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Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: Cross-Border Security-Based Swap Activities; Re-Proposal of Regulation SBSR and Certain Rules and Forms Relating to the Registration of Security-Based Swap Dealers and Major Security-Based Swap Participants, Release No. 34-69490; File Nos. S7-02-13, S7-34-10 and S7-40-11 (the "Proposal")[1]

Secretary Murphy:

The Institute of International Bankers (the "Institute") welcomes the opportunity to provide comments to the Securities and Exchange Commission (the "Commission") with respect to the Proposal. The topic addressed by the Proposal—the cross-border application of the security-based swap ("SBS") provisions of the Securities Exchange Act of 1934 (the "Exchange Act"), as amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank")[2]—is both highly consequential and complicated. We appreciate the Commission's thoughtful and comprehensive approach to this complex area. In particular, we believe that the Commission has appropriately sought to take into account the greater extent to which the SBS markets are globally interconnected, as well as the role that foreign regulators therefore must play as the primary supervisors of SBS market participants based abroad.

[1] 78 Fed. Reg. 30,968 (May 23, 2013).

[2] Pub. L. 11-203, 124 Stat. 1376 (2010).

In this regard, the Proposal includes elements that are similar to the final cross-border guidance recently adopted by the Commodity Futures Trading Commission (the "CFTC") with respect to its regulation of those aspects of the over-the-counter ("OTC") derivatives markets not regulated by the Commission (the "CFTC Guidance").[3] Both agencies have adopted or proposed to adopt broadly similar distinctions between entity-level and transaction-level requirements. Both also envision a substituted compliance framework under which non-U.S. market participants may comply with Dodd-Frank through compliance with comparable foreign rules. In some respects, the Proposal goes further than the CFTC Guidance in recognizing substituted compliance, such as in the context of transaction-level requirements applicable to cross-border transactions. In this way, the Proposal tracks closely the emerging OTC derivatives regulatory regime in the European Union (the "EU"). Consistency with the EU is especially important given the extent of cross-border activity between U.S. and EU market participants.

There are, however, a number of respects in which the Proposal departs from the CFTC Guidance and a recent consultation by the European Securities and Markets Authority ("ESMA" and such consultation, the "ESMA Consultation").[4] Viewed in isolation, many of the distinguishing features of the Proposal represent sensible policy outcomes. However, as discussed in more detail below, Dodd-Frank's mandates that the Commission consult and coordinate with the CFTC and foreign regulatory authorities weigh in favor of harmonization with respect to cross-border rules. So, too, do cost-benefit considerations.

In light of these considerations, in our view the Commission should generally seek to avoid any divergence from the CFTC's and international regulators' frameworks that is likely to give rise to undue costs or burdens. Rather, divergence is generally warranted only if the rule adopted by the Commission is more flexible than those adopted by others (and therefore would not preclude the voluntary adoption of consistent practices by market participants).

Accordingly, we have recommended modifications to the Proposal that are intended to emphasize consistency across regional regimes for the regulation of cross-border OTC derivatives activity. We believe that these modifications would help to avoid the adverse consequences that would result from the application of inconsistent rules to common markets and market participants, without undermining the Commission's objectives of mitigating risk to the U.S. financial system, promoting market transparency and ensuring protection of home/host country counterparties.

[3] Interpretive Guidance and Policy Statement Regarding Compliance With Certain Swap Regulations, 78 Fed. Reg. 45,292 (July 26, 2013).

[4] Consultation Paper: Draft Regulatory Technical Standards on contracts having a direct, substantial and foreseeable effect within the Union and non-evasion of provisions of EMIR, ESMA/2013/892 (July 17, 2013).

BACKGROUND

When the Commission initially published the Proposal in May 2013, other regulatory authorities had not yet adopted frameworks for the cross-border regulation of OTC derivatives activity. Although CFTC swap rules had begun to take effect on December 31, 2012, the CFTC had not yet provided guidance regarding the cross-border application of those rules. Instead, market participants were eligible for an exemption that largely limited the application of CFTC rules to swaps involving one or more U.S. persons. Likewise, requirements under the European Market Infrastructure Regulation ("EMIR")[5] were only just starting to come into effect, and ESMA had not yet issued a consultation regarding the cross-border application of EMIR.

The intervening finalization of the CFTC Guidance, the proposed ESMA framework and the framework understanding among international regulators introduces substantial new points of reference for evaluating the Proposal, given the strong policy and statutory mandates in favor of harmonization. As the Commission has recognized, despite the split in agency jurisdiction under Dodd-Frank between swaps and SBS, most registrants and market participants subject to Commission regulation will also be subject to CFTC regulation because they conduct business involving both SBS and swaps, often using the same technology platforms, personnel and documentation. Generally, applying two inconsistent sets of rules to market participants trading in similar products could be extremely costly. Such costs, as well as accompanying business and market disruptions resulting from duplicative or potentially conflicting requirements, would be magnified in the case of the Proposal because a substantial majority of the CFTC's substantive rules are already in effect. Dual registrants, in particular, would be disadvantaged.

The ESMA Consultation, in turn, suggests that the EU may well adopt an approach that is very similar to that embodied in the CFTC Guidance. Because CFTC and EU cross-border rules appear to be converging, rulemaking by the Commission that is inconsistent with the CFTC Guidance may well lead to conflicts with EU rules. For market participants that operate in both the U.S. and the EU, this additional conflict would result in substantial additional costs. Such market participants would face severe competitive disadvantages relative to those operating solely domestically or abroad.

Convergence by the Commission with the CFTC Guidance will in many cases promote efficiency and competition, consistent with the cost-benefit mandate embodied in Sections 3(f) and 23(a)(2) of the Exchange Act. In some other cases, divergence may not necessarily result in inefficient consequences, such as cases where the Commission's approach is more flexible.

[5] Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties (CCPs) and trade repositories (TRs).

In addition, Section 712 of Dodd-Frank requires the Commission to consult and coordinate with the CFTC to ensure "regulatory consistency and comparability, to the extent possible." Convergence with the EU, likewise, would be consistent with the Congressional mandate in Section 752 that the Commission consult and coordinate with foreign regulatory authorities on the "establishment of consistent international standards" with respect to the regulation of swaps and SBS. Both of these considerations were cited by the Commission as guiding principles behind its approach to the cross-border application of Title VII.[6]

Finally, we do not believe that differences in the wording of Section 30(c) of the Exchange Act, on the one hand, and the wording of Section 2(i) of the Commodity Exchange Act (the "CEA"), on the other, require that the two agencies adopt fundamentally different approaches to the extraterritorial application of Title VII.[7] Indeed, Congress' express mandate in Section 712 of Dodd-Frank that the Commission consult and coordinate with the CFTC and the prudential regulators for the purposes of assuring regulatory consistency and comparability clearly indicates the opposite Congressional objective.

DISCUSSION

I. Cross-Border Scope Generally

Under the Proposal, whether a Commission requirement would apply to an SBS transaction would generally depend on whether (a) one or both parties to the transaction is (i) a U.S. person (other than a foreign branch), (ii) has its performance under the SBS guaranteed by a U.S. person or (iii) is a foreign SBS dealer ("SBSD") or (b) the transaction is conducted within the U.S. Accordingly, because these concepts transcend the discussion of any particular requirement, we first discuss our comments with respect to the Proposal's "U.S. person" definition and its application of Commission requirements to transactions conducted within the U.S.

A. "U.S. Person" Definition

Under the Proposal, the term "U.S. person" would mean:

(A) any natural person resident in the United States;

[6] See Proposal at 30,987.

