



March 9, 2020

Mr. Christopher J. Kirkpatrick  
Secretary  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21st Street NW  
Washington, DC 20581

**Re: Cross-Border Application of the Registration Thresholds and Certain Requirements  
Applicable to Swap Dealers and Major Swap Participants (RIN 3038–AE84)**

Dear Mr. Kirkpatrick:

Citadel appreciates the opportunity to provide comments to the Commodity Futures Trading Commission (the “Commission”) on the proposal regarding the cross-border application of certain swap requirements (the “Proposal”).<sup>1</sup>

We strongly support the Commission’s continued efforts to promote market safety, stability and integrity, while improving conditions for investors through increased transparency and competition. In this regard, we agree with the Commission re-affirming its prior conclusion that swap transactions arranged, negotiated or executed using personnel located in the United States (“ANE Transactions”) fall squarely within the Commission’s jurisdiction under the Commodity Exchange Act (“CEA”), even if the transactions are booked to non-U.S. entities.<sup>2</sup> These transactions clearly constitute swap activity *in the United States*, and can pose risks to the U.S. financial system.

While we also agree that the Commission should apply its jurisdiction over ANE Transactions in a targeted manner, taking into account principles of international comity, we are concerned that the Proposal grants ANE Transactions overly broad exemptions. As we explain below, in no event should the Commission apply the proposed approach to regulatory reporting and public reporting, as these are central to the Commission’s supervisory interests and statutory objectives. Instead, the Commission should more closely harmonize with the approach taken by the Securities and Exchange Commission (“SEC”) and rely on transparent and comprehensive comparability determinations to mitigate any potential for overlapping or duplicative requirements.

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<sup>1</sup> 85 Fed. Reg. 952 (Jan. 8, 2020), available at: <https://www.cftc.gov/sites/default/files/2020/01/2019-28075a.pdf>.

<sup>2</sup> See Proposal at 978.

## I. The Commission Has Jurisdiction Over ANE Transactions

ANE Transactions fall squarely within the Commission’s jurisdiction under the CEA, as the transactions are arranged, negotiated or executed using personnel located in the U.S.<sup>3</sup> This conclusion is consistent with prior Commission action<sup>4</sup> and with the position taken by the SEC.<sup>5</sup>

As the Commission correctly observes, a firm that “engages in market-facing activity using personnel located in the United States is conducting a substantial aspect of its dealing business in the United States.”<sup>6</sup> Therefore, recognizing jurisdiction over ANE Transactions helps to ensure that financial firms are not able to operate in the U.S. and avoid Commission oversight merely by booking swaps to a non-U.S. entity. This levels the playing field between U.S. and non-U.S. swap dealers and ultimately protects the U.S. financial system, as the financial risks related to ANE Transactions may not always remain in the entity in which the swaps are booked given that U.S. financial groups can be expected to stand behind the obligations of their offshore affiliates (even in the absence of an explicit guarantee).

## II. The Commission Should Apply Regulatory and Public Reporting Requirements to ANE Transactions

Having affirmed jurisdiction over ANE Transactions, the Commission must determine how to apply that jurisdiction. We agree that the Commission should apply its jurisdiction over ANE Transactions in a targeted manner, taking into account principles of international comity, as well as its supervisory interests and statutory objectives. As highlighted by the Commission, relevant statutory objectives include not only mitigating systemic risk, but also increasing transparency, competition, and market integrity.<sup>7</sup> These considerations lead to the conclusion that, at a minimum, regulatory and public reporting requirements should apply to ANE Transactions.

The Commission has a strong supervisory interest in monitoring and surveilling trading activity that occurs in the U.S. As a result, regulatory reporting requirements should apply to ANE Transactions, particularly since these transactions could account for a material portion of total swap dealing activity in the U.S. This will enable the Commission to better monitor for disruptive

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<sup>3</sup> Given the Commission’s exclusive jurisdiction over “agreements . . . and transactions involving swaps” in the United States pursuant to CEA section 2(a)(1)(A), it is not necessary to address the Commission’s extraterritorial jurisdiction in the context of ANE Transactions. However, even if ANE Transactions could be viewed as outside the Commission’s domestic jurisdiction, they would clearly be captured by the Commission’s extraterritorial authority under CEA section 2(i) given their direct and significant connection with activities in, or effect on, commerce of the United States.

