By Electronic Mail

August 27, 2012
Commodity Futures Trading Commission
Three Lafayette Center
1155 21st Street, N.W.
Washington, D.C. 20219
Attention: David A. Stawick, Secretary

Regarding: Cross-Border Application of Certain Swaps Provisions of the Commodity Exchange Act

Dear Mr. Stawick:

The Financial Services Roundtable ("the Roundtable")[1] respectfully submits these comments in response to the proposed interpretive guidance and policy statement ("Cross-Border Guidance" or "Guidance") released by the Commodity Futures Trading Commission (the "Commission) regarding the application of the swaps provisions of Title VII of the Dodd-Frank Act to transactions involving non-U.S. based participants.[2] The Guidance represents the Commission's attempt to define its authority under Section § 2(i) of the Commodity Exchange Act ("CEA"), which governs the extraterritorial reach of the regulatory requirements applied to swaps transactions by Title VII of Dodd-Frank.

As an initial point, we believe that the gravity of the issues posed by the proposed Cross-Border Guidance merit the use of a formal rulemaking under the Administrative Procedures Act. The cross-border scope of CFTC authority is a key issue considering the global nature of the swaps market. As new swaps regulations are developed, it is vital that regulators acknowledge not only the importance of safety and transparency but also the importance of clarity and international comity. Domestic rules that are vague in either their requirements or in the application to foreign markets may place U.S. firms at a competitive disadvantage with regard to their international operations. Conversely, U.S. persons seeking financial services from foreign-based firms may encounter reduced options if market participants face the possible imposition of onerous and duplicative U.S. requirements. The Financial Stability Board ("FSB") and other international bodies have repeatedly stressed the importance of international standardization in the implementation of new derivatives requirements.[3] We believe that addressing this issue

[1] The Financial Services Roundtable represents 100 of the largest integrated financial services companies providing banking, insurance, and investment products and services to the American consumer. Member companies participate through the Chief Executive Officer and other senior executives nominated by the CEO. Roundtable member companies provide fuel for America's economic engine, accounting directly for $92.7 trillion in managed assets, $1.2 trillion in revenue, and 2.3 million jobs.
[2] Cross-Border Application of Certain Swaps Provisions of the Commodity Exchange Act, 77 Fed. Reg. 41214 (Jul. 12, 2012) (hereinafter "Cross-Border Guidance" or "Guidance").
[3] See Implementing OTC Derivatives Market Reforms, The Financial Stability Board, 7 (25 Oct. 2010).

pursuant to a formal rulemaking process or under the guise of a formal "memorandum of understanding" between international regulators would have better achieved the goal of creating a workable and transparent system for governing cross-border swap transactions. As it now stands, however, the Commission's Guidance lacks the benefit of a formal cost-benefit analysis or the pre-proposal input of foreign regulators regarding the viability and impact of the Commission's plan regarding cross-border regulation. As our comments will note below, the Proposed Guidance remains strikingly ambiguous on several key points. This ambiguity is all the more stark when considering that, as guidance, the proposal does not purport to extend any safe harbor protections for entities seeking to conduct their swaps activities beyond the purview of Title VII's requirements.[4] Generally, we also believe that the Guidance must be revised to reduce disparate treatment of different corporate structures within the financial market. These changes will help ensure that competitive parity is maintained regardless of the origin of any particular swaps entity.

In our letter we will also note the following broad concerns with respect to the Commission's current proposal:

- The proposed definition of the term "U.S. person" should be narrowed.
- The Guidance should expand the types of transactions that are exempt from aggregation for purposes of the "swap dealer" de minimis exception.
- The Guidance should expand and clarify when "substituted compliance" for Title VII requirements will be available.
- The Guidance should clarify and limit the scope of non-Title VII requirements on foreign entities.

