BILLING CODE: 6351-01-P

COMMODITY FUTURES TRADING COMMISSION

17 CFR Chapter 1

RIN 3038-AD85

Interpretive Guidance and Policy Statement Regarding Compliance with Certain Swap Regulations

AGENCY: Commodity Futures Trading Commission

ACTION: Notice of Interpretive Guidance and Policy Statement

SUMMARY: On July 12, 2012, the Commodity Futures Trading Commission ("Commission" or "CFTC") published for public comment its proposed interpretive guidance and policy statement ("Proposed Guidance") regarding the cross-border application of the swaps provisions of the Commodity Exchange Act ("CEA"), as added by Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act" or "Dodd-Frank"). On December 21, 2012, the Commission also proposed further guidance on certain aspects of the Proposed Guidance ("Further Proposed Guidance").

The Commission has determined to finalize the Proposed Guidance with certain modifications and clarifications to address public comments. The Commission's Interpretive Guidance and Policy Statement ("Guidance") addresses the scope of the term "U.S. person," the general framework for swap dealer and major swap participant registration determinations (including the aggregation requirement applicable to the de minimis calculation with respect to swap dealers), the treatment of swaps involving certain foreign branches of U.S. banks, the treatment of swaps involving a non-U.S. counterparty guaranteed by a U.S. person or "affiliate

conduit," and the categorization of the Dodd-Frank swaps provisions as "Entity-Level Requirements" or "Transaction-Level Requirements."

EFFECTIVE DATE: This Guidance will become effective immediately upon publication in the Federal Register.

FOR FURTHER INFORMATION CONTACT: Gary Barnett, Director, Division of Swap Dealer and Intermediary Oversight, (202) 418-5977, gbarnett@cftc.gov; Sarah E. Josephson, Director, Office of International Affairs, (202) 418-5684, sjosephson@cftc.gov; Mark Fajfar, Assistant General Counsel, Office of General Counsel, (202) 418-6636, mfajfar@cftc.gov; Laura B. Badian, Counsel, Office of General Counsel, (202) 418-5969, lbadian@cftc.gov; Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW., Washington, DC 20581.

SUPPLEMENTARY INFORMATION:

## Table of Contents


**I. Introduction ..... 7**

A. The Dodd-Frank Wall Street Reform and Consumer Protection Act ..... 7
B. The Proposed Guidance and Further Proposed Guidance ..... 13

**II. Scope of this Guidance ..... 19**

**III. Interpretation of Section 2(i) ..... 22**

A. Comments ..... 23
B. Statutory Analysis ..... 25
C. Principles of International Comity ..... 33

**IV. Guidance ..... 37**

A. Interpretation of the Term "U.S. Person" ..... 37
1. Proposed Interpretation ..... 37
2. Comments ..... 42
a. Phase-in Interpretation ..... 43
b. Comments on Particular Prongs of the Proposed Interpretation of the Term "U.S. Person" ..... 44
c. Commenters' Proposed Alternatives ..... 57
d. Due Diligence ..... 57
e. Non-U.S. Person that is Affiliated, Guaranteed, or Controlled by U.S. Person ..... 58
f. Foreign Branch of U.S. Person ..... 61
g. Regulation S ..... 62
h. Other Clarifications ..... 63
3. Commission Guidance ..... 64
a. Due Diligence ..... 87
b. Foreign Branch of U.S. Person ..... 89
c. Regulation S ..... 90
d. Other Clarifications ..... 92
4. Summary ..... 93
B. Registration ..... 95
1. Proposed Guidance ..... 95
2. Comments ..... 97
3. Commission Guidance ..... 101
a. Registration Thresholds for U.S. Persons and Non-U.S. Persons, Including Those Guaranteed by U.S. Persons ..... 101
b. Aggregation ..... 107
c. Exclusion of Certain Swaps by Non-U.S. Persons from the Swap Dealer De Minimis Threshold ..... 120
d. Exclusion of Certain Swaps by Non-U.S. Persons from the MSP Calculation ..... 123
e. Exclusion of Certain Swaps Executed Anonymously on a SEF, DCM, or Foreign Board of Trade ("FBOT") and Cleared ..... 126

f. MSP-Parent Guarantees ..... 128
4. Summary ..... 130
C. Interpretation of the Term "Foreign Branch;" When a Swap Should be Considered to be with the Foreign Branch of a U.S. Person that is a Swap Dealer or MSP ..... 133
1. Interpretation of the Term "Foreign Branch" and Treatment of Foreign Branches ..... 133
2. Comments ..... 136
3. Commission Guidance ..... 140
a. Scope of the Term "Foreign Branch" ..... 140
b. Commission Consideration of Whether a Swap is With a Foreign Branch of a U.S. Bank ..... 144
D. Description of the Entity-Level and Transaction-Level Requirements ..... 148
1. Description of the Entity-Level Requirements ..... 150
a. First Category of Entity-Level Requirements ..... 151
i. Capital adequacy ..... 151
ii. Chief compliance officer ..... 152
iii. Risk management ..... 152
iv. Swap data recordkeeping (except certain aspects of swap data recordkeeping relating to complaints and sales materials) ..... 153
b. Second Category of Entity-Level Requirements ..... 154
i. SDR Reporting ..... 154
ii. Swap data recordkeeping relating to complaints and marketing and sales materials ..... 155
iii. Physical commodity large swaps trader reporting (Large Trader Reporting) ..... 156
2. Description of the Transaction-Level Requirements ..... 157
a. Category A: Risk Mitigation and Transparency ..... 158
i. Required clearing and swap processing ..... 158
ii. Margin and segregation requirements for uncleared swaps ..... 160
iii. Trade execution ..... 161
iv. Swap trading relationship documentation ..... 162
v. Portfolio reconciliation and compression ..... 163
vi. Real-time public reporting ..... 164
vii. Trade confirmation ..... 164
viii. Daily trading records ..... 165
b. Category B: External Business Conduct Standards ..... 165
E. Categorization of Entity-Level and Transaction-Level Requirements ..... 166
1. Categorization under the Proposed Guidance ..... 167
2. Comments ..... 168
a. Reporting and trade-execution requirements ..... 168
b. Swap trading relationship documentation, portfolio reconciliation and compression, daily trading records and external business conduct standards ..... 170
c. Internal conflicts of interest requirement ..... 171
d. Position limits and anti-manipulation rules ..... 172
3. Commission Guidance ..... 172
a. Entity-Level Requirements ..... 173

i. The First Category – Capital Adequacy, Chief Compliance Officer, Risk Management, and Swap Data Recordkeeping (except for certain recordkeeping requirements) ... 176
ii. The Second Category – SDR Reporting, Certain Swap Data Recordkeeping Requirements and Large Trader Reporting ... 177
b. Transaction-Level Requirements ... 178
i. The Category A Transaction-Level Requirements ... 179
ii. The Category B Transaction-Level Requirements (External Business Conduct Standards) ... 182
F. Substituted Compliance ... 184
1. Proposed Guidance ... 184
2. Comments ... 185
3. Overview of the Substituted Compliance Regime ... 192
4. Process for Comparability Determinations ... 197
5. Conflicts Arising under Privacy and Blocking Laws ... 202
6. Clearing ... 203
a. Clearing Venues ... 203
b. Foreign End-Users ... 205
G. Application of the Entity-Level and Transaction-Level Requirements to Swap Dealers and MSPs ... 207
1. Comments ... 207
2. Commission Guidance ... 209
3. Application of the Entity-Level Requirements to Swap Dealers and MSPs ... 212
The Commission's policy on ... 213
a. To U.S. Swap Dealers and MSPs ... 213
b. To Non-U.S. Swap Dealers and MSPs ... 214
4. Application of the "Category A" Transaction-Level Requirements to Swap Dealers and MSPs ... 220
a. Swaps with U.S. Swap Dealers and MSPs ... 221
b. Swaps with Non-U.S. Swap Dealers and Non-U.S. MSPs ... 224
c. Swaps with a Non-U.S. Person Guaranteed by a U.S. Person ... 233
i. Proposed Guidance ... 233
ii. Comments ... 234
iii. Commission Guidance ... 239
d. Swaps with a Non-U.S. Person that is an Affiliate Conduit ... 246
i. Proposed Guidance ... 246
ii. Comments ... 247
iii. Commission Guidance ... 249
5. Application of the "Category B" Transaction-Level Requirements to Swap Dealers and MSPs ... 254
a. Swaps with U.S. Swap Dealers and U.S. MSPs ... 256
b. Swaps with Foreign Branches of a U.S. Bank that is a Swap Dealer or MSP ... 256
c. Swaps with Non-U.S. Swap Dealers and Non-U.S. MSPs ... 258
H. Application of the CEA's Swap Provisions and Commission Regulations to Market Participants that are not Registered as a Swap Dealer or MSP ... 261

1. Swaps between Non-Registrants Where One or More of the Non-Registrants is a U.S. Person ..... 262
2. Swaps between Non-Registrants that are Both Non-U.S. Persons ..... 269
a. Large Trader Reporting ..... 270
b. Swaps Where Each of The Counterparties is Either a Guaranteed or Conduit Affiliate ..... 271
c. Swaps Where Neither or Only One of the Parties is a Guaranteed or Conduit Affiliate ..... 273

**V. Appendix A – The Entity-Level Requirements ..... 274**

A. First Category of Entity-Level Requirements ..... 274
1. Capital adequacy ..... 274
2. Chief compliance officer ..... 275
3. Risk management ..... 276
i. Swap data recordkeeping (except certain aspects of swap data recordkeeping relating to complaints and sales materials) ..... 277
B. Second Category of Entity-Level Requirements ..... 278
1. SDR Reporting ..... 278
2. Swap data recordkeeping relating to complaints and marketing and sales materials ..... 279
3. Physical commodity large swaps trader reporting (Large Trader Reporting) ..... 280

**VI. Appendix B – The Transaction-Level Requirements ..... 281**

A. Category A: Risk Mitigation and Transparency ..... 281
1. Required clearing and swap processing ..... 281
2. Margin and segregation requirements for uncleared swaps ..... 283
3. Trade execution ..... 284
4. Swap trading relationship documentation ..... 284
5. Portfolio reconciliation and compression ..... 285
6. Real-time public reporting ..... 286
7. Trade confirmation ..... 287
8. Daily trading records ..... 287
B. Category B: External Business Conduct Standards ..... 288

**VII. Appendix C – Application of the Entity-Level Requirements to Swap Dealers and MSPs* ..... 289**

**VIII. Appendix D – Application of the Category A Transaction-Level Requirements to Swap Dealers and MSPs* ..... 290**

**IX. Appendix E – Application of the Category B Transaction-Level Requirements to Swap Dealers and MSPs* ..... 292**

**X. Appendix F – Application of Certain Entity-Level and Transaction-Level Requirements to Non-Swap Dealer/Non-MSP Market Participants* ..... 294**

## I. Introduction

### A. The Dodd-Frank Wall Street Reform and Consumer Protection Act

On July 21, 2010, President Obama signed the Dodd-Frank Act,[1] Title VII of which amended the CEA to establish a new regulatory framework for swaps. The legislation was enacted to reduce systemic risk (including risk to the U.S. financial system created by interconnections in the swaps market), increase transparency, and promote market integrity within the financial system by, among other things: (1) providing for the registration and comprehensive regulation of swap dealers[2] and major swap participants (each, an "MSP"); (2) imposing clearing and trade execution requirements on standardized derivatives products; (3) creating rigorous recordkeeping and data reporting regimes with respect to swaps, including real-time public reporting; and (4) enhancing the Commission's rulemaking and enforcement authorities over all registered entities, intermediaries, and swap counterparties subject to the Commission's oversight.

Section 722(d) of the Dodd-Frank Act amended the CEA by adding section 2(i),[3] which provides that the swaps provisions of the CEA (including any CEA rules or regulations) apply to cross-border activities when certain conditions are met, namely, when such activities have a "direct and significant connection with activities in, or effect on, commerce of the United States" or when they contravene Commission rules or regulations as are necessary or appropriate to

---

[1] Public Law 111–203, 124 Stat. 1376 (2010). The text of the Dodd-Frank Act may be accessed at http://www.cftc.gov/LawRegulation/OTCDERIVATIVES/index.htm.

[2] For purposes of this Guidance, the term "swap dealer" means any swap dealer registered with the Commission. Similarly, the term "MSP" means any MSP registered with the Commission.