[7] Specifically, Section 2(i) of the CEA addresses two classic bases for U.S. jurisdiction—conduct (embodied in Section 2(i)'s references to the location of "activities") and effects (embodied in Section 2(i)'s reference to a "direct and significant . . . effect on" U.S. commerce). Section 30(c) of the Exchange Act, in turn, is less precise in specifying the bases for Commission jurisdiction, but rather confirms that Title VII of Dodd-Frank does not apply to a person transacting a business in SBS "without the jurisdiction" of the U.S.

(B) any partnership, corporation, trust, or other legal person organized or incorporated under the laws of the United States or having its principal place of business in the United States; and

(C) any account (whether discretionary or non-discretionary) of a U.S. person.

The term "U.S. person" would not include the International Monetary Fund, the International Bank for Reconstruction and Development, the Inter-American Development Bank, the Asian Development Bank, the African Development Bank, the United Nations, and their agencies and pension plans, and any other similar international organizations, their agencies and pension plans.[8]

We generally believe that the Commission's proposed U.S. person definition represents a sensible approach to jurisdictional scope that is consistent with longstanding territorial principles. In particular, focusing on an entity's jurisdiction of incorporation and principal place of business appropriately limits application of the Commission's rules, and will help to avoid conflicting assessments of jurisdictional status. We also support the exclusion of international organizations from U.S. person status, which is generally consistent with the CFTC Guidance and well-established principles of international law.[9]

Accordingly, our comments on the U.S. person definition focus on certain technical and practical considerations with respect to the principal place of business test. While the other prongs of the definition may be relatively simple to apply, market participants are likely to have difficulty implementing the "principal place of business" test without additional Commission guidance. We therefore believe that it would be helpful for the Commission to provide further interpretive guidance on this prong when it adopts its final rules.

1. Operating Companies

Many operating companies that participate in the SBS markets have global businesses, with management, business lines, and significant numbers of personnel located in multiple jurisdictions worldwide. The "principal" center of business for such a company may not be obvious to its counterparties. Therefore, the Commission should clarify that an operating

[8] Proposed Rule 3a71-3(a)(7).

[9] As a general matter, the Commission should confirm that a counterparty representation would be sufficient to fulfill a person's diligence requirements under Commission rules, absent knowledge of facts that would cause a reasonable person to question the accuracy of the representation. Additionally, because the CFTC's U.S. person definition is broader than the Commission's proposed definition and includes all three prongs of the Commission's proposed definition, the Commission should also confirm that market participants may reasonably rely on a representation regarding a counterparty's U.S. person (or non-U.S. person) status under the CFTC Guidance for purposes of establishing such status under the Commission's rules.

company's principal place of business is considered to be the location of its headquarters (i.e., where the company's most senior management are physically located) and that a given company may only have one principal place of business.[10]

2. Funds

As the Commission is aware, the principal place of business of a fund can be less clear. While a fund's jurisdiction of organization is clearly and objectively determinable, its principal place of business may not be apparent because, unlike operating companies, the fund itself usually does not have employees, business lines, or a physical presence. We recommend that the Commission provide further guidance to enable market participants to reach rational, consistent U.S. person determinations for funds.

In our view, a fund's principal place of business should be the location of the person responsible for the fund's operational management, i.e., the location of the person responsible for establishing the fund and selecting its investment manager, brokers, and underwriter/placement agent. The locus of these operational management activities is the appropriate location to designate as the fund's principal place of business. Investment management activities, on the other hand, may take place in a different location and, often, multiple locations, depending on the investment strategies of the fund. We therefore recommend that the Commission clarify that a fund's principal place of business is the location from which the person responsible for its operational management activities, rather than investment management activities, conducts those activities.

B. Conduct Within the U.S.

Under the Proposal, an SBS transaction between a foreign SBSD and a non-U.S. counterparty, neither of which has its performance under the SBS guaranteed by a U.S. person, would nevertheless be subject to the following requirements if the transaction was "conducted within the" U.S. by *either* party:[11] (i) SBSD registration; (ii) external business conduct standards;

[10] We also recommend that the Commission provide workable criteria for a person to determine its counterparty's status with respect to the principal place of business prong, in the absence of a representation. If the counterparty is a public company, a market participant should be permitted to infer the company's principal place of business from information contained in the company's public securities filings. For a private company, the counterparty should be permitted to determine the company's principal place of business based on the location from which the company is doing business with the counterparty, unless the counterparty is in possession of information regarding the location of the company's headquarters.

[11] A transaction would be considered to be "conducted within the" U.S. if it is solicited, negotiated, executed or booked within the U.S. by or on behalf of either counterparty, unless the transaction is conducted through a foreign branch. Proposed Rule 3a71-3(a)(5). The determination of whether a transaction is "conducted through a foreign branch," in turn, would require that the transaction not be solicited, negotiated or executed by a person within the U.S. by or on behalf of the foreign branch or its counterparty. Proposed Rule 3a71-3(a)(4). We refer to the application of Commission requirements based on these considerations as a "conduct test."

(iii) mandatory clearing; (iv) mandatory trade execution; (v) regulatory reporting of SBS data; and (vi) public dissemination of SBS data.[12] In addition, if *both* parties conducted the transaction within the U.S., then their eligibility for substituted compliance would be limited.[13]

As noted in the Proposal, it is common for non-U.S. persons (including foreign SBSDs) to utilize U.S. agents for the execution of SBS because of their agents' expertise in the relevant market (such as in the case of an SBS with a U.S. underlier) or because of logistical matters (such as the time zones in which the parties conduct business). Such agents generally include U.S. affiliates and branches of foreign SBSDs and their employees.[14] They also include third-party brokers and investment managers acting for foreign clients.

We believe that applying the Commission requirements noted above to non-U.S. persons on the basis of conduct within the U.S. by their U.S. agents would create serious operational, legal and economic difficulties for foreign SBS market participants. We first note general consequences below, and then describe a number of specific shortcomings of the conduct test as proposed.

1. Adverse consequences of a territorial conduct test

The derivatives markets are international by nature, and globally active SBSDs may effect solicitation, negotiation and execution activities through offices and personnel located in many different jurisdictions. This is particularly true given that the speed and scope of derivatives activities increasingly incorporate and rely on electronic systems and processes that link activity within a global firm and make physical location of persons involved in these processes unknown or irrelevant. In this context, the proposed conduct test will create very substantial and unwarranted burdens on firms who would be required to isolate and measure involvement of personnel in U.S. locations. We note the following consequences:

[12] See Proposed Rules 3a71-3(b) (SBSD registration), 3a71-3(c) (external business conduct standards), 3Ca-3 (mandatory clearing), 3Ch-1 (mandatory trade execution), 908(a)(1) (regulatory reporting of SBS data) and Rule 908(a)(3) (public dissemination of SBS data).

[13] Specifically, the parties would not be eligible for substituted compliance with respect to SBSD registration, mandatory trade execution, regulatory reporting of SBS data or public dissemination of SBS data.

[14] In this regard, we note that the definition of the term "bank" in Section 3(a)(6) of the Exchange Act, which governs the application of broker-dealer registration requirements to foreign banks with a U.S. branch, distinguishes between the U.S. and non-U.S. branches of a foreign bank. The definition of "bank" contained in Section 202(a)(2) of the Investment Advisers Act of 1940 uses similar language. Therefore, we would consider the U.S. branch of a foreign bank to be an agent of the foreign bank for purposes of an SBS transaction solicited, negotiated or executed by U.S. branch personnel on behalf of the bank's head office or another foreign branch.