I. The proposed definition of the term "U.S. person" should be narrowed.

As noted by the Commission in the proposed Guidance, Section 722(d) of the Dodd-Frank Act added § 2(i) to the CEA which governs the international reach of Title VII's requirements on covered-swaps transactions. Section 2(i) states that Title VII "shall not apply" to activities outside the United States unless those activities— "(1) have a direct and significant connection with activities in, or effect on, commerce of the United States; or (2) contravene such rules or regulations as the Commission may prescribe or promulgate as are necessary or appropriate to prevent the evasion of any provision of this Act that was enacted by the [Dodd-Frank] Act of 2010."[5]

The Commission's Cross-Border Guidance proposes to apply the stated "direct and significant" test contained in § 2(i) by creating a class of person deemed to be "U.S. persons." Foreign-based entities must aggregate their swaps transactions with "U.S. persons" to see if they must formally register "swap dealers" or "major swap participants" and be regulated under Title VII of Dodd-Frank. The Guidance then promulgates proposed criteria for when foreign Title VII

[4] See Cross-Border Guidance at 41,217.
[5] Cross-Border Guidance at 41,217-41,218.

registrants may rely on foreign regulations when fulfilling Title VII's regulatory requirements and when they must strictly apply the rules articulated in the Commission's U.S. rulemakings.

Overall, the Commission's definition of "U.S. person" for cross-border purposes is a key component of the rule that will guide the scope of the Commission's regulatory authority. As an outgrowth of the Guidance, swap entities will be forced to review their transactions, literally on a case-by-case basis to determine which of their counterparties meet the Commission's newly articulated standard for U.S. person.

Many Roundtable members have expressed to us the difficulties they will face in implementing the Commission's definition of "U.S. person" as proposed. Our members note that one provision of the definitions, that U.S. persons will include legal entities "in which the direct or indirect owners thereof are responsible for the liabilities of such entity and one or more of such owners is a U.S. person"[6] represents a new concept that is unclear. Although one interpretation of this language is that it is intended only to pick up general partnerships (or limited partnerships where the general partner is a U.S. person), an alternative interpretation would require the reevaluation of most if not all counterparty relationships in order to determine what type of liability guarantees exist between an entity and its parent company or owner. Most swaps market participants currently have no procedures for collecting or even identifying the source of such information from their counterparties. It is unclear how quickly systems could be developed to reliably track and confirm this particular piece of counterparty information, or even if clients in the financial market would be willing to disclosure such information. At an initial level, problems with verification could lead to disparate "U.S. person" determinations with respect to the same entity, creating harmful competitive disadvantages and overall regulatory uncertainty. At its core, however, we believe the Guidance's proposed conception of U.S. person would impose a costly new data collection requirement on entities who may justifiably believe that their activities do not merit the supervision of U.S. regulators under the "direct and significant effect on U.S. Commerce" test contained in CEA § 2(i).

We further believe that the proposed U.S. person definition, as articulated, may reduce opportunities for U.S. affiliated entities that are seeking financing opportunities overseas. These include (i) investment funds or other vehicles with at least some U.S. ownership and (ii) foreign affiliates of U.S. companies, even where such foreign affiliates do not hold a U.S. guarantee . Foreign institutions facing the potential burden necessary to verify the status of such institutions may deliberately elect not to conduct business with any U.S. affiliated organizations. We believe that the Commission should work to ensure that such consequences do not occur as a result of its proposed regulation.

Overall, we believe the Commission's proposed definition of U.S. person to be substantially overbroad. As stated, the rule would cover even minority-U.S. owned institutions based only on a pro-rata (or less) parent liability guarantee.[7] The central focus that the proposal puts on guarantees seems especially misplaced in the absence of any independent empirical study. While we agree the Commission must develop rules that are cognizant of the complexities of international financial institutions, the U.S. person framework contained in the

[6] Cross-Border Guidance at 41,218.
[7] *Id.*

Cross-Border Guidance is not well-tailored to the examples from the 2008 financial crisis cited by the Commission. Furthermore, since 2008 multiple reforms have taken effect to increase capital and decrease leverage in all sectors of the financial market. We believe any discussion on the broad application of any new rule to globally active financial entities must be made with the consideration of such reforms in mind.

If the Commission retains its current framework, we believe that the definition of U.S. person contained in the guidance should be simplified to include only those entities that are residents of the United States, have a principal place of business in the United States, or have majority U.S. ownership. Such a definition should be sufficient, especially if the Guidance retains its current caveat that the proposed definition includes, but is not "limited to," any of the entities that are specifically denominated.[8]

II. The Guidance should expand the types of transactions that are exempt from aggregation when determining an entity's status under the swap dealer *de minimis* standard.