[3] 7 U.S.C. 2(i).

prevent evasion of the swaps provisions of the CEA enacted under Title VII of the Dodd-Frank Act.[4]

The potential for cross-border activities to have a substantial impact on the U.S. financial system was apparent in the fall of 2008, when a series of large financial institutional failures threatened to freeze foreign and domestic credit markets. In September 2008, for example, U.S.-regulated insurance company American International Group ("AIG") nearly failed as a result of risk incurred by the London swap trading operations of its subsidiary AIG Financial Products ("AIGFP").[5] Enormous losses on credit default swaps entered into by AIGFP and guaranteed by AIG led to a credit downgrade for AIG, triggering massive collateral calls and an acute liquidity crisis for both entities. AIG only avoided default through more than $112.5 billion in support

---

[4] Id. Section 2(i) of the CEA states:

> The provisions of this Act relating to swaps that were enacted by the Wall Street Transparency and Accountability Act of 2010 (including any rule prescribed or regulation promulgated under that Act), shall not apply to activities outside the United States unless those activities –
>
> (1) have a direct and significant connection with activities in, or effect on, commerce of the United States; or
>
> (2) contravene such rules or regulations as the Commission may prescribe or promulgate as are necessary or appropriate to prevent the evasion of any provision of this Act that was enacted by the Wall Street Transparency and Accountability Act of 2010.

[5] See, e.g., Congressional Oversight Panel, June Oversight Report, The AIG Rescue, Its Impact on Markets, and the Government's Exit Strategy, (Jun. 10, 2010), available at http://www.gpo.gov/fdsys/pkg/CPRT-111JPRT56698/pdf/CPRT-111JPRT56698.pdf ("AIG Report"); Office of the Special Inspector General for the Troubled Asset Relief Program, Factors Affecting Efforts to Limit Payments to AIG Counterparties (Nov. 17, 2009), available at http://www.sigtarp.gov/Audit%20Reports/Factors_Affecting_Efforts_to_Limit_Payments_to_AIG_Counterparties.pdf. AIGFP was a Delaware corporation based in Connecticut that was an active participant in the credit default swap ("CDS") market in the years leading up to the crisis. See id. at 23. AIGFP's CDS activities benefited from credit support provided by another Delaware corporation, American International Group, Inc., AIGFP's highly-rated parent company. Although both AIG and AIGFP were incorporated and headquartered in the U.S., much of AIGFP's CDS business was conducted through its London office and involved non-U.S. counterparties and credit exposures. Id. at 18. See also Office of the Special Inspector General for the Troubled Asset Relief Program, Factors Affecting Efforts to Limit Payments to AIG Counterparties, at 20 (Nov. 17, 2009) (listing AIG FP's CDS counterparties, including a variety of U.S. and foreign financial institutions), available at: http://www.sigtarp.gov/Audit%20Reports/Factors_Affecting_Efforts_to_Limit_Payments_to_AIG_Counterparties.pdf.

from the Federal Reserve Bank of New York and nearly $70 billion from the U.S. Department of the Treasury and the Federal Reserve.

A global, complex, and highly integrated business model also played a role in, and complicated, the bankruptcy of former U.S.-based multinational corporation Lehman Brothers Holding Inc. ("LBHI") in September 2008. In addition to guaranteeing certain swaps for its subsidiary Lehman Brothers International Europe ("LBIE"), estimated at nearly 130,000 OTC derivatives contracts at the time LBIE was placed into administration on September 15, 2008, LBHI and its global affiliates relied on each other for many of their financial and operational services, including treasury and depository functions, custodial arrangements, trading facilitation, and information management.[6] The complexity of the financial and operational relationships of LBHI and its domestic and international affiliates, including with respect to risk associated with swaps, provides an example of how risks can be transferred across multinational affiliated entities, in some cases in non-transparent ways that make it difficult for market participants and regulators to fully assess those risks.

Even in the absence of an explicit business arrangement or guarantee, U.S. companies may for reputational or other reasons choose, or feel compelled, to assume the cost of risks incurred by foreign affiliates. In 2007, U.S.-based global investment firm Bear Stearns decided to extend loans secured by assets of uncertain value to two Cayman Islands-based hedge funds it sponsored after they suffered substantial losses due to their investments in subprime mortgages,

---

[6] "The global nature of the Lehman business with highly integrated, trading and non-trading relationships across the group led to a complex series of inter-company positions being outstanding at the date of Administration. There are over 300 debtor and creditor balances between LBIE and its affiliates representing $10.5B of receivables and $11.0B of payables as at September 15 2008." See Lehman Brothers International (Europe) in Administration, Joint Administrators' Progress Report for the Period 15 September 2008 to 14 March 2009 (Apr. 14, 2009) ("Lehman Brothers Progress Report"), available at http://www.pwc.co.uk/en_uk/uk/assets/pdf/lbie-progress-report-140409.pdf.

even though Bear Stearns was not legally obligated to support those funds.[7] Shortly thereafter, the funds, filed for bankruptcy protection.[8]

Although the Dodd-Frank Act was enacted in the wake of the 2008 financial crisis, the impact of cross-border activities on the health and stability of U.S. companies and financial markets is not new. A decade before the AIG and Lehman collapses, a Cayman Islands hedge fund managed by Connecticut-based Long-Term Capital Management L.P. ("LTCM") nearly failed.[9] The hedge fund had a swap book of more than $1 trillion notional and only $4 billion in capital. The hedge fund avoided collapse only after the Federal Reserve Bank of New York intervened and supervised a financial rescue and reorganization by creditors of the fund.[10] While the fund was a Cayman Island partnership, its default would have caused significant market disruption in the United States.[11]

More recently, J.P. Morgan Chase & Co. ("J.P. Morgan"), the largest U.S. bank, disclosed a multi-billion dollar trading loss stemming in part from positions in a credit-related swap portfolio managed through its London Chief Investment Office.[12] The relationship

---

[7] See In re Bear Sterns High-Grade Structured Credit Strategies Master Funds, Ltd., 374 B.R. 122 (Bankr. S.D.N.Y. 2007), available at http://www.nysb.uscourts.gov/opinions/brl/158971_25_opinion.pdf.

[8] See id.

[9] See The President's Working Group on Financial Markets, Hedge Funds, Leverage, and the Lessons of Long-Term Capital Management (April 1999), available at http://www.treasury.gov/resource-center/fin-mkts/Documents/hedgfund.pdf.

[10] See id. at 13.

[11] See id. at 17.

[12] See Sen. Permanent Subcomm. on Investigations, 113th Cong., Majority and Minority Staff Report, JPMorgan Chase Whale Trades: A Case History of Derivatives Risks and Abuses (March 15, 2013), available at http://www.levin.senate.gov/download/?id=bfb5cd04-41dc-4e2d-a5e1-ab2b81abfaa8-2560k. See also Dodd-Frank Statement ("[A]ny suggestion that U.S. financial entities learned enough from AIG's devastating misjudgments are [sic] undercut by the multi-billion dollar loss incurred by a bank generally considered to be among the most careful – J.P.Morgan Chase – in its London derivative trading.").

between the New York and London offices of J.P. Morgan that were involved in the credit swaps that were the source of this loss demonstrates the close integration among the various branches, agencies, offices, subsidiaries and affiliates of U.S. financial institutions, which may be located both inside and outside the United States. Despite their geographic expanse, the branches, agencies, offices, subsidiaries and affiliates of large U.S. financial institutions in many cases effectively operate as a single business.[13]

Efforts to regulate the swaps market in the wake of the 2008 financial crisis are underway not only in the United States, but also abroad. In 2009, leaders of the Group of 20 ("G20")– whose membership includes the European Union ("EU"), the United States, and 18 other countries – agreed that: (i) OTC derivatives contracts should be reported to trade repositories; (ii) all standardized OTC derivatives contracts should be cleared through central counterparties and traded on exchanges or electronic trading platforms, where appropriate, by the end of 2012; and (iii) non-centrally cleared contracts should be subject to higher capital requirements. In line with the G20 commitment, much progress has been made to coordinate and harmonize international reform efforts, but the pace of reform varies among jurisdictions and disparities in regulations remain due to differences in cultures, legal and political traditions, and financial systems.[14]

---

[13] See Letter from Sen. Carl Levin, Chairman of the Permanent Subcommittee on Investigations at 4 (Apr. 23, 2013) ("Letter from Sen. Levin"), available at http://www.levin.senate.gov/download/levin_comment_letter_cftc_042313. See also Cross-Border Application of Certain Swaps Provisions of the Commodity Exchange Act, 77 FR 41214, 41216 (Jul. 12, 2012) ("Proposed Guidance").

[14] Legislatures and regulators in a number of foreign jurisdictions are undertaking significant regulatory reforms over the swaps market and its participants. See CFTC and SEC, Joint Report on International Swap Regulation Required by Section 719(c) of the Dodd-Frank Wall Street Reform and Consumer Protection Act at 13 (Jan. 31, 2012), available at http://www.cftc.gov/ucm/groups/public/@swaps/documents/file/dfstudy_isr_013112.pdf.

The failures of Lehman Brothers and the Bear Stearns hedge funds, and the near failures of LTCM's hedge fund and AIG (which required intervention by the government and Federal Reserve), and their collateral effects on the broader economy and U.S. commerce,[15] provide examples of how risks that a large financial institution takes abroad in swap transactions or otherwise can result in or contribute to substantial losses to U.S. persons and threaten the financial stability of the entire U.S. financial system. These failures and near failures revealed the vulnerability of the U.S. financial system and economy to systemic risk resulting from, among other things, poor risk management practices of certain financial firms, the lack of supervisory oversight for certain financial institutions as a whole, and the overall

---

For example, the European Commission released a public consultation on revising the Markets in Financial Instruments Directive ("MiFID") in December 2010. See "European Commission Public Consultation: Review of the Markets in Financial Instruments Directive" (Dec. 8, 2010), available at http://ec.europa.eu/internal_market/consultations/docs/2010/mifid/consultation_paper_en.pdf.

In October 2011, the European Commission released two public consultations, one to revise MiFID and the other for creating a new regulation entitled the Markets in Financial Instruments Regulation ("MiFIR"). See European Commission, Proposal for a Directive of the European Parliament and of the Council on markets in financial instruments repealing Directive 2004/39/EC of the European Parliament and of the Council, COM (2011) 656 final (Oct. 20, 2011), available at http://ec.europa.eu/internal_market/securities/docs/isd/mifid/COM_2011_656_en.pdf; European Commission, Proposal for a Regulation of the European Parliament and of the Council on markets in financial instruments and amending regulation [EMIR] on OTC derivatives, central counterparties and trade repositories, COM (2011) 652 final (Oct. 20, 2011), available at http://ec.europa.eu/internal_market/securities/docs/isd/mifid/COM_2011_652_en.pdf.

As of March 15, 2013, the majority of the regulatory technical standards (i.e., rulemakings) of the European Market Infrastructure Regulation ("EMIR") entered into force. The EMIR and the related regulatory technical standards generally regard requirements for clearinghouses, clearing, data repositories, regulatory reporting, and uncleared OTC transactions. Certain technical standards under EMIR have yet to be developed and completed. These standards regard margin and capital for uncleared transactions and contracts that have a "direct, substantial and foreseeable effect within the [European] Union." See EMIR Article 11(14)(e).

The Japanese legislature passed the Amendment to the Financial Instruments and Exchange Act ("FIEA") in May 2010. See Japan Financial Services Agency, Outline of the bill for amendment of the Financial Instruments and Exchange Act (May 2010), available at http://www.fsa.go.jp/en/refer/diet/174/01.pdf.

[15] On October 3, 2008, President Bush signed the Emergency Economic Stabilization Act of 2008, which was principally designed to allow the U.S. Treasury and other government agencies to take action to restore liquidity and stability to the U.S. financial system (e.g., the Troubled Asset Relief Program – also known as TARP – under which the U.S. Treasury was authorized to purchase up to $700 billion of troubled assets that weighed down the balance sheets of U.S. financial institutions). See Pub. L. 110-343, 122 Stat. 3765 (2008).

interconnectedness of the global swap business.[16] These failures and near failures demonstrate the need for and potential implications of cross-border swaps regulation.