- From an operational perspective, the introduction of a conduct test would create serious burdens that may in some cases be impossible to overcome. Currently, market participants do not capture data regarding the location of agents acting on their behalf that may be involved in negotiation, execution or other activities with respect to SBS transactions. Building operational systems to accurately capture this information would be extremely difficult, if not impossible. Because conduct is necessarily measured on a trade-by-trade basis, such a system would need to have the ability to flag activity and communications (e.g., conference calls, email chains, etc.) that may involve a person located in the U.S. As the Commission is aware, the creation of systems of this kind is a cost-intensive process subject to technological limitations and the risk of inaccuracy caused by human error.

- Because the conduct test would be triggered by activity of either counterparty, each market participant would need to know where its counterparty was conducting activity in order to accurately apply regulatory requirements. However, as noted above, the conduct test would necessarily be applied on a trade-by-trade basis, such that representations in relationship documentation may not provide an appropriate means of providing the required information. For market participants involved in numerous cross-border transactions, it would be disruptive and costly to attempt to determine the location of conduct for each individual SBS or even to attempt to obtain transaction-by-transaction representations as to the location of such conduct. Since many SBS transactions are conducted through electronic, automated systems, there may be no meaningful way to capture or provide this information. Incorporation of a conduct test into electronic trade systems would, at the least, require significant coordinated industry effort with concomitant costs.

- Because the CFTC Guidance does not generally set forth a conduct test, foreign SBSDs that are dually registered with the CFTC would incur significant costs and burdens as a result of a need to modify their existing Dodd-Frank systems, policies, procedures and controls to comply with two very different tests for whether Dodd-Frank applies to their activities.

- U.S. brokers and investment managers would be placed at a competitive disadvantage to foreign brokers and investment managers because foreign clients would be reluctant to subject their SBS activities to Commission requirements, in addition to local requirements, solely by virtue of using a U.S. broker or investment manager. In addition, personnel based in the U.S. could be encouraged to relocate elsewhere, and substantial U.S.-related trading activity could consequently migrate offshore. These actions would result in a loss of jobs and tax revenues for the broader U.S. economy.

- The application of U.S. mandatory clearing, mandatory trading, regulatory reporting and public dissemination requirements to SBS transactions between non-U.S. persons conducted within the U.S. through U.S. agents is likely to lead to conflicts with or duplication of foreign requirements applicable to such transactions. For example, under the ESMA Consultation, EMIR would apply to transactions between the U.S. branches of two entities established in the EU. As a result, two EU-based firms transacting with each other through their U.S. branches would be subject to both Dodd-Frank and EMIR at the same time. Under neither the ESMA Consultation nor the Proposal would the parties generally be eligible for substituted compliance or similar relief for such transactions. This is a prime example of the sort of "conflicting or duplicative" requirements that the Commission has otherwise sought to avoid with the Proposal.[15] Indeed, it should be expected that most jurisdictions would seek to apply their rules to transactions between two of their own domiciled persons, despite some of the activity being conducted abroad, for purposes of addressing systemic risk and customer protection concerns. For example, the Commission's own Proposal would apply all of its U.S. requirements to SBS transactions between two U.S. persons, even if some negotiation or execution activity took place in a foreign jurisdiction.

- We are particularly concerned that foreign rules will require non-U.S. persons to utilize clearing houses, execution platforms and trade repositories located or regulated abroad. For instance, an SBSD based in the EU that trades with U.S.-based asset managers representing their foreign clients through the SBSD's New York-based broker-dealer affiliate would likely be subject to EMIR's clearing and regulatory reporting requirements. In the future, it may also be subject to trading and public dissemination requirements under the Markets in Financial Instruments Regulation ("MiFIR").

2. Specific shortcomings of the territorial conduct test

Aside from these overall concerns, we note a number of more specific considerations.

- The conduct test gives no guidance as to the scope or degree of solicitation, negotiation or execution activity that would satisfy the test. Many transactions for which solicitation, negotiation or execution primarily occurs outside the United States might conceivably be brought within the test by a single phone call or electronic system including or involving U.S.-based

[15] See Proposal at 30,975.

personnel. In the context of electronically executed transactions involving foreign branches of U.S. swap dealers ("SDs") and major swap participants ("MSPs"), the CFTC has adopted clarifying guidance that U.S. conduct only occurs where a party's personnel managing the electronic execution are located within the U.S.[16] Similarly, the test as proposed could be read to suggest that even the involvement of personnel performing only clerical or ministerial functions within the U.S. could be considered conduct within the U.S. Again, the CFTC has given clarifying guidance in this respect.[17]

- The conduct test as proposed does not recognize the effect of existing regulation of the relevant agents. A person located within the U.S. that conducts brokerage activity in SBS on behalf of a non-U.S. person will be subject to registration with, and regulation by, the Commission as a broker-dealer, unless an independent exception or exemption applies. Similarly, a person located within the U.S. that provides investment advice with respect to SBS to a non-U.S. person will be subject to registration with, and regulation by, the Commission as an investment adviser, unless an independent exception or exemption applies. We believe that such direct regulation of U.S. agents should address most of the market integrity and customer protection objectives to be served by SBSD registration, as well as the external business conduct standards.[18] Accordingly, it would be duplicative and unnecessary for a conduct test to extend to U.S. agents that are duly registered with the Commission or exempted or excluded from such registration.[19]

- The conduct test would cover SBS "negotiated" within the U.S, but provides no guidance as to the scope of negotiation that would satisfy the test. As the Commission is aware, SBS trading relationships may involve a number of documents, including master agreements and schedules, netting agreements,

[16] See CFTC Guidance at 45,350.

[17] See id.

[18] See Letter re: Transactions in Foreign Securities by Foreign Brokers or Dealers with Accounts of Certain Foreign Persons Managed or Advised by U.S. Resident Fiduciaries from Catherine McGuire, Chief Counsel, Division of Market Regulation to Giovanni P. Prezioso, Cleary, Gottlieb, Steen & Hamilton, dated January 30, 1996.

[19] The Commission has recognized such principles in the exemption from broker-dealer registration contained in Rule 15a-6(a)(3), as well as Commission staff no-action relief from broker-dealer registration for foreign brokers or dealers trading with U.S.-resident fiduciaries. To the extent that the Commission believes that SBS-specific protections are warranted in connection with activities conducted by U.S. agents with non-U.S. persons, then the Commission could address those considerations in the context of rulemakings pertaining to its regulation of such agents.

> credit support annexes, and confirmations. Typically, only the confirmation or similar agreement relates to a particular transaction, while other documents govern the trading relationship generally. The test as proposed could be read to suggest that negotiation of relationship documentation or other ancillary documents could be considered conduct within the U.S.

While we appreciate that the Commission has adopted a territorial approach to securities regulation in the past, securities transactions and SBS are different markets with different market participants, purposes and characteristics. Importantly, the cash securities markets are generally regionalized, such that a territorial approach based on conduct is both more appropriate and less complex from an operational perspective. However, the derivatives markets are highly interconnected on a global scale, with a substantial portion of the market represented by transactions spanning across multiple jurisdictions. This cross-border activity is not limited to a single undertaking or arrangement, such as an offshore distribution of securities, where the Commission has applied a territorial approach in the past. Transactional activity that potentially involves multiple physical locations is a day by day or even minute by minute feature of the international derivatives market. In this context, a status-based test for jurisdictional application is the most sensible approach to regulation, as a territorial approach based on the location of conduct is both less relevant and significantly more difficult to implement.