<sup>4</sup> See, e.g., 78 Fed. Reg. 45292 (July 26, 2013) at 45350 FN 513, available at: <https://www.cftc.gov/sites/default/files/idc/groups/public/@lrfederalregister/documents/file/2013-17958a.pdf> and CFTC Staff Advisory No. 13–69 (Nov. 14, 2013), available at: <http://www.cftc.gov/idc/groups/public/@lrfederalregister/documents/letter/13-69.pdf>.

<sup>5</sup> 85 Fed. Reg. 6270 (Feb. 4, 2020) at 6272, available at: <https://www.govinfo.gov/content/pkg/FR-2020-02-04/pdf/2019-27760.pdf>.

<sup>6</sup> Proposal at 978.

<sup>7</sup> See Proposal at 953.

trading practices and will also provide the necessary data regarding overall market trading activity to allow the Commission to evaluate market trends and accurately assess the impact of other reforms implemented in the swaps market.

Public reporting requirements should also apply to ANE Transactions in light of the policy objectives of increasing transparency and enhancing price discovery for U.S. investors.<sup>8</sup> Data shows that, following the Commission granting no-action relief from public reporting and other transaction-level requirements for ANE Transactions,<sup>9</sup> interdealer trading activity in EUR interest rate swaps began to be booked almost exclusively to non-U.S. entities, a fact pattern that is “consistent with (although not direct proof of) swap dealers strategically choosing the location of the desk executing a particular trade in order to avoid trading in a more transparent and competitive setting.”<sup>10</sup> This has greatly reduced market transparency in EUR interest rate swaps for U.S. investors, jeopardizing the intended benefits of the Commission’s public reporting regime. Where public reporting is comprehensively implemented, market research consistently concludes that the benefits are material, including for Commission-regulated swaps<sup>11</sup> and corporate bonds.<sup>12</sup> However, leaving material gaps in the public reporting framework will impede the ability of U.S. investors to measure execution quality, perpetuating information asymmetries that benefit the incumbent bank liquidity providers and decreasing overall market competition.

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<sup>8</sup> *Id.*

<sup>9</sup> See CFTC Letter No. 13-71 (Nov. 26, 2013), available at: <https://www.cftc.gov/sites/default/files/idc/groups/public/@lrllettergeneral/documents/letter/13-71.pdf>.

<sup>10</sup> Benos, E., Payne, R., and Vasios, M., Centralized trading, transparency and interest rate swap market liquidity: evidence from the implementation of the Dodd-Frank Act, Bank of England Staff Working Paper (May 2018) at page 30, available at: <https://www.bankofengland.co.uk/-/media/boe/files/working-paper/2018/centralized-trading-transparency-and-interest-rate-swap-market-liquidity-update>.

<sup>11</sup> See, e.g., Loon, Y. C., Zhong, Z. K. The impact of central clearing on counterparty risk, liquidity, and trading: Evidence from the credit default swap market. *Journal of Financial Economics* (2013), available at: [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2176561](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2176561); and Loon, Y. C., Zhong, Z. K. Does Dodd-Frank affect OTC transaction costs and liquidity? Evidence from real-time CDS trade reports. *Journal of Financial Economics*, (2015), available at: [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2443654](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2443654)