### B. The Proposed Guidance and Further Proposed Guidance

To address the scope of the cross-border application of the Dodd-Frank Act, the Commission published the Proposed Guidance on July 12, 2012, setting forth its proposed interpretation of the manner in which it intends that section 2(i) of the CEA would apply Title VII's swaps provisions to cross-border activities.[17] In view of the complex legal and policy issues involved, the Commission published the Proposed Guidance to solicit comments from all interested persons and to further inform the Commission's deliberations. Specifically, the Proposed Guidance addressed the general manner in which the Commission proposed to consider: (1) when a non-U.S. person's swap dealing activities would justify registration as a "swap dealer,"[18] as further defined in a joint release adopted by the Commission and the Securities and Exchange Commission ("SEC");[19] (2) when a non-U.S. person's swaps positions

---

[16] See Financial Crisis Inquiry Commission, The Financial Crisis Inquiry Report: Final Report of the National Commission on the Causes of the Financial and Economic Crisis in the United States at xvi-xxvii (Jan. 21, 2011), available at http://www.gpo.gov/fdsys/pkg/GPO-FCIC/pdf/GPO-FCIC.pdf.

[17] See Proposed Guidance, 77 FR 41214. Simultaneously with publication of the Proposed Guidance, the Commission published a proposed exemptive order providing time-limited relief from certain cross-border applications of the swaps provisions of Title VII and the Commission's regulations. See Proposed Exemptive Order Regarding Compliance with Certain Swap Regulations, 77 FR 41110 (July 12, 2012) ("Proposed Order"). The Commission approved a final exemptive order on December 21, 2012, which reflected certain modifications and clarifications to the Proposed Order to address public comments. See Final Exemptive Order Regarding Compliance with Certain Swap Regulations, 78 FR 858 (Jan. 7, 2013) ("January Order").

[18] See 7 U.S.C. 1a(49) (defining the term "swap dealer").

[19] See Further Definition of 'Swap Dealer,' 'Security-Based Swap Dealer,' 'Major Swap Participant,' 'Major Security-Based Swap Participant' and 'Eligible Contract Participant,' 77 FR 30596 (May 23, 2012) ("Final Entities Rules").

would justify registration as a "major swap participant,"[20] as further defined in the Final Entities Rules; and (3) how foreign branches, agencies, affiliates, and subsidiaries of U.S. swap dealers generally should be treated. The Proposed Guidance also generally described the policy and procedural framework under which the Commission would consider compliance with a comparable and comprehensive regulatory requirement of a foreign jurisdiction as a reasonable substitute for compliance with the attendant requirements of the CEA. Last, the Proposed Guidance set forth the manner in which the Commission proposed to interpret section 2(i) of the CEA as it would generally apply to clearing, trading, and certain reporting requirements under the Dodd-Frank Act with respect to swaps between counterparties that are not swap dealers or MSPs.

The public comment period on the Proposed Guidance ended on August 27, 2012. The Commission received approximately 290 comment letters on the Proposed Guidance from a variety of interested parties, including major U.S. and non-U.S. banks and financial institutions that conduct global swap business, trade associations, clearing organizations, law firms (representing international banks and dealers), public interest organizations, and foreign regulators.[21]

---

[20] See 7 U.S.C 1a(33) (defining the term "major swap participant").

[21] The Commission also received approximately 26 comment letters on the Proposed Order. Because the Proposed Guidance and Proposed Order were substantially interrelated, many commenters submitted a single comment letter addressing both proposals. The comment letters submitted in response to the Proposed Order and Proposed Guidance may be found on the Commission's web site at http://comments.cftc.gov/PublicComments/CommentList.aspx?id=1234.

Approximately 200 individuals submitted substantially identical letters to the effect that oversight of the $700 trillion global derivatives market is the key to meaningful reform. The letters state that because the market is inherently global, risks can be transferred around the world with the touch of a button. Further, according to these letters, loopholes in the Proposed Guidance could allow foreign affiliates of Wall Street banks to escape regulation. Lastly, the letters request that the Proposed Guidance be strengthened to ensure that the Dodd-Frank derivatives

The Further Proposed Guidance, issued on December 21, 2012,[22] reflected the Commission's determination that further consideration of public comments regarding the Commission's proposed interpretation of the term "U.S. person," and its proposed guidance regarding aggregation for purposes of swap dealer registration, would be helpful to the Commission in issuing final interpretive guidance. In order to facilitate the Commission's further consideration of these issues, in the Further Proposed Guidance the Commission sought public comment on: (1) an alternative interpretation of the aggregation requirement for swap dealer registration in Commission regulation 1.3(ggg)(4);[23] (2) an alternative "prong" of the proposed interpretation of the term "U.S. person" in the Proposed Guidance which relates to U.S. owners that are responsible for the liabilities of a non-U.S. entity; and (3) a separate alternative prong of the proposed interpretation of the term "U.S. person" which relates to commodity pools and funds with majority-U.S. ownership.

The public comment period on the Further Proposed Guidance ended on February 6, 2013. The Commission received approximately 24 comment letters on the Further Proposed Guidance from interested parties including major U.S. and non-U.S. banks and financial institutions, trade associations, law firms (representing international banks and dealers), public interest organizations, and foreign regulators.[24] With respect to both the Proposed Guidance and the Further Proposed Guidance and throughout the process of considering this Guidance, the

---

protections will directly apply to the full global activities of all important participants in the U.S. derivatives markets.

[22] See Further Proposed Guidance Regarding Compliance With Certain Swap Regulations, 78 FR 909, 913 (Jan. 7, 2013) ("Further Proposed Guidance").

[23] 17 CFR 1.3(ggg)(4). The Commission's regulations are codified at 17 CFR Ch. I.

[24] The comment letters submitted in response to the Further Proposed Guidance are available on the Commission's web site at http://comments.cftc.gov/PublicComments/CommentList.aspx?id=1315.

Commission (and Commission's staff) held numerous meetings and discussions with various market participants, domestic bank regulators, and other interested parties.[25]

Further, the Commission's staff closely consulted with the staff of the SEC in an effort to increase understanding of each other's regulatory approaches and to harmonize the cross-border approaches of the two agencies to the greatest extent possible, consistent with their respective statutory mandates.[26] The Commission is cognizant of the value of harmonization by the Commission and the SEC of their cross-border policies to the fullest extent possible. The staffs of the Commission and the SEC have participated in numerous meetings to work jointly toward this objective. The Commission expects that this consultative process will continue as each agency works towards implementing its respective cross-border policy.

The SEC recently published for public comment proposed rules and interpretive guidance to address the application of the provisions of the Exchange Act, added by Subtitle B of Title VII of the Dodd-Frank Act, that relate to cross-border security-based swap activities.[27] The Commission has considered the SEC's cross-border proposal and has taken it into account in the process of considering this Guidance. The SEC's proposal acknowledges the statutory

---

[25] The records of these meetings and communications are available on the Commission's website at http://www.cftc.gov/LawRegulation/DoddFrankAct/Rulemakings/Cross-BorderApplicationofSwapsProvisions/index.htm.

[26] Sections 722 and 772 of the Dodd-Frank Act establish the scope of the Commission's and SEC's jurisdiction over cross-border swaps and security-based swaps, respectively. CEA section 2(i), which was added by section 722 of the Dodd-Frank Act, is discussed above. Section 30(c) of the Securities Exchange Act of 1934 ("Exchange Act"), which was added by section 772 of the Dodd-Frank Act, provides that the swaps provisions of the Exchange Act added by Title VII do not apply "to any person insofar as such person transacts a business in security-based swaps without the jurisdiction of the United States, unless such person transacts such business in contravention of such rules and regulations as the [SEC] may prescribe as necessary or appropriate to prevent the evasion of any provision [added by Title VII of the Dodd-Frank Act] … " See 15 U.S.C. 78dd(c).

[27] See 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, 78 FR 30968 (May 23, 2013) ("SEC Cross-Border Proposal").

provisions and regulatory precedents that are relevant to security-based swaps by virtue of the fact that security-based swaps are securities.[28] For example, the SEC's proposed rules regarding registration of security-based swap dealers build from the SEC's traditional approach to the registration of brokers and dealers under the Exchange Act.[29] The SEC's proposal also notes the SEC's belief that Congress intended the territorial application of Title VII to entities and transactions in the security-based swaps market to follow similar principles to those applicable to the securities market under the Exchange Act.[30] The Commission believes that one factor in harmonization of the two agencies' approaches is that Congress did not express a similar intent that the application of Title VII to entities and transactions in the swaps market should follow principles that preceded the Dodd-Frank Act, but rather mandated a new regulatory regime for swaps.[31]

The Commission also recognizes the critical role of international cooperation and coordination in the regulation of derivatives in the highly interconnected global market, where risks are transmitted across national borders and market participants operate in multiple jurisdictions. Close cooperative relationships and coordination with other jurisdictions take on

---

[28] The SEC Cross-Border Proposal notes that the definition of "security" in the Exchange Act includes security-based swaps, which raises issues related to the statutory definitions of "broker" and "dealer," the statutory exchange registration requirement, and other statutory requirements related to securities. Id. at 30972.

[29] Id. at 30990.

[30] Id. at 30983-84.

[31] One commenter expressed the view that the SEC's proposed rule is entirely inapplicable to the CFTC's statutory mandate to regulate the risks from cross border derivatives trading and related activities. This commenter stated that the SEC was given very limited statutory authority in the Dodd-Frank Act related solely to anti-evasion, in contrast to the Commission, which was given the same anti-evasion authority plus an affirmative statutory mandate to regulate cross-border derivative activities that "have a direct an significant connection with activities in, or effect on, commerce of the United States." This commenter further stated that a broader statutory mandate makes sense because the Commission "has decades of expertise and jurisdiction for virtually the entire derivatives markets," whereas the SEC has "jurisdiction for no more than 3.5 percent of those markets." See Better Markets Inc. ("Better Markets") (Jun. 24, 2013) at 2.

even greater importance given that, prior to the recent reforms, the swaps market has largely operated without regulatory oversight, and given that many jurisdictions are in differing stages of implementing their regulatory reform. To this end, the Commission's staff has actively engaged in discussions with their foreign counterparts in an effort to better understand and develop a more harmonized cross-border regulatory framework. The Commission expects that these discussions will continue as it implements the cross-border interpretive guidance and as other jurisdictions develop their own regulatory approaches to derivatives.[32]

In general, many of the financial institutions and law firms (representing financial institutions) that commented on the Proposed Guidance and Further Proposed Guidance stated that the Commission's proposed interpretation of the extraterritorial application of Title VII of the Dodd-Frank Act was overly broad and unnecessarily complex and unclear.[33] Among the issues they raised were concerns relating to the interpretation of the term "U.S. person," aggregation for purposes of swap dealer registration, lack of parity in the treatment of foreign branches and affiliates of U.S. persons, the approach to guaranteed non-U.S. affiliates and non-U.S. affiliate "conduits," and the "comparability" assessment for purposes of substituted

---

[32] This is one aspect of the Commission's on-going bilateral and multilateral efforts to promote international coordination of regulatory reform. The Commission's staff is engaged in consultations with Europe, Japan, Hong Kong, Singapore, Switzerland, Canada, Australia, Brazil, and Mexico on derivatives reform. In addition, the Commission's staff is participating in several standard-setting initiatives, co-chairs the IOSCO Task Force on OTC Derivatives, and has created an informal working group of derivatives regulators to discuss implementation of derivatives reform. See also Joint Press Statement of Leaders on Operating Principles and Areas of Exploration in the Regulation of the Cross-border OTC Derivatives Market, published as CFTC Press Release 6439-12, Dec. 4, 2012, available at http://www.cftc.gov/PressRoom/PressReleases/pr6439-12; OTC Derivatives Regulators Group Report to the G-20 Meeting of Finance Ministers and Central Bank Governors of 18-19 April 2013, linked to CFTC Press Release ODRG Report to G-20, Apr. 16, 2013, available at http://www.cftc.gov/PressRoom/PressReleases/odrg_reporttog20release.

[33] See, e.g., Securities Industry and Financial Markets Association ("SIFMA") (Aug. 27, 2012); Institute of International Bankers ("IIB") (Aug. 27, 2012); Sullivan & Cromwell, on behalf of Bank of America Corp., Citi, and J.P. Morgan ("Sullivan & Cromwell") (Aug. 13, 2012); Bank of America Merrill Lynch, Barclays Capital, and PNB Paribas et al., submitted by Cleary Gottlieb Steen & Hamilton LLP ("Cleary") (Aug. 16, 2012).

compliance. The commenters also urged the Commission to allow sufficient time after the publication of the final interpretive guidance for market participants to understand and implement any new policies of the Commission, before the Commission begins to apply such policies.