In determining whether a non-U.S. entity's transactions merit registration as a swap dealer under Title VII, the Commission's Guidance directs that the entity aggregate the notional value of all swap dealing transactions entered into by its affiliates under common control.[9] The resulting total is used to determine whether the entity's activities are above or below the limit for the *de minims* exception to the definition of swap dealer that has been set by the Commission. The aggregation requirement is in keeping with Commission Rule 1.3(ggg)(4) which was adopted as part of the Commission's final rule on the definition of swap dealer and major swap participant under Title VII.[10]

We believe that this portion of the Cross-Border Guidance again poses the risk that the Commission's Guidance will be applied much too broadly. Specifically, as a result of the current "common control" test in the proposal, any non-U.S. entity that engages in a *de minimis* amount of swap dealing and is affiliated with a registered Title VII dealer may, by default, be required to register simply because of its affiliation with an entity that is already registered and regulated with respect to U.S. standards. To avoid registration, the non-U.S. entity would seemingly be forced to verify that none of its transactions with U.S. persons constitute swap dealing under the Commission's regulations.

Moreover, by proposing to aggregate the swaps activities of all non-U.S. entities for purposes of the *de minimis* threshold, the Commission arguably would require a level of coordination and information sharing across international borders that may be illegal in some circumstances and may undermine the Commission's goals by forcing coordination or centralization of swaps activities that are now independent and local. The Commission's aggregation rules were based on a concern that entities that should be registering as swap dealers would evade registration by subdividing their swaps dealing activity into multiple entities. As the market moves toward implementation, however, the adverse consequences of that anti-evasion rule are becoming clearer, especially in the context of United States banks that are part

[8] Cross-Border Guidance at 41,218.
[9] Cross-Border Guidance at 41,219.
[10] Registration of Swap Dealers and Major Swap Participants, 77 Fed. Reg. 2613 (Jan. 19, 2012).

of multinational financial groups with entities regulated in numerous jurisdictions. In particular, U.S. banks are finding that they neither have access to information about, nor control over, the swaps activities of their non-U.S. affiliates. We therefore believe that aggregation should not be required beyond national (or international) borders. For instance, although it may be justifiable to require aggregation of the U.S. facing swaps activities of all affiliated entities located in Germany, for instance, we do not consider it reasonable to require a small Ecuadoran subsidiary of that entity that engages in a handful of swaps with U.S. persons to either inform itself about the activities of its German affiliates, register as a swap dealer in the U.S., or terminate that activity. Nor do we believe that a U.S. bank that has had no engagement with the Ecuadoran subsidiary of its German parent should—in the absence of evasion--have to count the activities of the Ecuadoran subsidiary (or the separately regulated German parent) in assessing its ability to rely on the *de minimis* exception.

We again believe that the Commission's Guidance regarding aggregation will have the unintended effect of limiting the financial options of U.S. persons overseas. We anticipate that some foreign-based entities will move to register formally with the Commission. However, we do not believe that such registration should give the Commission license to monitor the swaps activities of each and every affiliate of these organizations. Obviously, entities who register as swap dealers will present certain benefits to their counterparties. Those transactions will be governed by heightened disclosure and business conduct standards. However, Congress contemplated a *de minimis* exception from regulation as a swap dealer, and the Commission's aggregation proposals may effectively eliminate that for many non-U.S. entities.

Overall, the aggregation rule goes well beyond what is necessary in order to ensure that swap dealing is regulated in circumstances where U.S. commerce is significantly affected, and fails to respect legitimate (and often legally mandated) separations of both information and operations among affiliated entities. We request that the Commission amend this portion of the rule to allow all non-U.S. entities to exclude that value of swap positions taken by registered Title VII affiliates when determining their status under the *de minimis* threshold.