Accordingly, we strongly recommend that the Commission modify its proposal to remove the conduct test with respect to the application of the requirements described above, and instead consistently apply its rules based on the U.S. person status of the counterparties to an SBS transaction. To the extent that the Commission believes that SBS-specific protections are warranted in connection with activities conducted by U.S. agents with non-U.S. persons, then the Commission should address those considerations in the context of rulemakings pertaining to its regulation of such agents.

II. SBSD and MSBSP Registration Requirements

In addition to the "U.S. person" definition and the conduct test, which we discuss in Part I above, the Proposal's SBSD and major SBS participant ("MSBSP") registration rules also address (a) the treatment of transactions with the foreign branches of U.S. banks, (b) the treatment of inter-affiliate transactions, (c) cleared transactions executed anonymously on an SBS exchange or SBS execution facility ("SBSEF") and (d) aggregation under the SBSD de minimis exception.

A. Transactions Conducted Through Foreign Branches

Under the Proposal, a non-U.S. person may exclude from its SBSD de minimis calculation transactions that it enters into with the foreign branch of a U.S. bank. We strongly support this exception. Not only is it consistent with the CFTC Guidance,[20] but it is also critical in order to permit non-U.S. persons to access the liquidity provided by foreign branches, which are often significant participants in local foreign markets. The exception also is necessary to permit U.S. banks to compete in, and to hedge exposures through trades in, foreign markets.

With respect to MSBSP registration, the Proposal would require a non-U.S. person to include its transactions with U.S. persons, including transactions with the foreign branches of U.S. banks, other than inter-affiliate SBS with majority-owned affiliates.[21] Non-U.S. persons would also be required to include SBS transactions of U.S. persons that it guarantees, as well as SBS transactions with U.S. persons by non-U.S. persons that it guarantees, other than guarantees of a person subject to capital requirements imposed by the Commission, the CFTC, a U.S. banking regulator or a foreign regulator consistent with the Basel Accord of the Basel Committee on Banking Supervision.[22]

The Institute generally agrees with the Commission's approach to MSBSP registration. However, we note that the requirement that a non-U.S. person include transactions with the foreign branches of U.S. banks for registration purposes is inconsistent with both the Commission's proposed SBSD registration rules and the CFTC Guidance applicable to MSP registration.

We believe that the same rationale applicable to SBSD registration applies equally in the MSBSP context. While we recognize that the MSBSP registration category is intended to address risk to the U.S. financial system in a way that the SBSD category is not, we recommend that the Commission recognize, as the CFTC has, that there are other means for addressing such risk. Specifically, the CFTC was persuaded that clearing or variation margining of transactions between a foreign branch and a non-U.S. financial entity provided sufficient mitigation of risk so as to warrant an exception from the requirement that the non-U.S. financial entity count exposures arising from such transactions in computing its MSP status.[23] The CFTC also was persuaded that non-U.S., non-financial entities present more modest risk to the U.S., and therefore should not be required to count exposures arising from their transactions with foreign branches in computing their MSP status.[24] If, on the other hand, non-U.S. counterparties to the foreign branches of U.S. banks were required to include such transactions in their computation of MSP (or MSBSP) status, many such counterparties would cease transacting with

[20] See CFTC Guidance at 45,326.

[21] Proposal at 31,206.

[22] Id. at 31,033.

[23] See CFTC Guidance at 45,324-25.

[24] Id.

such foreign branches. We therefore recommend that the Commission adopt similar exceptions from its MSBSP calculations.

B. Inter-Affiliate Transactions

We support the Commission's proposal not to include inter-affiliate transactions for purposes of calculating the de minimis level of SBS dealing activity required for SBSD registration.[25] Inter-affiliate SBS serve very different functions from dealing activity with third parties and do not present similar risks to the U.S. financial markets or to customers. We therefore agree with the Commission that such transactions are not relevant for registration purposes.

C. Cleared, Anonymous Transactions on an SBS Exchange or SBSEF

As part of the CFTC Guidance, the CFTC adopted an exception from SD registration and transaction-level requirements for swaps that are (1) executed anonymously on a registered swap execution facility, designated contract market or foreign board of trade and (2) cleared.[26] In adopting these exceptions, the CFTC noted the practical difficulty in determining a counterparty's identity in the case of an anonymously executed transaction—an issue that was recognized by Congress in the statutory provisions governing business conduct standards—and the fact that most transaction-level requirements are already satisfied implicitly in the case of a transaction executed on a regulated platform and cleared.[27]

In our view, similar considerations warrant an exception from Commission requirements, too. In particular, SBS markets based outside the U.S. may wish to admit as participants, or permit their participants to provide direct access to, U.S. persons. As a result, a non-U.S. person trading on such a market could execute SBS transactions with U.S. persons and thus, under the Proposal, become subject to registration as an SBSD with the Commission. The possibility of becoming subject to SBSD registration could deter many unregistered non-U.S. liquidity providers from participating on SBS markets that provide access to U.S. persons. Foreign SBS markets may, in turn, be reluctant to provide access to U.S. persons.

At the same time, the Commission's interest in regulating liquidity providers on foreign SBS markets is relatively low. As a non-U.S. person, the risk arising from such person's conduct would be of concern to, and subject to regulation by, its home country regulator. In addition, systemic risk and safety and soundness considerations arising from the activity

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[25] Proposal at 31,006.

[26] See CFTC Guidance at 45,325; 45,352 and 45,360.

[27] See id.

conducted by such persons would already be addressed by Commission regulation of the SBS clearing agency ("SBSCA") through which such a person would clear. Market transparency and counterparty protection considerations, in turn, would already be addressed by Commission regulation of the SBS exchange or SBSEF on which the transaction is executed.

Accordingly, we recommend that the Commission adopt an exception from SBSD registration for an SBS transaction entered into by a non-U.S. person on an anonymous basis on a registered or exempt foreign SBS exchange or SBSEF and cleared through a registered or exempt SBSCA.

D. Aggregation under the De Minimis Exception

We support the Commission's proposal to exclude registered SBSD affiliates from aggregation requirements for affiliated groups under the SBSD de minimis exception.[28] Like the aggregation rule under the CFTC Guidance, which contains a similar exception,[29] this rule balances the Commission's goal of regulating the most significant SBS dealing activity within a corporate group, while allowing market participants the flexibility to structure certain dealing activities through other affiliates under the de minimis threshold.

A significant point of divergence from the CFTC Guidance, however, is the Commission's proposal that a registered SBSD affiliate be "operationally independent" of the registrant in order to qualify for the exclusion. For efficiency reasons, many corporate groups use centralized back office operations, risk management units and, in some cases, sales and trading personnel. This is particularly the case for groups subject to consolidated supervision, since consolidated supervisors require group-wide management of risk. Entities may also need to utilize common sales and trading personnel and systems for particular types of transactions for which market expertise is not widespread throughout the group. Preventing the sharing of such resources or group-wide risk management would effectively eliminate the exclusion for registered SBSDs.[30]

The aggregation rule already satisfies the Commission's anti-evasion concerns because only de minimis levels of dealing, in the aggregate, could occur outside of a group's registered entities. If it wished, the Commission could also clarify that personnel of an SBSD

[28] Proposed Rule 3a71-4.

[29] CFTC Guidance at 45,323.

