% or more of the required initial margin of U.S. clearing members for swaps across all registered or exempt DCOs; and/or (2) 20% or more of the initial margin requirements for swaps at that DCO must not be attributable to U.S. clearing members.⁷

We are generally supportive of clear thresholds for determining whether a CCP poses substantial risk to the U.S. financial system. We are concerned, however, that the second prong of the test misses the mark in assessing whether a CCP poses substantial risk to the U.S. financial system. The second prong does not gauge the risk of the relevant CCP to the U.S. financial system, but rather signifies the importance of U.S. clearing members to a particular CCP. Therefore, it may capture smaller-sized DCOs due to the large global presence of U.S. banking groups, including foreign branches of U.S. banking groups. A small CCP with very few clearing members and minimum exposure to the U.S. financial system may be deemed as having “substantial risk” simply because 20% or more of the initial margin collected is attributed to U.S. clearing members.

For example, a DCO may have a total of \$100 million in initial margin with \$21 million initial margin attributed to a U.S. clearing member. In this case, the U.S. clearing member's position does not pose systemic risk to U.S. markets. Additionally, the second prong may incentivize non-U.S. CCPs to limit, or put a cap on, clearing for U.S. persons for fear of being designated as posing significant risk to the U.S. financial system and thus coming into full scope of the DCO regime. This would be disadvantageous for U.S. banking groups, and could be viewed as

⁴ For more details, *see* ISDA, Regulatory-Driven Market Fragmentation (Jan. 2019), <https://www.isda.org/a/wpgME/Regulatory-Driven-Market-Fragmentation-January-2019-1.pdf>; *see also* ISDA Cross-Border Harmonization, <https://www.isda.org/a/9SKDE/ISDA-Cross-Border-Harmonization-FINAL2.pdf>.

⁵ *See* ISDA's response to the EMIR consultation at: <https://www.isda.org/2019/07/31/final-response-to-tiering-and-comparable-compliance-esma/>.

⁶ *See* ISDA's response to the EMIR consultation at: <https://www.isda.org/2019/07/31/final-response-to-tiering-and-comparable-compliance-esma/>.

⁷ Proposal at 34821-22.

violating the spirit of the PFMI requirement to provide non-discriminative treatment of all clearing members.⁸

For these reasons, the second prong of the test should be eliminated. At a minimum, the test should permit the Commission to determine whether a CCP poses “substantial risk” only if both of the two thresholds exceed 20%. This would more accurately capture the risks to the U.S. financial system and the CFTC’s intent to allow non-U.S. CCPs to comply with their home country regulations in lieu of certain Commission regulations.

In addition, we believe that the final rule should be revised to exclude foreign subsidiaries of U.S. swap dealers from the definition of U.S. clearing members to align with the treatment of foreign subsidiaries under the CFTC Cross-border Guidance.⁹ U.S. clearing members are defined in the Proposal as “clearing member[s] organized in the United States or whose ultimate parent company is organized in the United States, or an FCM.”¹⁰ Under the CFTC Cross-border Guidance, however, subsidiaries of U.S. swap dealers are not considered U.S. persons simply by virtue of being a part of a U.S. banking group.

Moreover, including subsidiaries in the definition would disincentivize non-U.S. DCOs from accepting significant levels of business from such subsidiaries in order to remain below the threshold, thus as stated above, putting U.S. banking groups at a competitive disadvantage. To ensure a consistent regulatory approach to the cross-border treatment of foreign subsidiaries and to allow market participants continued access to global liquidity pools, the Commission should amend the definition of U.S. clearing members to exclude foreign subsidiaries of U.S. swap dealers.

Another concern with respect to the proposed “substantial risk” test relates to the CFTC’s intent to “retain discretion in determining whether a non-U.S. DCO poses substantial risk to the U.S. financial system, particularly where the DCO is close to 20 percent on both prongs of the test. In these cases, in making its determination, the Commission may look at other factors that may reduce or mitigate the DCO’s risk to the U.S. financial system or provide a better indication of the DCO’s risk to the U.S. financial system.”¹¹ We believe that such statements undermine the Commission’s objective to provide a bright-line test and may lead to legal and compliance uncertainty. We therefore ask the Commission to clarify what “other factors” might reduce or mitigate, or provide a better indication of, a DCO’s risk to the U.S. financial system.¹²

⁸ Principle 18 (access and participation requirements) of the PFMI.

⁹ See Interpretive Guidance and Policy Statement Regarding Compliance with Certain Swap Regulations; Rule (July 26, 2013), available at

<https://www.cftc.gov/sites/default/files/idc/groups/public/@lrfederalregister/documents/file/2013-17958a.pdf>.

¹⁰ Registration with Alternative Compliance for Non-U.S. Derivatives Clearing Organizations, Notice of Proposed Rulemaking, 84 Fed. Reg. 34819 (July 19, 2019), <https://www.govinfo.gov/content/pkg/FR-2019-07-19/pdf/2019-15262.pdf>.

¹¹ Proposal at 35460.

¹² We also ask the Commission to provide transitional relief to foreign CCPs that currently operate under the CFTC’s no-action relief to allow these clearing organizations to continue to clear proprietary trades of U.S. clearing members. In the event of an exempt DCO exceeding the threshold, we believe time-limited relief should be provided to allow market participants to take the necessary steps to migrate their business and operations.

Finally, we ask the Commission to affirm that the CFTC will monitor the 20% threshold test by analyzing the data required to be reported to the CFTC, and that the relevant non-U.S. DCO has no other obligations with respect to the monitoring of the 20% threshold apart from such reporting requirements.

We appreciate the Commission's efforts to address longstanding concerns regarding the duplicative oversight of CCPs that operate on a global scale. Our members are strongly committed to maintaining the safety and efficiency of global derivatives markets and hope that the Commission will consider our recommendations, as they reflect the extensive knowledge and experience of industry professionals within our membership.

Please feel free to contact Bella Rozenberg, Senior Counsel and Head of Regulatory and Legal Practice Group, (202)-683-9334, if you have questions.

A handwritten signature in blue ink, reading "Bella Rozenberg". The signature is fluid and cursive, with the first name "Bella" and last name "Rozenberg" clearly distinguishable.

Bella Rozenberg
Senior Counsel & Head of Regulatory and Legal Practice Group
ISDA