Other commenters disagreed that the Commission's proposed interpretation of its extraterritorial authority was overly broad, instead arguing that the Commission had not gone far enough.[34] For example, AFR stated that the Proposed Guidance "takes some real positive steps in affirming CFTC jurisdiction over a variety of cross-border transactions," but "falls well short of closing potential cross-border loopholes."[35] Senator Levin wrote that although "members of the financial industry have filed comment letters urging the CFTC to weaken its proposals … American families and businesses deserve strong protections against the risks posed by derivatives trading, including from cross-border swaps, and … the Proposed Guidance should be strengthened rather than weakened."[36]

## II. Scope of this Guidance

After carefully reviewing and considering the comments on the Proposed Guidance and the Further Proposed Guidance, the Commission has determined to finalize the Proposed Guidance. This Guidance sets forth the general policy of the Commission in interpreting how section 2(i) of the CEA provides for the application of the swaps provisions of the CEA and Commission regulations to cross-border activities when such activities have a "direct and

---

[34] See, e.g., Americans for Financial Reform, submitted by Marcus Stanley ("AFR") (Aug. 27, 2012); Better Markets (Aug. 16, 2012); Michael Greenberger, Francis King Cary School of Law, University of Maryland ("Greenberger") (Aug. 13, 2012).

[35] AFR (Aug. 27, 2012) at 2.

[36] Letter from Sen. Levin at 3.

significant connection with activities in, or effect on, commerce of the United States" or when they contravene Commission rulemaking.[37] Unlike a binding rule adopted by the Commission, which would state with precision when particular requirements do and do not apply to particular situations, this Guidance is a statement of the Commission's general policy regarding cross-border swap activities[38] and allows for flexibility in application to various situations, including consideration of all relevant facts and circumstances that are not explicitly discussed in the guidance. The Commission believes that the statement of its policy in this Guidance will assist market participants in understanding how the Commission intends that the registration and certain other substantive requirements of the Dodd-Frank Act generally would apply to their cross-border activities.[39]

This release is intended to inform the public of the Commission's views on how it ordinarily expects to apply existing law and regulations in the cross-border context. In determining the application of the CEA and Commission regulations to particular entities and transactions in cross-border contexts, the Commission will apply the relevant statutory provisions, including CEA section 2(i), and regulations to the particular facts and circumstances. Accordingly, the public has the ability to present facts and circumstances that would inform the application of the substantive policy positions set forth in this release.

---

[37] See 7 U.S.C. 2(i).

[38] The Commission notes that part 23 of its regulations defines "swaps activities" to mean, "with respect to a [registered swap dealer or MSP], such registrant's activities related to swaps and any product used to hedge such swaps, including, but not limited to, futures, options, other swaps or security-based swaps, debt or equity securities, foreign currency, physical commodities, and other derivatives." See 17 CFR 23.200(j); 23.600(a)(7).

[39] In this regard, the Commission notes that it would consider codifying certain aspects of the Guidance in future rulemakings, as appropriate; but at this time, this guidance is intended to provide an efficient and flexible vehicle to communicate the agency's current views on how the Dodd-Frank swap requirements would apply on a cross-border basis.

The Commission understands the complex and dynamic nature of the global swap market and the need to take an adaptable approach to cross-border issues, particularly as it continues to work closely with foreign regulators to address potential conflicts with respect to each country's respective regulatory regime. Although the Commission is issuing the Guidance at this time, the Commission will continue to follow developments as foreign regulatory regimes and the global swaps market continue to evolve. In this regard, the Commission will periodically review this Guidance in light of future developments.

This release is organized into four main sections. Section III sets forth the Commission's interpretation of CEA section 2(i) and the general manner in which it intends to apply the swaps provisions of the Dodd-Frank Act to activities outside the United States. Section IV addresses the public comments and Commission Guidance on: (A) the Commission's interpretation of the term "U.S. person"; (B) swap dealer and MSP registration; (C) the scope of the term "foreign branch" of a U.S. bank and consideration of when a swap should be considered to be with the foreign branch of a U.S. bank; (D) a description of the entity-level requirements and transaction-level requirements under Title VII and the Commission's related regulations ("Entity-Level Requirements" and "Transaction-Level Requirements," respectively); (E) the categorization of Title VII swaps provisions (and Commission regulations) as either Entity-Level or Transaction-Level Requirements; (F) substituted compliance, including an overview of the principles guiding substituted compliance determinations for Entity-Level and Transaction-Level Requirements, a general description of the process for comparability determinations, and a discussion of conflicts arising under foreign privacy and blocking laws; (G) application of the Entity-Level Requirements and "Category A" and "Category B" Transaction-Level Requirements to swap

dealers and MSPs; and (H) application of the CEA's swaps provisions and Commission regulations where both parties to a swap are neither swap dealers nor MSPs.[40]

In addition, this Guidance includes the following Appendices, which should be read in conjunction with (and are qualified by) the remainder of the Guidance: (1) Appendix A – The Entity-Level Requirements; (2) Appendix B – The Transaction-Level Requirements: (3) Appendix C – Application of the Entity-Level Requirements; (4) Appendix D – Application of the Category A Transaction-Level Requirements to Swap Dealers and MSPs; (5) Appendix E – Application of the Category B Transaction-Level Requirements to Swap Dealers and MSPs; and (6) Appendix F – Application of Certain Entity-Level and Transaction-Level Requirements to Non-Swap Dealer/Non-MSP Market Participants.

## III. Interpretation of Section 2(i)

CEA section 2(i) provides that the swaps provisions of Title VII "shall not apply to activities outside the United States unless those activities –

(1) have a direct and significant connection with activities in, or effect on, commerce of the United States; or

(2) contravene such rules or regulations as the Commission may prescribe or promulgate as are necessary or appropriate to prevent the evasion of any provision of [the CEA] that was enacted by the [Dodd-Frank Act]."

In the Proposed Guidance, the Commission noted that section 2(i) provides the Commission express authority over swap activities outside the United States when certain

---

[40] Certain provisions of Title VII apply regardless of whether a swap dealer or MSP is a counterparty to the swap. These provisions include the clearing requirement (7 U.S.C. 2(h)(1)), the trade execution requirement (2(h)(8)), reporting to SDRs (2(a)(13)(G)), and real-time public reporting (2(a)(13)).

conditions are met, but it does not require the Commission to extend its reach to the outer bounds of that authorization. Rather, in exercising its authority with respect to swap activities outside the United States, the Commission will be guided by international comity principles.

### A. Comments

Some commenters addressing the interpretation of section 2(i) in the Proposed Guidance stated that the activities of the non-U.S. branches and subsidiaries of U.S. persons outside the United States with respect to swaps with non-U.S. persons should not be subject to Dodd-Frank requirements. Sullivan & Cromwell asserted that the non-U.S. branches and subsidiaries generally do not enter into swaps with U.S. persons and therefore the jurisdictional nexus with the United States that would justify application of the Dodd-Frank Act is absent.[41] Sullivan & Cromwell stated that there are legitimate business reasons for U.S. persons to establish non-U.S. branches and subsidiaries, so doing so should not be interpreted to mean that the U.S. person is using the branch to evade application of the Dodd-Frank Act.[42] Sullivan & Cromwell argued that the Dodd-Frank Act's application outside the United States should be narrowly construed because it includes only specific exceptions to the judicial precedent that U.S. laws should be interpreted to apply outside the United States only when such application is clearly expressed in the law.[43] Similarly, SIFMA argued that the Commission's proposal asserted a broad jurisdictional scope that is inconsistent with the congressional intent expressed in section 2(i) of the CEA.[44]

---

[41] Sullivan & Cromwell (Aug. 13, 2012) at 6-7.

[42] Id. at 8.

[43] Id. at 9.

[44] SIFMA (Aug. 27, 2012) at 2.

Sullivan & Cromwell cited past instances where the Commission has not applied its regulations to firms that deal solely with foreign customers and do not conduct business in or from the United States or to the non-U.S. subsidiaries of entities registered with the Commission.[45] Sullivan & Cromwell and SIFMA stated that the application of Dodd-Frank requirements to non-U.S. swap activities would be contrary to principles of international comity and cooperation with foreign regulators, would lead to less efficient use of regulatory resources, and would subject the affected entities to potentially conflicting regulations and increased costs of compliance.[46] SIFMA asserted that the jurisdictional scope in the Commission's proposal is not necessary to prevent evasive activity, because the Commission already has broad authority to address evasion.[47] Sullivan & Cromwell and SIFMA also argued that imposing the Dodd-Frank requirements on non-U.S. branches and subsidiaries of U.S. persons would put those entities at a disadvantage compared to competitors in foreign jurisdictions, while other federal laws and banking regulations (such as the Edge Act[48]) indicate that Congress wishes to promote such entities' ability to compete in foreign jurisdictions.[49]

By contrast, Senator Levin stated that the J.P. Morgan "whale trades" provide an example of how major U.S. financial institutions have integrated their U.S. and non-U.S. swap activities, and therefore supports the application of the swaps provisions of Title VII and Commission

---

[45] Sullivan & Cromwell (Aug. 13, 2012) at 10.

[46] Id. at 11; SIFMA (Aug. 27, 2012) at 3 and A55.

[47] SIFMA (Aug. 27, 2012) at 3.

[48] 12 U.S.C. 611-31.

[49] Id.; Sullivan & Cromwell (Aug. 13, 2012) at 12-14.

regulations to the non-U.S. offices of U.S. financial institutions.[50] He explained that a Senate investigation found that J.P. Morgan personnel in London executed the "whale trades" using money from the U.S. bank's excess deposits, and while traders in London conducted the trades, the trades were attributed to a U.S. affiliate of J.P. Morgan through back-to-back arrangements between the London branch and New York branch.[51] He also stated the whale trades were entered into with counterparties including major U.S. banks and J.P. Morgan's own investment bank.[52] Senator Levin concluded that because of the integration of U.S. and non-U.S. offices and affiliates of U.S. financial institutions, it is critical that the non-U.S. offices and affiliates of U.S. financial institutions follow the same Dodd-Frank requirements as are applicable to the U.S. financial institutions.[53]

### B. Statutory Analysis

In interpreting the phrase "direct and significant," the Commission has examined the plain language of the statutory provision, similar language in other statutes with cross-border application, and the legislative history of section 2(i).

The statutory language in new CEA section 2(i) is structured similarly to the statutory language in the Foreign Trade Antitrust Improvements Act of 1982 (the "FTAIA"),[54] which provides the standard for the cross-border application of the Sherman Antitrust Act.[55] The

---

[50] Letter from Sen. Levin at 4.

[51] Id.

[52] Id.

[53] Id. at 7. See also Dodd-Frank Statement ("An exemption for foreign derivatives activity by the [] affiliates of American institutions is a free pass no matter where that activity is located.").

[54] 15 U.S.C. 6a.

[55] 15 U.S.C. 1-7.

FTAIA, like CEA section 2(i), excludes certain non-U.S. commercial transactions from the reach of U.S. law. It provides that the antitrust provisions of the Sherman Act "shall not apply to [anti-competitive] conduct involving trade or commerce … with foreign nations."[56] However, like paragraph (1) of CEA section 2(i), the FTAIA also creates exceptions to the general exclusionary rule and thus brings back within antitrust coverage any conduct that: (1) has a "direct, substantial, and reasonably foreseeable effect" on U.S. commerce;[57] and (2) "such effect gives rise to a [Sherman Act] claim."[58] In F. Hoffman-LaRoche, Ltd. v. Empagran S.A., the Supreme Court stated that "this technical language initially lays down a general rule placing all (nonimport) activity involving foreign commerce outside the Sherman Act's reach. It then brings such conduct back within the Sherman Act's reach provided that the conduct both (1) sufficiently affects American commerce, i.e., it has a 'direct, substantial, and reasonably foreseeable effect' on American domestic, import, or (certain) export commerce, and (2) has an effect of a kind that antitrust law considers harmful, i.e., the 'effect' must 'giv[e] rise to a [Sherman Act] claim.'"[59]

It is appropriate, therefore, to read section 2(i) of the CEA as a clear expression of congressional intent that the swaps provisions of Title VII of the Dodd-Frank Act apply to activities beyond the borders of the United States when certain circumstances are present. These circumstances include, pursuant to paragraph (1) of section 2(i), when activities outside the

---

[56] 15 U.S.C. 6a.

[57] 6a(1).

[58] 6a(2).

[59] 542 U.S. 155, 162 (2004) (emphasis in original).

United States meet the statutory test of having a "direct and significant connection with activities in, or effect on," U.S. commerce.

