

COMMODITY FUTURES TRADING COMMISSION

17 CFR Chapter I

Request for Comment on Application of Commission Regulations to Swaps Between Non-U.S. Swap Dealers and Non-U.S. Counterparties Involving Personnel or Agents of the Non-U.S. Swap Dealers Located in the United States

AGENCY: Commodity Futures Trading Commission

ACTION: Notice of Request for Comment.

SUMMARY: The Commodity Futures Trading Commission (“Commission”) is requesting comment on an advisory issued by Commission staff on November 14, 2013 (the “Staff Advisory”), regarding the applicability of certain Commission regulations to the activity in the United States of swap dealers (“SDs”) and major swap participants (“MSPs”) registered with the Commission that are established in jurisdictions other than the United States (whether an affiliate or not of a U.S. person, a “non-U.S. SD” or “non-U.S. MSP”).

DATES: Comments must be received on or before [INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER].

ADDRESSES: You may submit comments by any of the following methods:

- The agency’s Web site, at <http://comments.cftc.gov>. Follow the instructions for submitting comments through the website.
- Mail: Melissa D. Jurgens, Secretary of the Commission, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street NW, Washington, DC 20581.

- Hand Delivery/Courier: Same as mail above.
- Federal eRulemaking Portal: <http://www.regulations.gov>. Follow the instructions for submitting comments.

Please submit your comments using only one method.

All comments must be submitted in English, or if not, accompanied by an English translation. Comments may be posted as received to <http://www.cftc.gov>. You should submit only information that you wish to make available publicly. If you wish the Commission to consider information that may be exempt from disclosure under the Freedom of Information Act, a petition for confidential treatment of the exempt information may be submitted according to the established procedures in CFTC Regulation 145.9 (17 CFR 145.9).

The Commission reserves the right, but shall have no obligation, to review, pre-screen, filter, redact, refuse, or remove any or all of your submission from www.cftc.gov that it may deem to be inappropriate for publication, such as obscene language. All submissions that have been redacted or removed that contain comments on the merits of the rulemaking will be retained in the public comment file and will be considered as required under the Administrative Procedure Act and other applicable laws, and may be accessible under the Freedom of Information Act.

FOR FURTHER INFORMATION CONTACT: Gary Barnett, Director, 202-418-5977, gbarnett@cftc.gov, or Frank Fisanich, Chief Counsel, 202-418-5949, ffisanich@cftc.gov, Division of Swap Dealer and Intermediary Oversight, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW, Washington, DC 20581.

SUPPLEMENTARY INFORMATION:

I. Background

On July 21, 2010, President Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act¹ (“Dodd-Frank Act” or “Dodd-Frank”), which, in Title VII, established a new regulatory framework for swaps.

In the three years since the enactment of Dodd-Frank, the Commission has finalized 68 rules, orders, and guidance statements in the process of implementing Title VII of the Dodd-Frank Act. The finalized rules promulgated under section 4s of the CEA, added by the Dodd-Frank Act, address registration of SDs and MSPs and other substantive requirements applicable to SDs and MSPs, while guidance published by the Commission provided the Commission’s general views regarding the scope of the cross-border application of such rules.² Among other things, the Guidance sets forth the Commission’s general views on how it ordinarily expects to apply, in accordance with section 2(i) of the CEA, the CEA and certain Commission regulations applicable on a transaction-by-transaction basis (the “transactional requirements”) to swaps between a non-U.S. SD and a non-U.S. person, including swaps involving guaranteed or conduit affiliates of U.S. persons.³ In addition, the Guidance addressed the circumstances under which the transactional requirements could be satisfied through substituted compliance.⁴

¹ Public Law 111-203, 124 Stat. 1376 (2010).

² See Interpretive Guidance and Policy Statement Regarding Compliance with Certain Swap Regulations 78 FR 45292 (July 26, 2013) (hereinafter, the “Guidance”).

³ For purposes of this notice, the Commission would generally interpret the terms “U.S. person,” “guaranteed affiliate,” and “affiliate conduit” in the same way as described in the Guidance, 78 FR at 45316-17, 45350-59. The Commission uses the term “non-U.S. person” to refer to any person outside its interpretation of the term “U.S. person.”

⁴ The Guidance generally describes the policy and procedural framework under which the Commission would consider a substituted compliance program with respect to Commission regulations applicable to

With few exceptions, the delayed compliance dates for the Commission's regulations implementing requirements of section 4s of the CEA have passed and SDs and MSPs are now required to be in full compliance with such regulations upon registration with the Commission.⁵

Subsequent to publication of the Guidance, swap market participants have raised questions with Commission staff regarding compliance by non-U.S. SDs with the transactional requirements when using personnel or agents located in the United States to enter into swaps with non-U.S. persons. In other words, swap market participants have asked whether the transactional requirements would apply to these swaps (and if so, whether substituted compliance may be available for these swaps) even though such swaps are between two non-U.S. persons, regardless of whether the activities of the non-U.S. SD that lead to such swaps take place in the United States.

