European Securities and Markets Authority

The Chair

Date: 21 August 2013
ESMA/2013/1142

Ms. Mary Jo White
Chair
Securities and Exchange Commission
100F Street,
NE - Washington
DC 20549-1090

Ref: File Numbers S7-02-13, S7-34-10, S7-40-11
Cross-border Security Based Swap Activities

Dear Chair White,

The European Securities and Markets Authority (ESMA) welcomes the opportunity to comment on the Securities and Exchange Commission's (SEC) proposed rules on cross-border security-based swap activities.

ESMA believes it is of paramount importance to provide legal certainty regarding the regulatory regime applicable to cross border OTC derivative transactions in order to support a safe and efficient global derivatives market.

For this purpose, the regulatory framework of a country should be clear, simple and duly consider the regulatory regime of other jurisdictions. We therefore welcome the application of substituted compliance. However, our view is that its scope of application is still limited and this could create duplications. Furthermore, we believe the framework of proposed rules is very complex.

Above all, ESMA believes that stronger reliance on supervision by, and cooperation with, other regulators is needed and will contribute to achieve clear and efficient rules for the cross-border OTC derivatives market.

You will find attached in Annex 1, some specific comments for your consideration.

Yours sincerely,

Steven Maijoor
Chair
European Securities and Markets Authority

ANNEX 1

SEC consultation on cross border security-based swap activity: items for consideration

Definition of a US person

ESMA has duly considered the proposed definition of a US person and would like to stress that it supports a definition that only covers persons located or incorporated in the US.

ESMA would like to get some clarity as indeed, a clear definition contributes to safe and efficient derivatives markets as it provides legal certainty on the application of the rules.

It is important that the definition of a US person only covers persons and entities established in the United States so as to avoid application to persons that would already be subject to another regulatory framework leading to potentially heavy duplication of applicable rules for the person or entity.

ESMA therefore invites the SEC to clarify the definition of US person when it comes to the "principal place of business". This concept may be given a different scope of application depending on how it is defined. For instance, it should not extend to the persons or entities that have a presence in the United States which is complementary to the principal activity conducted outside of the United States and for which a regulatory framework may already apply. More specifically, ESMA would welcome that US branches of entities established in other jurisdictions such as in the European Union would not be captured. Indeed, US branches of EU entities are part of the EU entities and as such are subject to EMIR. As a result, subjecting them to SEC rules would result in duplication of applicable rules.

Transactions conducted within the US

ESMA understands that because of links with the US territory, some derivative contracts may be subject to SEC rules. The definition of these links covers transactions that are solicited, negotiated, executed or booked within the US. This definition is broad and ESMA invites the SEC to consider limiting the definition to those derivative contracts that are booked within the US.

The place where the derivative contracts are booked is directly related to the place where the risk should be addressed, whereas the place of solicitation, negotiation or even execution of a derivative does not have such direct link with the place where the risk that should be addressed lies. For instance, under the proposed rules, a derivative concluded between a Japanese counterparty and a European counterparty, solicited in the US, would be considered a transaction conducted within the US and counterparties would be subject to the SEC rules although both counterparties would have no other link than solicitation in the US. It would mean that the derivative would

potentially be subject to Japanese, European and US rules which cannot be seen as an efficient result.

Furthermore, as highlighted above, ESMA invites the SEC to clarify in which cases derivatives concluded by the US branch of a party established in another jurisdiction such as the European Union, would be considered as being conducted within the US and would therefore be subject to the SEC regime. If that is the case, those derivatives would potentially be subject to two different regimes at the same time, i.e. the regime where the entity is established (and where the risk resides) and the regime where the branch is located. This would give rise to potential duplicative and conflicting requirements.

Substituted Compliance

ESMA welcomes the SEC approach to consider the outcome of the regulation of other jurisdictions in order to assess applicability of substituted compliance.

ESMA considers it is important that substituted compliance is assessed at the level of the jurisdiction, i.e. at the level of the Union, for Europe. EMIR rules are adopted at European level and apply directly in each Member State.

ESMA also believes that the request for equivalence should be made at the level of the Union and not by individual firms. Indeed, the regulatory framework extends above a single firm and dialogue between regulators should be reinforced.

ESMA invites the SEC to enlarge the scope of application of substituted compliance so as to reduce the number of situations where several sets of rules would apply. In particular, ESMA believes that substituted compliance should apply when a counterparty to the derivative transaction is established in an equivalent jurisdiction and is a non-US person. In such case, substituted compliance should be possible whatever the status of the other party is, including if it is a US person, and whatever the place out of which the transaction is conducted or executed. ESMA believes that substituted compliance should broadly apply when both counterparties are established outside of the US. In this situation, application of US rules should be limited to situations where the transaction would be guaranteed by a US person for a significant value.

Please find below a table of situations where substituted compliance could apply and where SEC rules should, in our view, not apply (N/A) in order to limit the duplication of applicable rules.

	Non US person within the US	*US person*
Registered US Security-Based Swap Dealer	Sub Comp	
Registered non-US Security-Based Swap Dealer with US guarantee	Sub Comp	Sub Comp
Unregistered non-US dealer with US guarantee	Sub Comp	Sub Comp
Registered non-US Security-Based Swap Dealer without US guarantee	N/A	Sub Comp
Unregistered non-US dealer without US guarantee	N/A	Sub Comp

Access to books and records

ESMA understands that as a condition for non-US Security-Based Swap Dealers (SBSD) to register, they need to grant the SEC full access to all their books and records and would be submitting to onsite inspection and examination by the SEC. This means that non-US SBSD would be subject to the SEC jurisdiction for all their activities and not just for activities facing US clients. According to the proposed cross-border release, the SEC "*preliminarily believes that, before a foreign security-based swap dealer should be permitted to make a substituted compliance request, it should assure the Commission that it can provide the Commission with prompt access to books and records and submit to onsite inspection and examination because we expect that access to books and records and the ability to inspect and examine a foreign security-based swap dealer will be essential conditions of any substituted compliance determination*"[1].

This would result in an entity being subject to the supervision of multiple regulators from different jurisdictions that may impose multiple and potentially conflicting requirements. This would create consistency risks and burden on market stakeholders and regulators and could also conflict with national regulations in some EU Member States preventing regulated entities from disclosing certain types of data directly to foreign authorities.

On the contrary, where rules are deemed comparable, ESMA is of the view that regulators should be able to defer to each other in performing their supervisory duties.

[1] Page 313 of the SEC consultation (http://www.sec.gov/rules/proposed/2013/34-69490.pdf)

ESMA therefore believes that this requirement is excessively far-reaching and unnecessary. It could be efficiently replaced by strong cooperation between regulators as is already the case today based on international principles governing cooperation between regulators. Where appropriate, MoUs between the SEC and the relevant national competent authorities may be signed in order to provide a clear framework for cooperation between authorities. This would help preventing conflicting requirements or requests being imposed on the market stakeholders. This approach would also allow for an efficient approach for regulators that would avoid duplication of efforts, for instance in performing on-site inspections.

The objective of substituted compliance and the necessary cooperation of the non-US authorities that accompany such a determination should not be pre-empted by an invasive approach based on direct access to all books and records and on-site inspections which are not conducted in a coordinated manner with the home jurisdiction competent authority.

Foreign Security-Based Swap Execution Facilities

ESMA welcomes reliance on strong cooperation between regulators for foreign Security-Based Swap Execution Facilities. MoUs between the SEC and the relevant competent authorities may be set up in order to provide a clear framework for exchange of information between authorities.