[30] Again, in its application of Rule 15a-6 under the Exchange Act, the Commission has viewed foreign broker-dealers as separate from their U.S. affiliates for purposes of registration requirements, without requiring that the foreign broker-dealer be "operationally independent" of such U.S. affiliates.

may not "book" transactions to an unregistered affiliate for the purpose of evading or avoiding the application of requirements applicable to an SBSD (e.g., business conduct requirements).

For the foregoing reasons, we recommend that the Commission eliminate the "operationally independent" condition to the aggregation exception for registered SBSDs in favor of an approach that looks to whether the affiliate is being used as a booking vehicle for purposes of avoiding Commission SBS requirements.

III. Title VII Requirements Applicable to SBSDs

The Proposal would categorize the following requirements applicable to SBSDs and MSBSPs as "entity-level" requirements: capital, margin, risk management, recordkeeping, internal systems and controls, diligent supervision, conflicts of interest, chief compliance officer, inspection and examination, and licensing requirements and statutory disqualification. The Proposal also would categorize external business conduct standards and segregation requirements as "transaction-level" requirements.

Under the Proposal, a foreign SBSD would generally be eligible for substituted compliance with respect to entity-level requirements and external business conduct standards.[31] In addition, a foreign SBSD would not be subject to external business conduct standards with respect to its SBS transactions with non-U.S. persons conducted outside the U.S.[32] The application of segregation requirements to a foreign SBSD would differ as between cleared and uncleared SBS, as well as between broker-dealer and non-broker-dealer SBSDs; generally speaking, however, foreign SBSDs that are foreign banks with a U.S. branch or agency would not be subject to segregation requirements with respect to assets received from non-U.S. persons.[33]

We support the Commission's overall proposal to distinguish between entity-level and transaction-level requirements, as well as its proposal to permit a foreign SBSD to comply with U.S. requirements through substituted compliance with comparable foreign requirements. Accordingly, our comments focus on eligibility for substituted compliance, as well as the categorization of particular requirements as either entity-level or transaction-level.[34]

[31] See Proposed Rule 3a71-5.

[32] See Proposed Rule 3a-71-3(c).

[33] See Proposed Rule 18a-4(e).

[34] We discuss the application of certain requirements based on conduct within the U.S. in Part I.B above.

A. <u>Capital Requirements</u>

In discussing the eligibility of foreign SBSDs for substituted compliance with respect to capital requirements, the Proposal focuses on the Commission's proposal to subject nonbank SBSDs to a "net liquid assets test" similar to the broker-dealer net capital rule.[35] It goes on to note that, accordingly, the substituted compliance analysis for a foreign, nonbank SBSD would focus on whether the SBSD's home country capital rules permit it to hold more illiquid assets as regulatory capital than would Commission rules and, if so, whether the SBSD has access to sufficient liquidity to support the liabilities it might incur as a result of its business activity.[36] Finally, the Commission would also consider the impact of any reduced liquidity associated with the application of foreign capital standards on the ability of the nonbank SBSD to wind down operations quickly and distribute assets to customers.[37]

We are concerned that the considerations described above could, if weighted too heavily, lead the Commission to conclude that Basel-compliant foreign capital requirements would not be a sufficient basis on which to grant substituted compliance. We do not believe that such a determination would be warranted under the statute. It is clear under Title VII that Congress intended that foreign bank SDs and SBSDs would be subject to home country capital standards that are deemed by the Board of Governors of the Federal Reserve System to be comparable to the capital required in the case of a similarly situated U.S. banking organization. This is the approach that has been followed by the prudential regulators in their proposed capital rules for SDs and SBSDs.[38] We do not believe that the Proposal demonstrates that the differences between bank and nonbank SBSDs' funding models creates risks that are not captured by Basel-compliant capital requirements.

The Basel standards represent the international consensus on robust capital requirements for financial institutions. Their application to SBSDs is fully consistent with Dodd-Frank, as evidenced by Congress' deference to existing bank capital rules for bank SBSDs. It is also important for the Commission to have due regard for the regulatory structure of other jurisdictions—many of which do not have functional regulators like the U.S.— as well as applicable insolvency law and rules governing access to central bank liquidity.

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[35] Proposal at 31,090. Capital requirements for bank SBSDs are subject to the exclusive jurisdiction of the prudential regulators.

[36] <u>Id.</u>

[37] <u>Id.</u>

[38] <u>See</u> 76 Fed. Reg. 27,564, 27,582 (May 11, 2011).

Additionally, the Commission's net liquid assets test is generally an outlier relative to capital standards applicable to nonbank financial institutions in other jurisdictions, many of which apply Basel-based capital standards to bank and nonbank institutions alike. Consequently, a general rejection by the Commission of foreign, Basel-compliant capital standards would amount to a broad-based application of Commission capital requirements abroad. Most foreign, nonbank SBSDs would find simultaneous compliance with Commission and home country requirements practically impossible, and therefore could be compelled to withdraw from the U.S. market. The drain on Commission staff resources entailed by oversight of idiosyncratic capital requirements abroad would also be considerable.

Accordingly, we recommend that the Commission operate from a presumption that a foreign SBSD subject to Basel-compliant home country capital requirements will be eligible for substituted compliance with respect to capital requirements, absent extenuating circumstances that suggest that the relevant foreign supervisor's administration of those requirements is not consistent with international standards.

B. Margin Requirements

Under the Proposal, margin requirements would be categorized as entity-level requirements.[39] We appreciate the Commission's desire to treat margin and capital as part of an integrated financial safety and soundness regime. We further recognize the Commission's perspective that margin requirements address registrant safety and soundness concerns. Nonetheless, we believe that the divergence between the Commission's approach and that adopted by the CFTC and envisioned by EMIR with respect to margin requirements would render the Commission's proposed categorization impracticable. Absent substantive harmonization of international margin standards, the proposed categorization could also lead to significant competitive distortions.

Under the CFTC Guidance, margin requirements are categorized as transaction-level requirements and their application therefore depends on the characteristics of the particular counterparties to a swap.[40] Likewise, under EMIR, margin requirements would be a component of risk mitigation requirements that are applicable on a counterparty-by-counterparty basis.

Divergence by the Commission from this categorization could result in a non-U.S. SBSD being subject solely to home country requirements in relation to its swap transactions with non-U.S. persons, but subject to both Commission and home country requirements in relation to its SBS transactions with non-U.S. persons. Consequently, the non-U.S. SBSD would need to

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[39] Id. Like capital, the Commission is responsible for margin requirements for nonbank SBSDs, while the prudential regulators have exclusive jurisdiction over bank SBSDs.

[40] See CFTC Guidance at 41,226.

negotiate and execute separate credit support documentation, make separate margin calculations and have separate operational procedures across its swap and SBS transactions. Such disparate and duplicative documentation and operational systems would be extremely cost-intensive for non-U.S. SBSDs. Moreover, for its SBS transactions, the non-U.S. SBSD would need to reconcile potentially conflicting U.S. and home country requirements, which under certain scenarios may not even be possible.

The application of conflicting requirements would be especially problematic in those jurisdictions, such as the EU, that require a full two-way exchange of collateral between the parties; it is unclear how the Commission would envision its margin requirements applying to a trade between non-U.S. persons in such a jurisdiction. Of course, each of these issues would present competitive disadvantages for foreign SBSDs registered with the Commission vis-à-vis those that are not. This dynamic would create a strong disincentive to registration with the Commission.