<sup>12</sup> See, e.g., Asquith, P., et al., “The Effects of Mandatory Transparency in Financial Market Design: Evidence from the Corporate Bond Market” (April 2019), available at: <https://www.nber.org/papers/w19417>; Bessembinder, H., et al., “Market transparency, liquidity externalities, and institutional trading costs in corporate bonds” (2006) *Journal of Financial Economics*, available at: [https://www.researchgate.net/publication/222515781\\_Market\\_Transparency\\_Liquidity\\_Externalities\\_and\\_Institutional\\_Trading\\_Costs\\_in\\_Corporate\\_Bonds](https://www.researchgate.net/publication/222515781_Market_Transparency_Liquidity_Externalities_and_Institutional_Trading_Costs_in_Corporate_Bonds); Edwards, A. K., et al., “Corporate bond market transaction costs and transparency” (2007) *The Journal of Finance*, available at: [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=593823](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=593823); and Jacobsen, S., et al., “Does trade reporting improve market quality in an institutional market? Evidence from 144A corporate bonds” (2018), available at: [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3171056](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3171056).

As a result, we recommend that the Commission, at a minimum, apply regulatory and public reporting requirements to ANE Transactions. This would be consistent with the SEC’s approach,<sup>13</sup> and will ensure that both the Commission and U.S. investors have adequate information regarding trading activity in ANE Transactions. We note that the Proposal does not appear to analyze current trading volumes in ANE Transactions, an analysis which should be performed prior to granting any regulatory exemptions. This analysis, including whether ANE transactions are typically executed (i) on a cleared or uncleared basis and (ii) on-venue or off-venue, will also inform whether it is appropriate to apply certain other transaction-level requirements to ANE Transactions, such as the Commission’s clearing and SEF trading requirements.

### **III. The Commission Should Rely on Transparent and Comprehensive Comparability Determinations**

We agree with the Commission that substituted compliance may be appropriate for non-U.S. swap entities (excluding U.S. branches) and foreign branches of U.S. swap entities in certain circumstances, including for ANE Transactions.<sup>14</sup> However, substituted compliance should only be permitted following a transparent and comprehensive comparability determination. In this regard, we are concerned that the Proposal contains two main flaws:

- Actual comparability is not required in order for the Commission to grant substituted compliance; and
- Public feedback does not appear to be contemplated.

First, while we agree that the Commission may not need to perform a line-by-line comparison of rule text in order to determine that a foreign jurisdiction is comparable, a substantive comparison must still be undertaken for each entity-level or transaction-level requirement. For example, in order for the Commission to determine that a foreign jurisdiction has comparable public reporting requirements, it would need to conclude that the public reporting requirements in that jurisdiction provide an equivalent level of transparency to market participants. In contrast, the Proposal appears to suggest that the Commission could determine that a foreign jurisdiction has comparable public reporting requirements even if it had no public reporting requirements at all, based on a “holistic finding of comparability that considers the broader context of a foreign jurisdiction’s related regulatory standards.”<sup>15</sup> In our view, this introduces an unacceptable level of discretion and subjectivity into a process that should be based on an objective comparison of regulatory requirements and market outcomes. In addition, it raises the prospect that U.S. investors may be harmed (even if their transactions are not eligible for substituted compliance) by an overall reduction in market transparency and liquidity if trading activity is permitted to migrate to less transparent jurisdictions as a result of inaccurate comparability determinations.

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<sup>13</sup> See 81 Fed. Reg. 53546 (Aug. 12, 2016), available at: <https://www.govinfo.gov/content/pkg/FR-2016-08-12/pdf/2016-17032.pdf>.

<sup>14</sup> Proposal at 985. We do not agree with further expanding the scope of entities eligible for substituted compliance.

<sup>15</sup> Proposal at 987. See also Proposal at 986, FN 342.

Second, we recommend that the Commission provide an opportunity for public feedback prior to finalizing a comparability determination. This will help to ensure the Commission has considered all relevant costs and benefits prior to finalizing a determination that could influence where swaps trading activity is conducted.

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We appreciate the opportunity to provide comments on the Proposal. Please feel free to call the undersigned at (646) 403-8200 with any questions regarding these comments.

Respectfully,

/s/ Stephen John Berger

Managing Director

Global Head of Government & Regulatory Policy