An examination of the language in the FTAIA, however, does not provide an unambiguous roadmap for the Commission in interpreting section 2(i) of the CEA. There are both similarities, and a number of significant differences, between the language in CEA section 2(i) and the language in the FTAIA. Further, the Supreme Court has not provided definitive guidance as to the meaning of the "direct, substantial, and reasonably foreseeable" test in the FTAIA, and the lower courts have interpreted the individual terms in the FTAIA differently.

Although a number of courts have interpreted the various terms in the FTAIA, only the term "direct" appears in both CEA section 2(i) and the FTAIA. Relying upon the Supreme Court's definition of the term "direct" in the Foreign Sovereign Immunities Act ("FSIA"),[60] the U.S. Court of Appeals for the Ninth Circuit construed the term "direct" in the FTAIA as requiring a "relationship of logical causation,"[61] such that "an effect is 'direct' if it follows as an immediate consequence of the defendant's activity."[62] However, in an en banc decision, the U.S. Court of Appeals for the Seventh Circuit held that "the Ninth Circuit jumped too quickly on the assumption that the FSIA and the FTAIA use the word 'direct' in the same way."[63] After

---

[60] See 28 U.S.C. 1605(a)(2).

[61] United States v. LSL Biotechnologies, 379 F.3d 672, 693 (9th Cir. 2004). "As a threshold matter, many courts have debated whether the FTAIA established a new jurisdictional standard or merely codified the standard applied in [United States v. Aluminum Co. of Am., 148 F.2d 416 (2d Cir. 1945)] and its progeny. Several courts have raised this question without answering it. The Supreme Court did as much in [Harford Fire Ins. Co. v. California, 509 U.S. 764 (1993)]." Id. at 678.

[62] Id. at 692-3, quoting Republic of Argentina v. Weltover, Inc., 504 U.S. 607, 618 (1992) (providing that, pursuant to the FSIA, 28 U.S.C. 1605(a)(2), immunity does not extend to commercial conduct outside the United States that "causes a direct effect in the United States").

[63] Minn-Chem, Inc. v. Agrium, Inc., 683 F.3d 845, 857 (7th Cir. 2012) (en banc).

examining the text of the FTAIA as well as its history and purpose, the Seventh Circuit found persuasive the "other school of thought [that] has been articulated by the Department of Justice's Antitrust Division, which takes the position that, for FTAIA purposes, the term 'direct' means only 'a reasonably proximate causal nexus.'"[64] The Seventh Circuit rejected interpretations of the term "direct" that included any requirement that the consequences be foreseeable, substantial, or immediate.[65]

Other terms in the FTAIA differ from the terms used in section 2(i) of the CEA. First, the FTAIA test explicitly requires that the effect on U.S. commerce be a "reasonably foreseeable" result of the conduct.[66] Section 2(i) of the CEA, by contrast, does not provide that the effect on U.S. commerce must be foreseeable. Second, whereas the FTAIA solely relies on the "effects" on U.S. commerce to determine cross-border application of the Sherman Act, section 2(i) of the CEA refers to both "effect" and "connection." "The FTAIA says that the Sherman Act applies to foreign 'conduct' with a certain kind of harmful domestic effect."[67] Section 2(i), by contrast, applies more broadly – not only to particular instances of conduct that have an effect on U.S. commerce, but also to activities that have a direct and significant "connection with activities in" U.S. commerce. Unlike the FTAIA, section 2(i) applies the swaps provisions of the CEA to activities outside the United States that have the requisite

---

[64] Id.

[65] Id. at 856-57.

[66] See, e.g., Animal Sciences Products. v. China Minmetals Corp., 654 F.3d 462, 471 (3d Cir. 2011) ("[T]he FTAIA's 'reasonably foreseeable' language imposes an objective standard: the requisite 'direct' and 'substantial' effect must have been 'foreseeable' to an objectively reasonable person.").

[67] Hoffman-LaRoche, 452 U.S. at 173.

connection with activities in U.S. commerce, regardless of whether a "harmful domestic effect" has occurred.

As the foregoing textual analysis indicates, Congress crafted section 2(i) differently from its analogue in the antitrust laws. Congress delineated the cross-border scope of the Sherman Act in section 6a of the FTAIA as applying to conduct that has a "direct" and "substantial" and "reasonably foreseeable" "effect" on U.S. commerce. In section 2(i), on the other hand, Congress did not include a requirement that the effects or connections of the activities outside the United States be "reasonably foreseeable" for the Dodd-Frank swaps provisions to apply. Further, Congress included language in section 2(i) to apply the Dodd-Frank swaps provisions in circumstances in which there is a direct and significant connection with activities in U.S. commerce, regardless of whether there is an effect on U.S. commerce. The different words that Congress used in paragraph (1) of section 2(i), as compared to its closest statutory analogue in section 6a of the FTAIA, inform the Commission in construing the boundaries of its cross-border authority over swap activities under the CEA.[68] Accordingly, the Commission believes it is appropriate to interpret section 2(i) such that it applies to activities outside the United States in circumstances in addition to those that would be reached under the FTAIA standard.

As further described in the Proposed Guidance, one of the principal rationales for the enactment of the Dodd-Frank derivatives reforms was the need for a comprehensive scheme of

---

[68] The provision that ultimately became section 722(d) of the Dodd-Frank Act was added during consideration of the legislation in the House of Representatives. See 155 Cong. Rec. H14685 (Dec. 10, 2009). The version of what became Title VII that was reported by the House Agriculture Committee and the House Financial Services Committee did not include any provision addressing cross-border application. See 155 Cong. Rec. H14549 (Dec. 10, 2009). The Commission finds it significant that, in adding the cross-border provision before final passage, the House did so in terms that, as discussed in text, were different from, and broader than, the terms used in the analogous provision of the FTAIA.

regulation to prevent systemic risk in the U.S. financial system.[69] More particularly, a primary purpose of Title VII of the Dodd-Frank Act is to address risk to the U.S. financial system created by interconnections in the swaps market.[70] Title VII of the Dodd-Frank Act gave the Commission new and broad authority to regulate the swaps market to address and mitigate risks arising from swap activities that in the future could cause a financial crisis.

In global markets, the source of such risk is not confined to activities within U.S. borders. Due to the interconnectedness between firms, traders, and markets in the U.S. and abroad, a firm's failure, or trading losses overseas, can quickly spill over to the United States and affect activities in U.S. commerce and the stability of the U.S. financial system. Accordingly, Congress did not limit the application of the Dodd-Frank Act to activities within the United States. Rather, in recognition of the global nature of the swaps market, and the fact that risks to the U.S. financial system may arise from activities outside the United States, as well as from activities within the United States, Congress explicitly provided for cross-border application of Title VII to activities outside the United States that pose risks to the U.S. financial system.[71]

---

[69] See Proposed Guidance, 77 FR at 41215-16.

[70] Cf. 156 Cong. Rec. S5818 (July 14, 2010) (statement of Sen. Lincoln) ("In 2008, our Nation's economy was on the brink of collapse. America was being held captive by a financial system that was so interconnected, so large, and so irresponsible that our economy and our way of life were about to be destroyed."), available at http://www.gpo.gov/fdsys/pkg/CREC-2010-07-14/pdf/CREC-2010-07-14.pdf; 156 Cong. Rec. S5888 (July 15, 2010) (statement of Sen. Shaheen) ("We need to put in place reforms to stop Wall Street firms from growing so big and so interconnected that they can threaten our entire economy."), available at http://www.gpo.gov/fdsys/pkg/CREC-2010-07-15/pdf/CREC-2010-07-15-senate.pdf; 156 Cong. Rec. S5905 (July 15, 2010) (statement of Sen. Stabenow) ("For too long the over-the-counter derivatives market has been unregulated, transferring risk between firms and creating a web of fragility in a system where entities became too interconnected to fail."), available at http://www.gpo.gov/fdsys/pkg/CREC-2010-07-15/pdf/CREC-2010-07-15-senate.pdf.

[71] The legislative history of the Dodd-Frank Act shows that in the fall of 2009, neither the Over-the-Counter Derivatives Markets Act of 2009, H.R. 3795, 111th Cong. (1st Sess. 2009), reported by the Financial Services Committee chaired by Rep. Barney Frank, nor the Derivatives Markets Transparency and Accountability Act of 2009, H.R. 977, 111th Cong. (1st Sess. 2009), reported by the Agriculture Committee chaired by Rep. Collin

Therefore, upon consideration of the statutory language, as well as the prophylactic purpose of the CEA and the amendments made to it by Title VII, the Commission construes section 2(i) to apply the swaps provisions of the CEA to activities outside the United States that have either: (1) a direct and significant effect on U.S. commerce; or, in the alternative, (2) a direct and significant connection with activities in U.S. commerce, and through such connection present the type of risks to the U.S. financial system and markets that Title VII directed the Commission to address. The Commission interprets section 2(i) in a manner consistent with the overall goals of the Dodd-Frank Act to reduce risks to the U.S. financial system and avoid future financial crises.[72]

Consistent with this overall interpretation, the Commission believes that the term "direct" in CEA section 2(i) should be interpreted in a manner consistent with the position of the Department of Justice Antitrust Division with respect to the meaning of the same term in the FTAIA, and as recently adopted by the Seventh Circuit.[73] The Commission therefore interprets

---

Peterson, included a general territoriality limitation that would have restricted Commission regulation of transactions between two foreign persons located outside of the United States. During the House Financial Services Committee markup on October 14, 2009, Rep. Spencer Bachus offered an amendment that would have restricted the jurisdiction of the Commission over swaps between non-U.S. resident persons transacted without the use of the mails or any other means or instrumentality of interstate commerce. Chairman Frank opposed the amendment, noting that there may well be cases where non-U.S. residents are engaging in transactions that have an effect on the United States and that are insufficiently regulated internationally and that he would not want to prevent U.S. regulators from stepping in. Chairman Frank expressed his commitment to work with Rep. Bachus going forward, and Rep. Bachus withdrew the amendment. See H. Fin. Serv. Comm. Mark Up on Discussion Draft of the Over-the-Counter Derivatives Markets Act of 2009, 111th Cong., 1st Sess. (Oct. 14, 2009) (statements of Rep. Bachus and Rep. Frank), available at http://financialservices.house.gov/calendar/eventsingle.aspx?EventID=231922.

[72] The Commission also notes that the Supreme Court has indicated that the FTAIA may be interpreted more broadly when the government is seeking to protect the public from anticompetitive conduct than when a private plaintiff brings suit. See Hoffman-LaRoche, 452 U.S. at 170 ("A Government plaintiff, unlike a private plaintiff, must seek to obtain the relief necessary to protect the public from further anticompetitive conduct and to redress anticompetitive harm. And a Government plaintiff has legal authority broad enough to allow it to carry out its mission.").

[73] See note 63 and accompanying text, supra.

the term "direct" in section 2(i) so as to require "a reasonably proximate causal nexus" and not to require foreseeability, substantiality, or immediacy.[74]

Consistent with the purpose of Title VII to protect the U.S. financial system against the build-up of systemic risks, the Commission does not read section 2(i) so as to require a transaction-by-transaction determination that a specific swap outside the United States has a "direct and significant connection with activities in, or effect on, commerce of the United States" in order to apply the swaps provisions of the CEA to such transactions. Rather, it is the connection of swap activities, viewed as a class or in the aggregate, to activities in commerce of the United States that must be assessed to determine whether application of the CEA swaps provisions is warranted.[75]

This conclusion is bolstered by similar interpretations of other federal statutes regulating interstate commerce. Recently, the Supreme Court reaffirmed a similar "aggregate effects" approach in Nat'l Fed'n of Indep. Bus. v. Sebelius.[76] In that case, the Court phrased the holding

---

[74] The Seventh Circuit's rationale for rejecting the Ninth Circuit's interpretation applies with at least equal, if not greater, force to the interpretation of the word "direct" in section 2(i) of the CEA. As discussed in note 68 and the accompanying text, supra, Congress expressly declined to import the FTAIA standards of substantiality, immediacy, or foreseeability into section 2(i). The Commission believes that the terms included in section 2(i) that are the same as the terms in the FTAIA should be interpreted in a manner consistent with Congress's determination to not import other, different standards from the FTAIA into section 2(i). Where Congress has included in a new statute one term but not another from an existing statute, it is reasonable to conclude that Congress did not want the other existing standards included in the new statute.