C. Risk Management, Recordkeeping and Reporting, Internal Systems and Controls, Diligent Supervision, Conflicts of Interest and Chief Compliance Officer Requirements

The Proposal indicates that the Commission expects to evaluate substituted compliance across entire groups of related requirements (e.g., capital, together with risk management, general recordkeeping and reporting, and diligent supervision).[41] We agree with the Commission that requirements related to internal controls (such as risk management, recordkeeping and reporting, internal systems and controls, diligent supervision and chief compliance officer requirements) should generally be evaluated holistically. These requirements are commonly overseen and administered by a single prudential supervisor.

While the CFTC has determined to evaluate chief compliance officer, risk management,[42] and swap data recordkeeping requirements separately, it appears to have done so because many foreign jurisdictions have been implementing OTC derivatives reforms in an incremental manner, thus raising timing inconsistencies with the CFTC's requirements.[43] We believe that this consideration is less likely to be relevant for the Commission because it has more closely synchronized the timing of its implementation of Title VII with the implementation of reforms in major foreign jurisdictions.

[41] Proposal at 31,088.

[42] Under the CFTC Guidance, the "risk management" category covers risk management, position limits monitoring, conflicts of interest, and business continuity and disaster recovery requirements. CFTC Guidance at 45,365.

[43] See id. at 45,343.

D. <u>Inspection and Examination Requirements</u>

We agree with the Commission's assessment that inspection and examination requirements should be categorized as entity-level requirements, as these requirements relate to the comprehensive oversight of the Commission's registrants. Certainly, registered SBSDs can and should be obligated to keep their books and records open to inspection and examination of the Commission, to the extent that they are able to do so under applicable law.

However, the Proposal would impose certain standards on registrants that would be impossible for many foreign market participants to satisfy. Under the Proposal, a foreign registered SBSD would be required to certify that it can, as a matter of law, provide the Commission with prompt access to its books and records and submit to onsite inspection and examination. Registrants would also be required to provide an opinion of counsel concurring with this certification.[44] As the Commission is aware, a number of foreign jurisdictions—including jurisdictions in which many potential SBSD registrants are based or operate—have strict blocking, secrecy and privacy laws.[45] Given the relatively severe penalties for violation of these laws, including substantial fines and possible imprisonment in some cases, many non-U.S. potential registrants would find it impossible to register as SBSDs with the Commission.[46]

In the absence of relief from the Commission's certification and opinion of counsel requirements, we expect that some significant foreign participants in the SBS markets would be forced to restructure or cease their activities in order to avoid registration. This process would be extremely costly and would likely cause widespread market disruption, in addition to introducing competitive disparities with respect to market access. We therefore believe that the Commission should modify its rules to remove the requirement that foreign SBSDs provide a certification and opinion of counsel with respect to inspection and examination rights.

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[44] Proposal at 31,015.

[45] For example, Article 271 of the Swiss Penal Code prohibits disclosure of a wide range of data to a foreign state or its representatives without the authorization of the appropriate Swiss authority. Penalties for violations of Swiss privacy law include fines of up to CHF 1,080,000 and, for natural persons, imprisonment of up to three years. Other relevant provisions of Swiss law include: (i) Article 28 of the Swiss Civil Code; Article 47 of the Federal Act on Banks and Saving Institutions of 8 November 1934; (iii) Article 43 of the Federal Act on Stock Exchanges and Securities Trading of 24 March 1995; and (iv) Article 4, para. 3, Swiss Federal Act on Data Protection and the Ordinance to the Federal Act on Data Protection. <u>See also</u>, <u>e.g.</u>, French Code monétaire et financier for credit institutions, Article L. 511-33 *et seq.*; French Code monétaire et financier for investment firms, Article L. 531-12 *et seq.* (disclosure prohibitions under French law, including fines up to €75,000 and possible imprisonment); Korean Financial Real Name Transaction and Secrecy Protection Act, Articles 3 and 4.1 (disclosure restrictions under Korean law, including fines up to 100 million Korean won and possible imprisonment).

[46] Foreign blocking, secrecy and privacy laws have already led to significant conflicts for CFTC registrants in the context of CFTC reporting obligations. <u>See</u> CFTC No-Action Letter No. 13-41 (Jun. 28, 2013).

E. Licensing Requirements and Statutory Disqualification

Under the Proposal, statutory disqualification requirements would be categorized as entity-level and therefore apply to a foreign registered SBSD as a whole, without regard to the identity of a given counterparty.[47] The practical result of this categorization is that non-U.S. employees of non-U.S. SBSDS who do not interact with U.S. customers at all would still be required to submit to U.S. background checks for statutory disqualification purposes.

This approach diverges from that adopted by the CFTC, which does not apply its statutory disqualification requirements to associated persons of its registrants who engage in activity outside the U.S. and limit such activity to customers located outside the U.S.[48] It is also inconsistent with the Commission's own treatment of foreign associated persons of foreign broker-dealers under Rule 15a-6.[49]

Categorization of statutory disqualification as a transaction-level requirement, on the other hand, would limit its application to foreign associated persons conducting activity with U.S. person counterparties. In addition to being consistent with the CFTC's rules and the Commission's rules for broker-dealers, such an approach would preserve the Commission's resources to better serve customer protection interests within the U.S. The Commission's interests in protecting foreign customers are limited, while foreign regulators naturally have a strong interest in regulating such activity. Moreover, properly limiting background checks to personnel interacting with U.S. persons would help eliminate potential conflicts with local privacy laws, which in some cases prohibit background checks for employees based abroad. For these reasons, we recommend that the Commission re-categorize licensing and statutory disqualification requirements as transaction-level requirements.

F. Segregation Requirements

Under the Proposal, the Commission would apply segregation requirements differently as between cleared SBS and uncleared SBS, as well as between a foreign SBSD that is also registered with the Commission as a broker-dealer and one that is not:

- For cleared SBS: (1) a foreign SBSD that is a broker-dealer would apply Commission segregation requirements to assets received from all

[47] Proposal at 31,015. Because the Commission has not proposed any licensing requirements for associated persons of registered SBSDs, we limit our discussion to the statutory disqualification rules.

[48] See CFTC Rule 3.12(h)(1)(iv) (providing exception with respect to commodity futures and options activity); CFTC No-Action Letter No. 12-43 (Dec. 7, 2012) (extending exception to swap activity).

[49] See Rule 15a-6(b)(2) (limiting the definition of "foreign associated person" to those associated persons of a foreign broker or dealer who participate in the solicitation of certain U.S. investors).

counterparties; (2) a foreign SBSD that is not a broker-dealer and is also not a foreign bank with a U.S. branch or agency would apply Commission segregation requirements to assets received from all counterparties only if it also accepts assets from U.S. persons; and (3) a foreign SBSD that is not a broker-dealer but is a foreign bank with a U.S. branch or agency would only apply Commission segregation requirements to assets received from U.S. counterparties.[50]

- For uncleared SBS: (1) a foreign SBSD that is a broker-dealer would apply Commission segregation requirements to assets received from all counterparties and (2) a foreign SBSD that is not a broker-dealer would apply Commission segregation requirements only to assets received from U.S. counterparties.[51]

We generally support the Commission's proposed cross-border application of segregation requirements to foreign SBSDs, which we believe is consistent with the objective of applying segregation requirements so that they work in tandem with applicable insolvency laws, namely the Securities Investor Protection Act ("SIPA") and the stockbroker liquidation provisions of the U.S. Bankruptcy Code.