Consistent with the foregoing, the Roundtable also asks the Commission to clarify the aggregation requirements of the *de minimis* exception with reference to U.S. based affiliates of foreign financial companies. We note that in the Cross-Border release, foreign entities need not aggregate the positions of U.S. based affiliates when determining their status under the *de minimis* limit.[11] Ostensibly, this determination was reached because the swaps operations of such entities clearly fall within the full purview of U.S.-based swap regulations. Similarly, we believe that when determining their own status under the *de minimis* exception, U.S. affiliates of foreign institutions should not be required to aggregate the swaps positions of their foreign-based affiliates. Such treatment is in keeping with the importance of international comity and will ensure the viability of the United States as a market for investment by foreign financial institutions. An aggregation rule as we propose will ensure that U.S. based affiliates of foreign firms do not have to report higher de minimis figures than what is submitted by their foreign affiliates. It will also keep U.S. based affiliates from facing the untenable position of accessing and reviewing large amounts of data on the activities of numerous affiliates. Such information

[11] Cross-Border Guidance at 41,220.

will often be subject to blocking statutes and other bank secrecy laws, making full access to it unlikely.

III. The Guidance should expand upon and clarify when "substituted compliance" for Title VII requirements will be available.

Under the current proposed Cross-Border Guidance, Title VII requirements are divided into two large categories, "Entity Level" and "Transaction Level," for purposes of determining when compliance with foreign regulations will act as a substitute for compliance with U.S. regulations. This issue is of particular interest to our members who will likely register with the Commission as non-U.S. swap dealers or who are U.S. swap dealers that maintain branches, agencies, affiliates, or subsidiaries in foreign markets. As a default matter, each of these entities will be subject to the regulatory regime of each of the respective financial markets in which it operates.

The Proposed Guidance states that substituted compliance will be allowed in the case of Entity Level requirements when the Commission finds that "such requirements are comparable to cognate requirements under the CEA and Commission regulations."[12] With respect to Transaction Level Requirements, the Proposed Guidance states that substituted compliance will not be permitted to the extent that foreign swap dealers or foreign affiliates of U.S. based swap dealers conduct transactions with a U.S. person.[13] The Proposed Guidance would, however, allow substituted compliance in cases where the transaction was conducted with a non-U.S. person even if the swap obligations are guaranteed by a U.S. person.

As an initial matter, we support the Commission's observation that "comparable does not necessarily mean identical" and that foreign requirements may be found acceptable for purposes of substituted compliance despite being different from U.S. standards.[14] We believe that these statements are consistent with a principles-based review process that considers the objectives of the regulatory requirement and is not merely a comparison to the requirements of U.S. based regulations. Conversely, however, statements in the Commission's Proposed Guidance indicate that the Commission may also review foreign regulations for substituted compliance on an "individual requirement basis."[15]

In conducting reviews for substituted compliance, we strongly urge the Commission not to apply a strict equivalence standard which, given the necessary differences of law that exist in separate jurisdictions, will likely become unworkable and cumbersome in practice. We believe a regime that places an emphasis on shared principles and mutual recognition is much more likely to result in a global regulatory regime that provides workable standards and that avoids conflicting and unnecessarily complex regulations that will impose considerable costs on the market. Such an approach has the benefit of decreasing debate and conflict between the regulators of different nations. Mutual recognition and standardized principles also allows regulators to leverage the enforcement capabilities of their foreign counterparts by limiting the

[12] Cross-Border Guidance at 41,229.
[13] Cross-Border Guidance at 41,390.
[14] Cross-Border Guidance at 41,233.
[15] Cross-Border Guidance at 41,220.

amount of resources domestic regulators must spend on policing activities that occur in foreign markets.

We urge the Commission to ensure that any final guidance released on its substituted compliance process is in keeping with international efforts that are already in progress. We note that some foreign regulators have already raised concerns regarding the breath of U.S. requirements that may be imposed on foreign dealers.[16] As its stands we believe the thorough review process contemplated by the current Cross-Border review process is both administratively and politically unpalatable. The approach would be greatly improved by encouraging the development of international standards and creating a process for reciprocal recognition of foreign regulations.