[75] The Commission believes this interpretation is supported by Congress's use of the plural term "activities" in CEA section 2(i), rather than the singular term "activity." The Commission believes it is reasonable to interpret the use of the plural term "activities" in section 2(i) to require not that each particular activity have the requisite connection with U.S. commerce, but rather that such activities in the aggregate, or a class of activity, have the requisite nexus with U.S. commerce. This interpretation is consistent with the overall objectives of Title VII, as described above. Further, the Commission believes that a swap-by-swap approach to jurisdiction would be "too complex to prove workable." See Hoffman-LaRoche, 542 U.S. at 168.

[76] 132 S. Ct. 2566 (2012).

in the seminal "aggregate effects" decision, Wickard v. Filburn,[77] in this way: "[The farmer's] decision, when considered in the aggregate along with similar decisions of others, would have had a substantial effect on the interstate market for wheat."[78] In another recent case, Gonzales v Raich,[79] the Court adopted similar reasoning to uphold the application of the Controlled Substance Act[80] to prohibit the intrastate use of medical marijuana for medicinal purposes. In Raich, the Court held that Congress could regulate purely intrastate activity if the failure to do so would "leave a gaping hole" in the federal regulatory structure. These cases support the Commission's cross-border authority over swap activities that as a class, or in the aggregate, have a direct and significant connection with activities in, or effect on, U.S. commerce – whether or not an individual swap may satisfy the statutory standard.[81]

### C. Principles of International Comity

The case law in the antitrust area also teaches the importance of recognizing the laws and interests of other countries in applying an ambiguous federal statute across borders; in such circumstances, principles of international comity counsel courts and agencies to act reasonably in exercising jurisdiction with respect to activity that takes place elsewhere. In Hoffman-LaRoche,

---

[77] 317 U.S. 111 (1942).

[78] 132 S. Ct. 2566, 2588 (2012). At issue in Wickard was the regulation of a farmer's production and use of wheat even though the wheat was "not intended in any part for commerce but wholly for consumption on the farm." 317 U.S. at 118. The Supreme Court upheld the application of the regulation, stating that although the farmer's "own contribution to the demand for wheat may be trivial by itself," the federal regulation could be applied when his contribution "taken together with that of many others similarly situated, is far from trivial." Id. at 128-29. The Court also stated it had "no doubt that Congress may properly have considered that wheat consumed on the farm where grown, if wholly outside the scheme of regulation, would have a substantial effect in defeating and obstructing its purpose …." Id.

[79] 545 U.S. 1 (2005).

[80] 21 U.S.C. 801 et seq.

[81] In Sebelius, the Court stated, "Where the class of activities is regulated, and that class is within the reach of federal power, the courts have no power to excise, as trivial, individual instances of the class." 132 S. Ct. at 2587 (quoting Perez v. United States, 402 U.S. 146, 154 (1971).

an antitrust class action lawsuit alleging an international price-fixing conspiracy by foreign and domestic vitamin manufacturers and distributors, the Supreme Court held that ambiguous statutes should be construed to "avoid unreasonable interference with the sovereign authority of other nations."[82] The Court explained that this rule of construction "reflects customary principles of international law" and "helps the potentially conflicting laws of different nations work together in harmony – a harmony particularly needed in today's highly interdependent commercial world."[83]

In determining whether the exercise of jurisdiction by one nation over activities in another nation would be reasonable, the courts and agencies are guided by the Restatement (Third) of Foreign Relations Law of the United States (the "Restatement"). Drawing upon traditional principles of international law, the Restatement provides bases of jurisdiction to prescribe law, as well as limitations on the exercise of jurisdiction. In addition to recognizing territoriality and nationality as bases for jurisdiction, the Restatement expressly provides that a country has jurisdiction to prescribe law with respect to "conduct outside its territory that has or is intended to have substantial effect within its territory."[84]

The Restatement also provides that even where a country has a basis for jurisdiction, it should not prescribe law with respect to a person or activity in another country when the exercise of such jurisdiction is unreasonable.[85] The reasonableness of such an exercise of jurisdiction, in

---

[82] 542 U.S. at 164.

[83] Id. at 165.

[84] See Restatement § 402(1)(c). A comment to the Restatement also identifies jurisdiction with respect to activity outside the country, but having or intended to have substantial effect within the country's territory, as an aspect of jurisdiction based on territoriality. See Restatement § 402 cmt. d.

[85] Restatement § 403(1).

turn, is to be determined by evaluating all relevant factors, including certain specifically enumerated factors where appropriate:

> (a) the link of the activity to the territory of the regulating state, i.e., the extent to which the activity takes place within the territory, or has substantial, direct, and foreseeable effect upon or in the territory;
>
> (b) the connections, such as nationality, residence, or economic activity, between the regulating state and the persons principally responsible for the activity to be regulated, or between that state and those whom the regulation is designed to protect;
>
> (c) the character of the activity to be regulated, the importance of regulation to the regulating state, the extent to which other states regulate such activities, and the degree to which the desirability of such regulation is generally accepted;
>
> (d) the existence of justified expectations that might be protected or hurt by the regulation;
>
> (e) the importance of the regulation to the international political, legal, or economic system;
>
> (f) the extent to which the regulation is consistent with the traditions of the international system;
>
> (g) the extent to which another state may have an interest in regulating the activity; and
>
> (h) the likelihood of conflict with regulation by another state. [86]

Notably, the Restatement does not preclude concurrent regulation by multiple jurisdictions. However, where concurrent jurisdiction by two or more jurisdictions creates conflict, the Restatement recommends that each country evaluate both its interests in exercising jurisdiction and those of the other jurisdiction, and where possible, to consult with each other.[87]

---

[86] Restatement § 403(2).

[87] With regard to conflicting exercises of jurisdiction, section 403(3) of the Restatement states:

> (3) When it would not be unreasonable for each of the two states to exercise jurisdiction over a person or activity, but the prescriptions by the two states are in conflict, each state has an obligation to evaluate its own as well as the other state's interest in exercising jurisdiction, in light of all the relevant factors, including those set out in Subsection (2), a state should defer to the other state if that state's interest is clearly greater.

Comment e. to section 403 of the Restatement states:

Consistent with the Restatement, in determining the extent to which the Dodd-Frank swaps provisions apply to activities abroad, the Commission has strived to protect U.S. interests as determined by Congress in Title VII, and minimize conflicts with the laws of other jurisdictions. The Commission has carefully considered, among other things, the level of the home jurisdiction's supervisory interests over the subject activity and the extent to which the activity takes place within the foreign territory.[88] At the same time, the Commission has also considered the potential for cross-border activities to have substantial connection to or impact on the U.S. financial system and the global, highly integrated nature of today's swap business; to fulfill the purposes of the Dodd-Frank swaps reform, the Commission's supervisory oversight cannot be confined to activities strictly within the territory of the United States.

The Commission believes that the Guidance strikes the proper balance between these competing factors to ensure that the Commission can discharge its responsibilities to protect the U.S. markets, market participants, and financial system, consistent with the traditions of the international system and comity principles, as set forth in the Restatement. Of particular

---

> *Conflicting exercises of jurisdiction.* Subsection (3) applies when an exercise of jurisdiction by each of two states is not unreasonable, but their regulations conflict. In that case, each state is required to evaluate both its interests in exercising jurisdiction and those of the other state. When possible, the two states should consult with each other. If one state has a clearly greater interest, the other should defer, by abandoning its regulation or interpreting or modifying it so as to eliminate the conflict. When neither state has a clearly stronger interest, states often attempt to eliminate the conflict so as to reduce international friction and avoid putting those who are the object of the regulations in a difficult situation. Subsection (3) is addressed primarily to the political departments of government, but it may be relevant also in judicial proceedings.
>
> Subsection (3) applies only when one state requires what another prohibits, or where compliance with the regulations of two states exercising jurisdiction consistently with this section is otherwise impossible. It does not apply where a person subject to regulation by two states can comply with the laws of both; for example, where one state requires keeping accounts on a cash basis, the other on an accrual basis. It does not apply merely because one state has a strong policy to permit or encourage an activity which another state prohibits, or one state exempts from regulation an activity which another regulates. Those situations are governed by Subsection (2), but do not constitute conflict within Subsection (3).

[88] For purposes of this Guidance, the terms "home jurisdiction" or "home country" are used interchangeably and refer to the jurisdiction in which the person or entity is established, including the European Union.

relevance is the Commission's approach to substituted compliance, which would be expected to mitigate any burden associated with potentially conflicting foreign regulations and would generally be appropriate in light of the supervisory interests of foreign regulators in entities domiciled and operating in its jurisdiction.[89]

In addition, recognizing that close cooperation and coordination with other jurisdictions is vital to the regulation of derivatives in the highly interconnected global market, the Commission's staff expects to remain actively engaged in discussions with foreign regulators as the Commission implements the cross-border interpretive guidance and as other jurisdictions develop their own regulatory requirements for derivatives. The Commission recognizes that conflicts of law may exist and is ready to address those issues as they may arise. In that regard, where a real conflict of laws exists, the Commission strongly encourages regulators and registrants to consult directly with its staff.

## IV. Guidance

### A. Interpretation of the Term "U.S. Person"

#### 1. Proposed Interpretation

Under the Proposed Guidance, the term "U.S. person" identifies those persons who, under the Commission's interpretation, could be expected to satisfy the jurisdictional nexus under section 2(i) of the CEA based on their swap activities either individually or in the

---

[89] As discussed in section IV.F, infra, the Commission's recognition of substituted compliance would be based on an evaluation of whether the requirements of the foreign jurisdiction are comparable and comprehensive compared to the applicable requirement(s) under the CEA and Commission regulations, based on a consideration of all relevant factors, including among other things: (i) the comprehensiveness of the foreign regulator's supervisory compliance program, and (ii) the authority of such foreign regulator to support and enforce its oversight of the registrant's branch or agency with regard to such activities to which substituted compliance applies.

aggregate.[90] As proposed, the Commission's interpretation of the term "U.S. person" would generally encompass: (1) persons (or classes of persons) located within the United States; and (2) persons that may be domiciled or operate outside the United States but whose swap activities nonetheless have a "direct and significant connection with activities in, or effect on, commerce of the United States" within the meaning of CEA section 2(i).

Specifically, as set forth in the Proposed Guidance, the Commission's interpretation of the term "U.S. person" would generally include, but not be limited to:

(i) any natural person who is a resident of the United States;

(ii) any corporation, partnership, limited liability company, business or other trust, association, joint-stock company, fund or any form of enterprise similar to any of the foregoing, in each case that is either (A) organized or incorporated under the laws of the United States or having its principal place of business in the United States (legal entity) or (B) in which the direct or indirect owners thereof are responsible for the liabilities of such entity and one or more of such owners is a U.S. person;

(iii) any individual account (discretionary or not) where the beneficial owner is a U.S. person;

(iv) any commodity pool, pooled account, or collective investment vehicle (whether or not it is organized or incorporated in the United States) of which a majority ownership is held, directly or indirectly, by a U.S. person(s);

---

[90] See Proposed Guidance, 77 FR at 41218. The discussion of the term "U.S. person" in this Guidance is limited to the relevance of this term for purposes of the Commission regulations promulgated under Title VII. The Commission does not intend that this discussion would apply to other uses of the term "person" in the CEA.

(v) any commodity pool, pooled account, or collective investment vehicle the operator of which would be required to register as a commodity pool operator under the CEA;

(vi) a pension plan for the employees, officers or principals of a legal entity with its principal place of business inside the United States; and

(vii) an estate or trust, the income of which is subject to U.S. income tax regardless of source.

Under the proposed interpretation, a "U.S. person" would include a foreign branch of a U.S. person; on the other hand, a non-U.S. affiliate guaranteed by a U.S. person would not be within the Commission's interpretation of the term "U.S. person."

The Further Proposed Guidance included alternatives for two "prongs" of the proposed interpretation of the term "U.S. person" in the Proposed Guidance: prong (ii)(B), which relates to U.S. owners that are responsible for the liabilities of a non-U.S. entity; and prong (iv), which relates to commodity pools and funds with majority-U.S. ownership.

The alternative version of prong (ii)(B) in the Further Proposed Guidance would limit its scope to a non-U.S. legal entity that is directly or indirectly majority-owned by one or more natural persons or legal entities that meet prong (i) or (ii) of the interpretation, in which such U.S. person(s) bears unlimited responsibility for the obligations and liabilities of the legal entity. This alternative prong (ii)(B) would generally not include an entity that is a corporation, limited liability company or limited liability partnership where shareholders, members or partners have limited liability. Further, the Commission stated in the Further Proposed Guidance that the majority-ownership criterion would be intended to avoid capturing those legal entities that have negligible U.S. ownership interests. Unlimited liability corporations where U.S. persons have

majority ownership and where such U.S. persons have unlimited liability for the obligations and liabilities of the entity generally would be covered under this alternative to prong (ii)(B).