We are concerned, however, that the Commission's proposed segregation rules for SBSDs would, as a default matter, apply omnibus segregation requirements based largely on the broker-dealer customer protection rule (Rule 15c3-3) to foreign SBSDs that are not registered broker-dealers, including foreign banks with a U.S. branch or agency. As the Commission notes, the insolvency and liquidation of a foreign SBSD that is a foreign bank with a U.S. branch or agency would be subject to banking regulations, not SIPA or the stockbroker liquidation provisions of the Code.[52] Therefore, the primary justification for applying the Commission's proposed omnibus segregation requirements is not relevant to such an SBSD. In addition, bank SBSDs that hold custody of customer assets are already subject to customer protection requirements by their primary regulators. Requiring them to comply with new, omnibus segregation requirements would be duplicative, burdensome and unnecessary. The same is true of foreign SBSDs that are regulated as broker-dealers or their equivalent under home country law.

Instead, we recommend that the Commission take an approach similar to the one taken by the Treasury Department for the segregation rules applicable to banks that are

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[50] Proposed Rule 18a-4(e)(2).

[51] Proposed Rule 18a-4(e)(1).

[52] Proposal at 31,021.

government securities dealers.[53] Specifically, the Treasury Department provides an exemption to the government securities dealer customer protection requirements for banks that meet certain conditions and are subject to the "rules and standards of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation [or] the Office of Thrift Supervision governing the holding of government securities in a fiduciary capacity by depository institutions."[54] Similarly, foreign bank SBSDs whose custody of customer assets is subject to rules and standards adopted by their U.S. prudential regulator (or a foreign prudential regulator) should not be subject to omnibus segregation requirements with respect to the assets of either U.S. or non-U.S. counterparties. Such SBSDs would still be subject to Dodd-Frank's independent segregation requirements for uncleared SBS, as well as the Commission's proposed segregation-related disclosure requirements.[55] Likewise, foreign SBSDs whose segregation and custody of customer assets are subject to the supervision of a local regulatory authority with respect to broker-dealer activities should not be subject to the Commission's omnibus segregation requirements.

IV. Title VII Requirements Applicable to MSBSPs

Under the Proposal, MSBSPs, unlike SBSDs, would not be eligible for substituted compliance with respect to entity-level requirements or transaction-level requirements specifically applicable to MSBSPs.[56] This aspect of the Proposal appears to be based on the assumption that MSBSPs may not be involved in banking and other financial and investment banking activities.[57] However, it is quite possible that a foreign banking or other financial institution may be subject to regulation as an MSBSP. Many financial institutions that do not deal in credit default swaps still enter into them for hedging purposes. For instance, banks commonly enter into credit default swaps to hedge credit risk assumed as part of their lending businesses. We see no reason why such institutions, if they exceed one of the MSBSP thresholds, should be no less eligible for substituted compliance than a foreign SBSD. Accordingly, we recommend that the Commission permit foreign MSBSPs to be eligible for substitute compliance to the same extent as foreign SBSDs. If a particular foreign MSBSP is not subject to home country oversight that is the basis for a Commission substituted compliance determination, then that MSBSP should not be subject to the determination.

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[53] See 17 C.F.R. Part 450.

[54] 17 C.F.R. § 450.3.

[55] Proposed Rule 18a-4(e)(3).

[56] Proposal at 31,035-36.

[57] Id. at 31,036.

V. Mandatory Clearing and Trading Requirements

A. Cross-Border Scope

Under the Proposal, Dodd-Frank's mandatory clearing and trading requirements would apply to an SBS transaction (1) that is conducted within the U.S. by either counterparty, unless neither counterparty is a U.S. person, a non-U.S. person whose performance is guaranteed by a U.S. person or a foreign SBSD or (2) that is conducted outside the U.S., if (a) either direct counterparty is a U.S. person (other than a transaction conducted through the foreign branch of a U.S. bank) or (b) one counterparty is a foreign branch of a U.S. bank or a non-U.S. person whose obligations are guaranteed by a U.S. person, and the other counterparty is a foreign branch, a non-U.S. person whose obligations are guaranteed by a U.S. person or a foreign SBSD.[58]

Subject to our comments in Part I.B above regarding the application of mandatory clearing and trading requirements based on conduct within the U.S., we generally support the proposed cross-border application of those requirements. Putting aside the conduct test, the Proposal is generally consistent with the relevant CFTC Guidance.

B. Substituted Compliance

Under the Proposal, any person subject to the mandatory clearing requirement would be permitted to satisfy the requirement by clearing the transaction through a registered SBSCA, a foreign SBSCA that is exempt from registration or a foreign SBSCA that is neither registered nor exempt, but for which the Commission has made a substituted compliance determination.[59] In contrast, substituted compliance with respect to mandatory trading would be available if (1) at least one of the direct counterparties is either a non-U.S. person or a foreign branch of a U.S. bank and (2) the transaction is not solicited, negotiated or executed by a person within the U.S. on behalf of such counterparty.[60]

We generally support the proposed scope of substituted compliance with respect to mandatory trading.[61] In particular, we observe that the Commission's proposal to permit substituted compliance in the context of transactions between a foreign SBSD or MSBSP, on the

[58] Proposed Rules 3Ca-3 and 3Ch-1.

[59] Proposal at 31,098.

[60] Proposed Rule 3Ch-2. The Commission would evaluate substituted compliance with respect to mandatory trading based on whether a single SBS market or a class of SBS markets within a foreign jurisdiction is subject to comparable, comprehensive supervision and regulation by the relevant foreign regulatory authority.

[61] For similar reasons, we generally support the proposed scope of substituted compliance with respect to regulatory reporting and public dissemination requirements.

one hand, and a U.S. person, on the other, is consistent with EMIR (and, likely, MiFIR, once adopted).[62] In addition, while the CFTC does not contemplate granting substituted compliance with respect to the application of transaction-level requirements to a swap involving a U.S. person, it does envision granting relief under which a market participant entering into such a swap would be deemed in compliance with Dodd-Frank where it complies with home country requirements that are "essentially identical" to the relevant Dodd-Frank requirements.[63] The CFTC will evaluate whether home country requirements are essentially identical to Dodd-Frank on a provision-by-provision basis.[64] As a result, the principal difference between the CFTC Guidance and the Proposal in this area is that, under the Proposal, the Commission's review of the relevant foreign requirements would be less granular than the CFTC's. This is an example of a difference between the Proposal and the CFTC Guidance that is unlikely to result in significant costs or burdens because the Proposal would permit the Commission to take a more flexible approach than the CFTC, but would not preclude convergence if warranted in a particular case.

We believe that the scope of substituted compliance under the Commission's framework with respect to mandatory clearing should be the same as that applicable to mandatory trading. In particular, we are concerned that the Proposal suggests that a market participant may not rely on an exception or exemption from mandatory clearing under a foreign clearing regime, even if the exception or exemption is generally comparable to one applicable under Commission rules. This approach would depart from the CFTC Guidance, under which the CFTC envisions exercising "broad discretion" with respect to whether an exemption or exception from mandatory clearing under a foreign regime is comparable to Dodd-Frank.[65] The Commission's approach would likely result in undue burdens due to the application of duplicative substantive and procedural standards for reliance on a clearing exception or exemption, especially for transactions subject to mandatory clearing under Dodd-Frank solely because of the involvement of a foreign branch or guaranteed affiliate. The goal of substituted compliance in the context of mandatory clearing should not be to determine whether every transaction that is exempt under a foreign regime is also exempt under the Commission's regime, but rather whether, in the aggregate, the foreign clearing requirement and its exemptions will subject a sufficiently comparable volume of transactions to clearing.

[62] See Article 13 of EMIR; see also ESMA Consultation at p. 7-8.