We believe that the Proposed Guidance must be revised to enhance its flexibility. We also believe that the Commission's proposal to categorically exclude any transaction-based requirements from possible substituted compliance is misplaced considering the overall tenor of CEA § 2(i), which seeks to limit Title VII's application in foreign markets. While we understand the Commission's interest in ensuring the safety and integrity of the U.S. market, the unilateral imposition of universal rules, especially in the absence of a discussion or analysis on the reliability of any foreign-based swaps regime, seems especially premature and may lead to similar broad pronouncements from other foreign regulators. During this period of intense regulatory change, we strongly urge the Commission to retain the option of allowing substituted compliance in all areas. Overall, we believe that providing for flexibility in these determinations will be a key factor in ensuring the success of a global framework for the regulation of swaps that is consistent with the overall objectives of Title VII.

IV. The Guidance should clarify and limit the scope of non-Title VII requirements on foreign entities.

The guidance contained in the Commission's Cross-Border Guidance is tailored to the new requirements of the CEA as contained in Title VII of the Dodd-Frank Act. We note, however, that the requirements of new Title VII rules often reference pre-existing Commission rules that themselves impose various regulatory requirements. Several of our members are concerned regarding the applicability of such requirements to non-U.S. swap dealers or to U.S. swap dealers that maintain branches, agencies, affiliates, or subsidiaries in foreign markets.

Congruent with our earlier comments, we believe that the Commission should allow for the recognition of foreign requirements on a much more flexible basis than proposed. This recognition should be extended to other aspects of the Commission's regulatory framework that goes beyond the requirements of Title VII. For example, the proposal seems to presume that foreign entities will keep relevant records according to the requirements of Commission Regulation 1.31.[17] We believe, however, that Regulation 1.31 represents a prime example of a

[16] *See* Letter from Patrick Raaflaub, Chief Executive Officer and Mark Branson, Head of Banks Division, Swiss Financial Market Supervisory Authority FINMA to Chairman Gary Gensler, U.S. Commodity Futures Trading Commission (Jul. 5, 2012) ; Letter from Masamichi Kono, Vice Commissioner for International Affairs, Financial Services Agency of Japan and Hideo Hayakawa, Executive Director Bank of Japan to Chairman Gary Gensler, U.S. Commodity Futures Trading Commission (August 13, 2012).

[17] Cross-Border Guidance at 41,233, fn. 127.

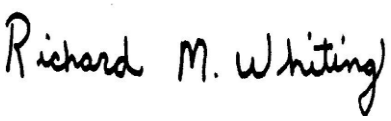
situation where the Commission should either allow compliance by allowing foreign entities to rely on domestically sanctioned regulations or work proactively with foreign regulators to create a mutually recognized memorandum of understanding.

We also believe that the registration requirements in Forms 7-R and 8-R must be carefully tailored to prevent over-inclusion. Under the swap dealer registration framework adopted by the Commission earlier this year, swap dealers have Form 8-R filing obligations in relation to their principals, which include "officers, directors, and persons who own ten percent or more of the outstanding shares of the applicant."[18] Form 7-R requires a representation that no "associated persons" of the registrant are subject to a statutory disqualification. The scope of associated persons includes any person who is involved in the supervision of business personnel. Considering the fact that many foreign registrants will have substantial non-swap dealing operations, we believe that the Commission should clarify in its guidance that these particular registration requirements are limited only to officials in the department or division of a non-U.S. registrant that conducts the entity's swap dealing business with U.S. persons. We believe that this clarification is consistent with the Commission's overall framework to concentrate its oversight on foreign parties that directly face U.S. based persons.

Conclusion

Due to the global nature of the swaps market, the Commission's Cross-Border Guidance will constitute a key component in the implementation and effectiveness of the overall framework envisioned by the 2009 G-20 Agreement with respect to the regulation of over-the-counter derivatives. We appreciate your consideration of our comments regarding this important topic. If you have any questions, please do not hesitate to call me or Richard Foster, the Roundtable's Senior Regulatory Counsel, at (202) 589-2424.

Sincerely,



Richard M. Whiting
Executive Director and General Counsel
Financial Services Roundtable

[18] Registration of Swap Dealers and Major Swap Participants, 77 Fed. Reg. 2613, 2618 (Jan. 19, 2012).