In response to these inquiries, the Staff Advisory⁶ was issued, stating that for swaps between a non-U.S. SD and a non-U.S. person, the transactional requirements either do not apply or, in some cases, may be subject to substituted compliance if the activities of the non-U.S. SD take place outside the United States. The Staff Advisory further stated that, for transactions arranged, executed, or negotiated by personnel or

non-U.S. SDs. Specifically, the Commission described circumstances where it expected that compliance with a comparable regulatory requirement of a foreign jurisdiction would serve as a reasonable substitute for compliance with the attendant requirements of the CEA and the Commission's regulations, 78 FR at 45342-44.

⁵ The compliance dates are summarized on the Compliance Dates page of the Commission's Web site. (<http://www.cftc.gov/LawRegulation/DoddFrankAct/ComplianceDates/index.htm>.)

⁶ Division of Swap Dealer and Intermediary Oversight, Applicability of Transaction-Level Requirements to Activity in the United States, Nov. 14, 2013. Available at: <http://www.cftc.gov/ucm/groups/public/@lrllettergeneral/documents/letter/13-69.pdf>. As stated in the Staff Advisory, the advisory, and the views expressed therein, represent the views of the Division of Swap Dealer and Intermediary Oversight only, and do not represent the position or view of the Commission or of any other office or division of the Commission.

agents located in the United States of non-U.S. SDs (whether affiliates or not of a U.S. person) regularly using personnel or agents located in the U.S. to arrange, negotiate, or execute swaps with non-U.S. persons (the “Covered Transactions”), the non-U.S. SD generally would be required to comply with the transactional requirements. The Staff Advisory further stated that this view would also apply to a Covered Transaction booked in a non-U.S. branch of the non-U.S. SD.⁷

The Commission notes that subsequent to the Staff Advisory, the Commission’s Divisions of Swap Dealer and Intermediary Oversight, Market Oversight, and Clearing and Risk provided non-U.S. SDs time-limited staff no-action relief from certain transactional requirements for Covered Transactions,⁸ and have recently extended such relief until September 15, 2014, subject to certain terms and conditions stated in such Divisions’ no-action letter.⁹

II. Request for Comment

In view of the complex legal and policy issues involved with respect to the Staff Advisory, the Commission is soliciting comment from all interested parties to further inform the Commission’s and its staff’s deliberations regarding the subjects addressed in the Staff Advisory.

Accordingly, the Commission requests comment on all aspects of the Staff Advisory, including but not limited to the following points. If a comment relates to one

⁷ See the Staff Advisory, *supra* note 6.

⁸ See CFTC Staff Letter 13-71, available on the Commission’s website: <http://www.cftc.gov/ucm/groups/public/@lrlettergeneral/documents/letter/13-71.pdf>.

⁹ See CFTC Staff Letter 14-01, available on the Commission’s website.

of the specific points noted below, please identify the point by number and provide a detailed rationale supporting the response.

1. The Commission invites comment on whether the Commission should adopt the Staff Advisory as Commission policy, in whole or in part.

2. The Commission invites commenters to provide their views on whether transactional requirements should apply to Covered Transactions with non-U.S. persons who are not guaranteed or conduit affiliates of U.S. persons. Please provide a detailed analysis of any such view and its effect on other aspects of the Commission's cross-border policy, if any.

3. The Commission invites comment on whether there should be any differentiation in treatment of swaps with non-U.S. counterparties depending on the nature of the SD (i.e., whether it is a guaranteed affiliate or a conduit affiliate of a U.S. person).

4. To the extent a non-U.S. SD must comply with the transactional requirements when entering a Covered Transaction, should the non-U.S. SD be able to rely on a substituted compliance program for purposes of complying with the relevant transactional requirements? If so, should substituted compliance be available for all transactional requirements or only specific requirements? Which requirements? Would the response be different depending on the nature of the counterparty (i.e., whether the non-U.S. counterparty is a guaranteed affiliate or a conduit affiliate of a U.S. person)?

5. The Commission invites comment on the meaning of "regularly" in the phrase "persons regularly arranging, negotiating, or executing swaps for or on behalf of an SD" and whether such persons are performing core, front-office activities of that SD's swap

dealing business. If not, what specific activities would constitute the core, front-office activities of an SD's swap dealing business? What characteristics or factors distinguish a "core, front-office" activity from other activities? Please be exhaustive in describing such activities.

6. The Commission invites comment on the scope and degree of "arranging, negotiating, or executing" swaps as used in this context.

Issued in Washington, DC on January 3, 2014, by the Commission.

Melissa D. Jurgens,

Secretary of the Commission

Appendices to Request for Comment on Application of Commission Regulations to Swaps Between Non-U.S. Swap Dealers and Non-U.S. Counterparties Involving Personnel or Agents of the Non-U.S. Swap Dealers Located in the United States

Appendix 1 – Commission Voting Summary

On this matter, Chairman Gensler and Commissioners Chilton and Wetjen voted in the affirmative. Commissioner O'Malia voted in the negative.