[63] CFTC Guidance at 45,353.

[64] Id.

[65] See id. at 45,362-63.

VI. Regulatory Reporting and Public Dissemination Requirements

The Proposal indicates that the Commission intends to consider regulatory reporting and public dissemination requirements together for substituted compliance purposes.[66] Under the CFTC Guidance, regulatory reporting under Parts 45 and 46 of the CFTC's Regulations and real-time public reporting under Part 43 of the CFTC's Regulations would be considered separately for substituted compliance purposes.[67] Regulatory reporting and public reporting each serve distinct goals. Regulatory reporting provides the Commission with the tools for market surveillance and oversight of its regulated markets, while public dissemination is designed to provide the market, rather than regulators, real-time price transparency. Because of these discrete objectives, some foreign regulators may adopt one set of reporting requirements but not the other, or adopt both but implement them on separate timelines. At the same time, given the discrepancies in terms of the CFTC's and the Commission's definition of U.S. person and other differences between their respective rules, disparate treatment in the availability of substituted compliance would impose unjustified burdens from the technological infrastructure and other compliance costs necessary to address overlapping and inconsistent reporting requirements. Thus, we believe that the Commission should make individual/separate substituted compliance determinations with respect to regulatory reporting and public dissemination requirements, and should coordinate closely with the CFTC in this respect.

We do not believe that such separate determinations are likely to lead to operational complexities. If a jurisdiction's rules were determined comparable for regulatory reporting but not public reporting, then those SBS transactions subject to both requirements would still need to be reported to a registered SBS data repository ("SBSDR"), but SBS transactions subject solely to regulatory reporting could be reported to a local trade repository. Given that the Proposal contemplates that regulatory reporting requirements would apply to a broader range of transactions than public dissemination requirements—such as transactions between a foreign SBSD and a non-U.S. person whose obligations are not guaranteed by a U.S. person[68]—such a split determination could prove to be quite meaningful in practice. Due to the significant costs associated with the documentation, procedures and technological systems necessary to comply with reporting regimes, the separate possibility of substituted compliance for either regulatory reporting or public dissemination could substantially reduce costs for non-U.S. market participants while still achieving the Commission's important market surveillance and transparency goals.

[66] Proposal at 31,092.

[67] CFTC Guidance at 45,344.

[68] See Proposed Rule 908.

In this respect, we also note that there remain substantial differences between the Commission's approach to regulatory reporting and public dissemination under Regulation SBSR and the CFTC's approach under its reporting rules, including with respect to reporting fields and timing requirements. Most market participants have already developed documentation and operational systems to comply with CFTC reporting requirements, which are already in effect. Differences between the Commission's reporting requirements and the CFTC's approach, therefore, would necessitate the development of parallel systems at substantial cost to market participants.

Additionally, as part of the Proposal, the Commission re-proposed Regulation SBSR, which would set forth the standards for the regulatory reporting and public dissemination of SBS transactions. Among other changes, the Commission modified the "reporting duty" rules under Regulation SBSR, which establish which side of a SBS transaction has the responsibility to report the transaction to SBSDR. Under these rules, generally a registrant would be required to report when facing a non-registered counterparty. When neither side of the transaction includes an SBSD or MSBSP, the U.S. person counterparty would be responsible for reporting.[69]

Under the Commission's rules, some market participants may engage in SBS activity without being required to register as SBSDS because their SBS dealing activity falls below the de minimis threshold for registration (such entities, "De Minimis SBSDs"). Because De Minimis SBSDs are involved in dealing activity, it is likely that such entities have greater technological capability and resources available to fulfill the reporting function. Other non-registrants that do not engage in dealing activity, such as corporate end users, typically do not have such capability. However, under Regulation SBSR as re-proposed, a U.S. end user facing a non-U.S. De Minimis SBSD would be the reporting counterparty for the transaction. We believe that it would be more efficient and fair for the Commission to modify its rules to allow a De Minimis SBSD to agree with its counterparty to be the reporting party when facing a U.S. non-registrant counterparty.[70]

VII. Substituted Compliance Application Standards and Procedures

The Proposal sets forth the Commission's proposed framework for making substituted compliance determinations permitting certain market participants to comply with foreign regulations in lieu of the Dodd-Frank requirements, including the process for making substituted compliance requests and the standards under which the Commission would find comparability. The Institute generally supports the Commission's proposed substituted

[69] Proposed Rule 901.

[70] The Institute has also engaged in discussions with the CFTC regarding the possibility of allowing such agreement between entities that are the equivalent of De Minimis SBSDs with respect to their swap activities and their U.S. non-registrant counterparties.

compliance process, which we believe will be critical for avoiding conflicts or overlap with foreign law. In particular, the Commission's focus on regulatory objectives, rather than identical implementation, represents a sensible approach that comports with principles of international comity while achieving the Commission's important goals under Dodd-Frank.[71]

We have concerns, however, with respect to the substituted compliance application procedures. The Proposal envisions that an application must be submitted by market participants, rather than their regulators.[72] However, this approach runs contrary to current practice, under which the CFTC has initiated a direct, regulator-to-regulator process for substituted compliance in a number of major jurisdictions. We believe that such direct dialogue is more efficient than action by local market participants in most cases, especially given that the Commission will, in any event, need to engage with foreign regulators in order to establish memoranda of understanding and similar arrangements. We also are not aware of any disadvantages to permitting foreign regulators to submit substituted compliance applications on behalf of entities operating within their jurisdiction.

VIII. Market Infrastructures

Generally, the Proposal takes a territorial approach to the registration and regulation of SBS market infrastructures, including SBSDRs, SBSEFs and SBSCAs. Both SBSCAs and SBSDRs would be required to register with the Commission if they performed their functions within the U.S., subject to an exemption for non-U.S. SBSDRs subject to a regulatory authority with which the Commission has entered into a memorandum of understanding.[73] SBSEFs would be required to register if they provided U.S. persons, or non-U.S. persons located in the U.S., the ability to directly execute or trade SBS.[74] We agree with the Commission that a territorial approach to registration is appropriate for market infrastructures. This approach will help to achieve the Commission's market oversight objectives while avoiding conflicts with foreign regulators, and it is consistent with the CFTC's approach.

IX. Timing Considerations

As the Commission recognizes, the SBS markets are truly global in nature. A substantial portion of activity occurs between counterparties located in different jurisdictions, often utilizing market infrastructures or involving other participants located in yet other

[71] Proposal at 31,088.

[72] See, e.g., Proposed Rule 3a71-5(c) (requests by foreign SBSDs).

[73] Proposal at 31,038 and 31,042.

[74] Id. at 31,054.

jurisdictions. Since Title VII of Dodd-Frank creates a new comprehensive regulatory regime, implementation will require significant modifications to technological systems, policies and procedures, legal documentation, personnel arrangements, and a host of other important business considerations. It is critical, therefore, that the scope of a person's obligations be clearly delineated with enough time to make necessary changes. In particular, final cross-border rules should be available well in advance of the deadline for SBSD and MSBSP registration, as these registrants will be subject to a number of complex new rules. We believe that an appropriately sequenced rulemaking process, with finalization of the Commission's cross-border rules occurring before any other substantive rules take effect, would greatly help in accomplishing the Commission's goal of an orderly transition to the Dodd-Frank regime.

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The Institute appreciates the Commission's consideration of these matters. If the Commission or its staff has any questions regarding this letter, please do not hesitate to contact the undersigned at (212) 421-1611.

Respectfully submitted,

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