The alternative prong (ii)(B) in the Further Proposed Guidance was as follows:

(ii) A corporation, partnership, limited liability company, business or other trust, association, joint-stock company, fund or any form of enterprise similar to any of the foregoing, in each case that is either (A) organized or incorporated under the laws of a state or other jurisdiction in the United States or having its principal place of business in the United States or (B) directly or indirectly majority-owned by one or more persons described in prong (i) or (ii)(A) and in which such person(s) bears unlimited responsibility for the obligations and liabilities of the legal entity (other than a corporation, limited liability company or limited liability partnership where shareholders, members or partners have limited liability);

The Further Proposed Guidance explained that this alternative proposed prong would generally treat an entity as a U.S. person if one or more of its U.S. majority owners has unlimited responsibility for losses of, or nonperformance by, the entity. This prong would reflect that when the structure of an entity is such that the U.S. direct or indirect owners are ultimately liable for the entity's obligations and liabilities, the connection to activities in, or effect on, U.S. commerce would be expected to satisfy the requisite jurisdictional nexus. This "look-through" requirement also would serve to discourage persons from creating such indirect ownership structures for the purpose of engaging in activities outside of the Dodd-Frank regulatory regime. Under the Further Proposed Guidance, this alternative proposed prong generally would not render a legal entity organized or domiciled in a foreign jurisdiction a "U.S. person" simply because the entity's swaps obligations are guaranteed by a U.S. person.

With respect to prong (iv) of the interpretation of the term "U.S. person" in the Proposed Guidance, the Further Proposed Guidance set forth an alternative under which any commodity pool, pooled account, investment fund or other collective investment vehicle generally would be within the interpretation of the term "U.S. person" if it is (directly or indirectly) majority-owned by one or more natural persons or legal entities that meet prong (i) or (ii) of the interpretation of the term "U.S. person." The Further Proposed Guidance explained that for purposes of this alternative prong (iv), the Commission would interpret "majority-owned" to mean the beneficial ownership of more than 50 percent of the equity or voting interests in the collective investment vehicle. Similar to the alternative prong (ii)(B) discussed above, the Commission generally would not interpret the collective investment vehicle's place of organization or incorporation to be determinative of its status as a U.S. person. The Further Proposed Guidance clarified that under alternative prong (iv), the Commission would interpret the term "U.S. person" to include a pool, fund, or other collective investment vehicle that is publicly traded only if it is offered, directly or indirectly, to U.S. persons.

The alternative prong (iv) in the Further Proposed Guidance was as follows:

(iv) A commodity pool, pooled account, investment fund, or other collective investment vehicle that is not described in prong (ii) and that is directly or indirectly majority-owned by one or more persons described in prong (i) or (ii), except any commodity pool, pooled account, investment fund, or other collective investment vehicle that is publicly-traded but not offered, directly or indirectly, to U.S. persons;

The Further Proposed Guidance explained that this alternative proposed prong (iv) is intended to capture collective investment vehicles that are created for the purpose of pooling

assets from U.S. investors and channeling these assets to trade or invest in line with the objectives of the U.S. investors, regardless of the place of the vehicle's organization or incorporation. These collective investment vehicles may serve as a means to achieve the investment objectives of their beneficial owners, rather than being separate, active operating businesses. As such, the beneficial owners would be directly exposed to the risks created by the swaps that their collective investment vehicles enter into.

2. **Comments**

In general, commenters stated that the proposed "U.S. person" interpretation presented significant interpretive issues and implementation challenges.[91] The commenters contended that it would be difficult to determine U.S. person status because of the breadth of the proposed interpretation, potential ambiguities it contains, and the collection of information its application may require. The commenters, therefore, urged the Commission to consider how the proposed interpretation could be stated in a simpler and more easily applied manner.[92] While a number of commenters stated that the Commission's construction of the term "U.S. person" in the Proposed Guidance was overbroad,[93] several commenters on the Further Proposed Guidance advocated for a broader reading of the term than any of those proposed by the Commission.[94]

---

[91] See SIFMA (Aug. 27, 2012) at 5; Societe Generale ("SocGen") (Aug. 8, 2012) at 4; IIB (Aug. 27, 2012) at 4-14; Deutsche Bank AG ("Deutsche Bank") (Aug. 27, 2012) at 1-4; Goldman Sachs "(Goldman") (Aug. 27, 2012) at 3; The Hong Kong Association of Banks ("Hong Kong Banks") (Aug. 27, 2012) at 3-4; Australian Bankers' Association Inc. ("Australian Bankers") (Aug. 27, 2012) at 4.

[92] SIFMA (August 27, 2012) at A10.

[93] See, e.g., European Commission (Aug. 24, 2012) at 1-2; Hong Kong Banks (Aug. 27, 2012) at 4; J.P. Morgan (Aug. 13, 2012) at 9.

[94] See Better Markets (Feb. 15, 2013) at 4-8; Michael Greenberger and Brandy Bruyere, University of Maryland, and AFR ("Greenberger/AFR") (Feb. 6, 2013) at 3 (stating that none of the definitions of U.S. person proposed by the CFTC are sufficient to protect U.S. taxpayers from the risks of foreign subsidiaries and affiliates of U.S. financial institutions). See also Letter from Sen. Levin at 7-8.

### a. Phase-in Interpretation

A number of commenters requested that the Commission adopt an interim interpretation of "U.S. person" that would allow firms to rely on their existing systems and classifications and avoid the need to develop systems to follow a temporary interpretation of the term "U.S. person" that may change in the near future.[95] IIB explained that applying any interpretation of "U.S. person" that departs from status based on residence or jurisdiction of organization, and in some cases principal place of business, will require sufficient time to implement relevant documentation conventions and diligence procedures.[96] IIB, therefore, requested that the Commission implement a phased-in approach to the "U.S. person" interpretation that would encompass, in general, (1) a natural person who is a U.S. resident and (2) a corporate entity that is organized or incorporated under the laws of the United States or has its place of business in the United States.[97]

SIFMA also urged the Commission to phase in the "U.S. person" interpretation, citing the implementation difficulties identified by IIB. Specifically, SIFMA recommended that the Commission allow market participants to apply an interim interpretation of "U.S. person" until 90 days after the final interpretation of "U.S. person" is published.[98] SIFMA stated that the interim interpretation – which was identical to IIB's interim interpretation – should identify "core" U.S. persons and would allow its members to phase in compliance with the Dodd-Frank

---

[95] See, e.g., Cleary (Aug. 16, 2012) at 6; SIFMA (Aug. 27, 2012) at A8-9; IIB (Aug. 9, 2012) at 4; Deutsche Bank (Aug. 13, 2012) at 2; State Street Corporation ("State Street") (Aug. 27, 2012) at 2; Goldman (Aug. 27. 2012) at 3.

[96] See IIB (Aug. 9, 2012) at 4.

[97] For purposes of IIB's definition, a foreign branch of a U.S. swap dealer would be considered a non-U.S. person. IIB added that it believes that the Commission should adopt a final definition of "U.S. person" that is consistent with its proposed interim definition. Id.

[98] See SIFMA (Aug. 25, 2012) at A8.

requirements without building new systems that might have to be changed when the Commission states a final interpretation of the term.[99]

**b. Comments on Particular Prongs of the Proposed Interpretation of the Term "U.S. Person"**

Commenters' concerns were primarily (though not exclusively) directed to three prongs of the proposed "U.S. person" interpretation: prong (ii)(B) relating to U.S. owners that are responsible for the liabilities of a non-U.S. company; prong (iv) relating to commodity pools and funds with majority-U.S. ownership; and prong (v) relating to registered commodity pool operators. Below, the Commission describes the main comments to all the prongs of the proposed interpretation of "U.S. person" in greater detail.

Commenters generally did not comment on prong (i).

With respect to prong (ii)(A), the Investment Industry Association of Canada (IIAC) stated that the Commission should look to the location of a legal entity's management (or the majority of its directors and executive officers), instead of the location of organization.[100] Two commenters stated that the "principal place of business" element of the interpretation was ambiguous and difficult to administer and thus recommended that it be removed.[101]

On the other hand, Senator Levin supported an inclusive interpretation of the term "U.S. person" that would encompass foreign offices and affiliates of U.S. financial institutions and corporations, because requiring a case-by-case analysis of whether they should be subject to the

---

[99] Id. at A8.

[100] See IIAC (Aug. 27, 2012) at 3-5.

[101] See Lloyds Banking Group ("Lloyds") (Aug. 24, 2012) at 3; Managed Fund Association and Alternative Investment Management Association ("MFA/AIMA") (Aug. 28, 2012) at 6.

Dodd-Frank Act would be complicated, burdensome, and susceptible to gamesmanship.[102] He also suggested that, since it appears that typically foreign affiliates and subsidiaries operate not as independent actors but are closely integrated with their parent corporations, obtaining from them the financial backing needed for their derivative trades, the Commission's interpretation should presume that a foreign affiliate engaged in swap activity is an extension of the parent corporation, unless the parent can demonstrate that the foreign affiliate should be treated as independent.[103] Senator Levin also stated that the Commission's interpretation should include as a U.S. person any foreign affiliate under common control with a U.S. person, based on factors such as common management, funding, systems, and financial reporting.[104]

With respect to prong (ii)(B) of the interpretation, which addresses situations where the direct or indirect owners of an entity are responsible for its liabilities, several commenters stated that the phrase "responsible for the liabilities" was vague. For example, the Committee on Capital Markets Regulation ("Capital Markets") stated that the phrase "responsible for the liabilities" was open to interpretation and requested that the Commission provide more details regarding its interpretation of this phrase.[105] SIFMA sought clarification on whether the Commission intended to capture partnerships where the partners have unlimited liability.[106] The International Swaps and Derivatives Association Inc. ("ISDA") stated that it was not clear

---

[102] See Letter from Sen. Levin at 7-8.

[103] Id. (stating that it "makes little economic sense, given the insubstantial reality of many foreign affiliates and subsidiaries in the financial industry" to "view a foreign affiliate or subsidiary as a non-U.S. person even if it were fully integrated with its U.S. parent, operated as a wholly owned shell operation with no offices or employees of its own, and functioned in the same way as a branch or agency office").

[104] Id. at 8.

[105] See Capital Markets (Aug. 24, 2012) at 5.

[106] See SIFMA (Aug. 27, 2012) at A13 and A19.

whether the concept includes guarantees, sureties, simple risk of loss of equity, or other type of exposure.[107] Deutsche Bank further noted that the language in prong (ii)(B) could be read to include an entity guaranteed by a U.S. person, which appears at odds with possibly varying policies elsewhere in the Proposed Guidance for entities guaranteed by U.S. persons.[108]

Commenters also expressed concerns about the lack of a minimum U.S.-ownership threshold. For example, Sumitomo Mitsui Trust Bank Ltd. ("Sumitomo") stated that there should be a minimum level of ownership of the entity in question by one or more U.S. persons for this prong to apply, and suggested that the majority ownership threshold used in prong (iv) apply here as well.[109] ISDA emphasized a different point, stating that without clear thresholds, a non-U.S. business would be within the Commission's interpretation of the term "U.S. person" by virtue of even negligible ownership interests by U.S. persons.[110] The Financial Services Roundtable ("FSR") stated that prong (ii) is overbroad because it would cover even minority-U.S. owned institutions based only on a pro-rata (or less) parent liability guarantee.[111]

Capital Markets raised a concern that whether a conclusion that the direct or indirect owners of a U.S. legal entity are "responsible for the liabilities" of such entity requires

---

[107] See ISDA (Aug. 27, 2012) at 9; MFA/AIMA (Aug. 28, 2012) at 6.

[108] See Deutsche Bank (Aug. 27, 2012) at 3. See also Peabody Energy Corporation ("Peabody")(Aug. 28, 2012) at 2-3 ("By contrast, a foreign affiliate or subsidiary of a U.S. person would be considered a non-U.S. person, even where such an affiliate or subsidiary has certain or all of swap-related obligations guaranteed by the U.S. person.") (citing Proposed Guidance, 77 FR at 41218); SIFMA (Aug.27, 2012) at A2 (stating that the Commission should clarify that prong (ii)(B) of the interpretation is not meant to capture an entity merely because it is guaranteed by a U.S. person).