Appendix 2 – Dissenting Statement of Commissioner Scott D. O'Malia

If you thought that the Commission's approach last year regarding cross-border issues resulted in an unsound rulemaking process, the start of 2014 is no better.

Today's announcement of the request for comment on a staff Advisory abrogates the Commission's fundamental legal obligations under the Administrative Procedure Act ("APA") and provides another example of the Commission's unsound rule implementation process.

Making matters worse, today's request for comment is completely outside the scope of the cross-border Guidance and the Exemptive Order as the Commission did not address the issue relating to swaps negotiated between non-U.S. swap dealers ("SDs") and non-U.S. counterparties acting through agents of the non-U.S. SDs located in the United States. This is simply a strategic move by the Commission to try to duck blame for consistently circumventing the fundamental tenets of the APA and failing to adhere faithfully to the express congressional directive to limit the extraterritorial application of the Dodd-Frank Act to foreign transactions that "have a direct and significant connection with activities in, or effect on, commerce of the United States."¹

Moreover, I question why the Commission has decided to request comment on a narrow issue of the extraterritorial application of Dodd-Frank, while essentially ignoring the dozens of comments already filed as part of the Commission's cross-border Exemptive Order.² Simply requesting comment on a staff Advisory does not endorse the validity of the cross-border Guidance or the staff Advisory issued based on the Guidance.

Additionally, I have serious concerns with the evolving jurisdictional application of the Commission's authority over cross-border trades. It appears based on the staff Advisory, that the Commission is applying a "territorial" jurisdiction test to elements of a

¹ 7 U.S.C. 2(i).

² See Statement of Dissent by Commissioner Scott D. O'Malia, Interpretive Guidance and Policy Statement Regarding Compliance With Certain Swap Regulations and Related Exemptive Order, July 12, 2013, <http://www.cftc.gov/PressRoom/SpeechesTestimony/omaliastatement071213b>.

trade between non-U.S. entities. To better understand the legal underpinnings of this position, I have included several additional questions to be considered as part of the overall comment file. It is my hope that public comments will provide greater clarity regarding our cross-border authority and identify areas where we must harmonize global rules with our international regulatory partners in the near future. It makes no sense to apply guidance or staff advisories that do not enjoy the full support and authority provided through rulemakings based on the Commodity Exchange Act (“CEA”).

Looking forward into this year, the CFTC needs to do away with the reflexive rule implementation process via staff no-action and advisories that are not voted on by the Commission. It should be the goal of the Commission to develop rules that adhere to the APA and ensure proper regulatory oversight, transparency and promote competition in the derivatives space.

In this regard, I would like to seek additional comment on the following points:

1. Please provide your views on whether Covered Transactions with non-U.S. persons who are not guaranteed or conduit affiliates of U.S. persons meet the direct and significant test under CEA section 2(i).³ Please provide a detailed analysis of any such view and its effect on other aspects of the Commission’s cross-border policy, if any. Would your view change depending on whether a non-U.S. SD is a guaranteed affiliate or a conduit affiliate of a U.S. person?
2. CEA section 2(a)(1)⁴ provides for the general jurisdiction of the Commission. Please provide your views on whether Covered Transactions with non-U.S. persons who are not guaranteed or conduit affiliates of U.S. persons fall

³ 7 U.S.C. 2(i).

⁴ 7 U.S.C. 2(a)(1).

within the Commission's jurisdiction under CEA section 2(a)(1) or any other provision of the CEA providing for Commission jurisdiction. Please provide a detailed analysis of any such view and its effect on other aspects of the Commission's cross-border policy, if any. Would your view change depending on the nature of the non-U.S. SD (i.e., whether it is a guaranteed affiliate or a conduit affiliate of a U.S. person)?

3. To the extent that Covered Transactions fall within the Commission's jurisdiction, should a non-U.S. SD be required to comply with all, or only certain, Transaction-Level Requirements? Please provide a detailed analysis of any such view and its effect on other aspects of the Commission's cross-border policy, if any. Would your view change depending on the nature of the non-U.S. SD (i.e., whether it is a guaranteed affiliate or a conduit affiliate of a U.S. person)?
4. In the open meeting to consider the cross-border final guidance and cross-border phase-in exemptive order, I asked about the Commission's enforcement and legal authority under the cross-border guidance. The Commission's General Counsel replied, "[T]he guidance itself is not binding strictly. We couldn't go into court and, in a count of the complaint, list a violation of the guidance as an actionable claim."⁵ If the Commission adopts the staff Advisory as Commission policy (and not through the rulemaking process), please provide your views on the Commission's ability to enforce such policy.

⁵ Transcript of Open Meeting to Consider Cross-Border Final Guidance and Cross-Border Phase-In Exemptive Order (July 12, 2013), page 79.