[109] See Sumitomo (Aug. 24, 2012) at 2.

[110] See ISDA (Aug. 10, 2012) at 8 (recommending that regardless of the nature of the "responsibilities for the liabilities," only direct owners of apparent non-U.S. persons should be considered, and that the Commission adopt a presumptive control threshold of 25% direct ownership for distinguishing between control persons and owners that need not be considered in assessing the status of an entity as a U.S. person).

[111] See FSR (Aug. 27, 2012) at 3.

knowledge of each counterparty's legal and ownership structure.[112] FSR stated that interpretation of prong (ii)(B) would depend on a reevaluation of most, if not all, counterparty relationships in order to determine what type of liability guarantees exist between an entity and its parent.[113] Both Capital Markets and FSR stated that firms do not currently have any reasonable means to obtain information necessary to assess this element of the interpretation, particularly within the short time frame prior to the registration date.

One commenter supported finalization of the alternative prong (ii)(B) in the Further Proposed Guidance, with minor clarifying changes. The Commercial Energy Working Group ("CEWG") stated that the words "all of" should be added to clarify that this prong would generally apply when U.S. persons that are majority owners bear "unlimited responsibility for all of the obligations and liabilities of the legal entity …"[114] The CEWG also stated that the Guidance should reaffirm that a guarantee of a non-U.S. person by a U.S. person, in and of itself, generally would not invoke U.S. person status.[115] Other commenters that supported the principles of the alternative prong (ii)(B) thought that the interpretation of "U.S. person" in this regard should be restructured. The Investment Company Institute ("ICI") stated that the Commission should clarify that collective investment vehicles would not fall within the alternative prong (ii)(B) because the investors' liabilities are limited to the amount of their investment.[116] Thus, ICI stated that it believes the alternative prong (ii)(B) would be superfluous

---

[112] See Capital Markets (Aug. 24, 2012) at 5.

[113] See FSR (Aug. 27, 2012) at 3.

[114] See CEWG, submitted by Sutherland Asbill & Brennan LLP (Feb. 25, 2013) at 5.

[115] Id.

[116] See ICI (Feb. 6, 2013) at 3.

with respect to collective investment vehicles because the alternative prong (iv) in the Further Proposed Guidance would address these entities if they are majority-owned by U.S. persons.[117] MFA/AIMA, on the other hand, supported the combination of majority ownership and unlimited liability elements in the alternative prong (ii)(B) and recommended that collective investment vehicles be considered under that prong.[118]

Other commenters stated that the Commission should clarify that the language at the end of the proposed alternative prong (ii)(B), which refers to limited liability companies and limited liability partnerships, would generally also apply to other types of entities where owners have limited liability but where the entities have different names in foreign legal jurisdictions.[119] MFA/AIMA and SIFMA AMG stated that the Commission should clarify how frequently an entity should consider (e.g., annually) whether U.S. persons are its direct or indirect majority owners, and provide for a transition period after an entity falls within this prong of the interpretation for the first time.[120]

Other commenters were critical of the alternative prong (ii)(B). Greenberger/AFR and Better Markets stated that this proposed prong is too narrow, because it appears to require that U.S. persons be both the majority owners of an entity and bear unlimited responsibility for the

---

[117] See id. at 2. See also IIB (Feb 6, 2013) at 10-11 (collective investment vehicles should be excluded from prong (ii) and addressed only in prong (iv)).

[118] See MFA/AIMA (Feb. 6, 2013) at 7-8. Thus under MFA/AIMA's approach, the status of collective investment vehicles would be determined by reference to only the tests in alternative prong (ii)(B).

[119] Id. at 10-11; Asociación Bancaria y de Entidades Financieras de Colombia ("Colombian Bankers") (Feb. 6, 2013) at 1-2; IIB (Feb. 6, 2013) at 10; ISDA (Feb. 6, 2013) at 5-6.

[120] See MFA/AIMA (Feb. 6, 2013) at 12; SIFMA/AMG (Feb. 14, 2013) at 6. ISDA stated that the Commission should clarify how the prong would apply to an entity where some but not all of the owners have unlimited responsibility. In this case, the Commission should clarify whether the U.S. owners with majority ownership of the entity also each must bear unlimited responsibility for the entity's obligations and liabilities or, rather, whether it suffices that a single U.S. owner has unlimited responsibility once U.S. majority ownership is established. See ISDA (Feb. 6, 2013) at 5-7.

entity's obligations and liabilities, in order for the entity to be within the Commission's interpretation of the term "U.S. person" based solely on ownership by U.S. persons.[121] Greenberger/AFR pointed out that a U.S. person could be the majority owner of an entity organized outside the United States, and be responsible for 99% of the entity's obligations, yet the entity would not fall within the Commission's interpretation under the proposed prong.[122]

Other commenters suggested that the alternative prong (ii)(B) is too broad, recommending that the ownership element be limited to when a majority of the direct owners of an entity are U.S. persons, because considering the indirect ownership of an entity will be unworkable for many entities.[123] ISDA also stated that the concept of "unlimited responsibility" is too amorphous to be a basis for the Commission's interpretation, because it could turn on fact-sensitive and uncertain legal judgments under doctrines such as "veil-piercing" or "alter ego" entities.[124] Moreover, ISDA asserted that the Commission has not justified the treatment of unlimited liability entities in the proposed alternative prong (ii)(B) by demonstrating how such

---

[121] See Greenberger/AFR (Feb. 6, 2013) at 7; Better Markets (Feb. 15, 2013) at 7-8.

[122] See Greenberger/AFR (Feb. 6, 2013) at 7.

[123] See MFA/AIMA (Feb. 6, 2013) at 7; SIFMA, The Clearing House, Association LLC ("The Clearing House"), and FSR ("SIFMA/CH/FSR") (Feb. 6, 2013) at 2, A8-9; ISDA (Feb. 6, 2013) at 5. IIB and SIFMA/AMG made similar comments and questioned whether extending this prong to entities where a majority of indirect owners are U.S. persons would be consistent with the "direct and significant connection" language in CEA section 2(i). See IIB (Feb. 6, 2013) at 10; SIFMA/AMG (Feb. 14, 2013) at 3-4.

[124] See ISDA (Feb. 6, 2013) at 6. ISDA also stated that the Commission should make clear that the reference to "unlimited responsibility" does not include responsibility arising out of separate contractual arrangements or extraordinary circumstances, such as conduct by owners that results in veil piercing or limited partner participation in management of a partnership. See id. SIFMA/CH/FSR made similar points and stated that this prong is not necessary because market participants have not used unlimited liability entities to avoid Dodd-Frank regulations. See SIFMA/CH/FSR (Feb. 6, 2013) at A12.

entities are more susceptible to being used to evade Dodd-Frank regulations or otherwise raise the concerns addressed by the Commission's regulations.[125]

Commenters were also critical of the element of the alternative prong (ii)(B) that would treat a collective investment vehicle as a U.S. person if its principal place of business is in the United States. They stated that application of this element would be very unclear and difficult on an operational level.[126] Commenters also stated that a collective investment vehicle should be treated as a U.S. person if it is organized in the U.S., not if its manager or operator is in the U.S.[127]

Peabody Energy Corporation ("Peabody") and SIFMA/AMG stated the Commission should adopt the interpretation of U.S. person in the January Order, which does not include all the elements of the proposed alternative prong (ii)(B).[128]

Commenters generally did not comment on prong (iii) of the proposed interpretation of the term "U.S. person."

With respect to prong (iv) relating to majority direct- or indirect- owned commodity pools, pooled accounts, or collective investment vehicles, several commenters stated that this prong was unworkable because the proposed interpretation would require potentially

---

[125] See ISDA (Feb. 6, 2013) at 6.

[126] Id. at 6-7; SIFMA/CH/FSR (Feb. 6, 2013) at A1, A5-6, B5; IIB (Feb. 6, 2013) at 7-8, 10.

[127] See MFA/AIMA (Feb. 6, 2013) at 8-9; SIFMA/AMG (Feb. 6, 2013) at A7-8. The Japanese Bankers Association made similar comments and stated that the Commission should clarify whether the location of the principal place of business of a subsidiary that is controlled by its parent is the location of the subsidiary's headquarters or the parent's headquarters. Japanese Bankers Association (Feb. 6, 2013) at 7.

[128] See Peabody (Feb. 5, 2013) at 1-2; SIFMA/AMG (Feb. 6, 2013) at 1-3.

unascertainable information.[129] According to SIFMA, reliance on representations would be the only practical way to consider the status of counterparties as U.S. persons under this prong since other types of information, such as the direct and indirect ownership of any commodity pool, pooled account or collective investment vehicle with which a market participant transacts, may be unavailable, non-public or otherwise sensitive.[130] Moreover, a fund would be required to monitor its level of U.S. ownership on an on-going basis, and this prong could result in frequent changes in the fund's U.S. person status.[131] The Clearing House argued that the interpretation should not look through direct investors to indirect investors, unless there is evidence of evasion.[132] Other commenters questioned whether the proposed interpretation of "U.S. person" for commodity pools, pooled accounts, and collective investment vehicles meets the "direct and significant" jurisdictional nexus applicable to the Commission's application of Title VII to transactions with such persons.[133]

Cleary urged that the Commission not adopt an interpretation of "U.S. person" based on the composition of fund ownership, at least prior to finalizing the interpretation.[134] As it explained, even if the Commission's interpretation would allow for reasonable reliance on counterparty representations, fund counterparties would not be able to provide any representation

---

[129] See, e.g., ISDA (Aug. 10, 2012) at 8; SIFMA (Aug. 27, 2012) at A17; Credit Suisse (Aug. 27, 2012) at 3-4; The Clearing House Association LLC ("The Clearing House") (Aug.27, 2012) at 12-13; Cleary (Aug. 16, 2012) at 7; IIB (Aug. 27, 2012) at 6-7.

[130] See SIFMA (Aug. 27, 2012) at A17-18. See also IIB (Aug. 27, 2012) at 7 (arguing that since pools cannot ascertain or control the status of their indirect investors, the reference to indirect ownership should be removed).

[131] SIFMA (Aug. 27, 2012) at A17.

[132] See The Clearing House (Aug. 13, 2012) at 15 n. 20.

[133] See, e.g., SIFMA/AMG (Aug. 27, 2012) at 2-3; MFA/AIMA (Aug. 28, 2012) at 4-5; ICI (Aug. 23, 2012) at 4.

[134] See Cleary (Aug. 16, 2012) at 6-7.

except with respect to funds formed after the finalization of the interpretation for which the fund's subscription materials could have been modified to capture the relevant information.[135] If the Commission nevertheless decided to adopt an interpretation based on investor composition, Cleary argued against including a fund in the interpretation on the basis of indirect ownership at any level less than a majority-ownership.[136]

Consideration of majority-ownership is particularly problematic with respect to funds that are publicly traded, according to several commenters.[137] For example, ICI explained that U.S. persons typically purchase shares in non-U.S. funds through intermediaries, and that such shares are registered and held in nominee/street name accounts.[138] In such cases, the fund manager/operator would not have information regarding the underlying investors.[139] SIFMA recommended that publicly offered and listed commodity pools organized in foreign jurisdictions be excluded from the interpretation.[140] Credit Suisse stated that a fund should not be considered a U.S person to the extent that it is organized outside the United States and is subject to foreign regulation that is comparable to U.S. law. To the extent the fund is not so regulated, then the

---

[135] Id.

[136] Id. IIB also noted that fund sponsors/operators verify investor status through subscription materials provided at the time of initial investment. Therefore, they request that any test based on fund ownership apply only to funds formed after the effective date of the final "U.S. person" interpretation. IIB also agreed that majority ownership is the minimum threshold under which a foreign fund should be included in the interpretation of the term "U.S. person." See IIB (Aug. 27, 2012) at 6-7.

[137] See, e.g., SIFMA (Aug. 27, 2012) at A20; ICI (Aug. 23, 2012) at 3-7; MFA/AIMA (Aug. 28, 2012) at 4; Credit Suisse (Aug. 27, 2012) at 3-4.

[138] See ICI (Aug. 23, 2012) at 3.

[139] ICI also noted that certain jurisdictions may prohibit disclosure by intermediaries of beneficial owner information. Id.

[140] See SIFMA (Aug. 27, 2012) at A19-20.

fund would be within the U.S. person interpretation only where it is organized under the laws of the United States or marketed to U.S. residents.[141]

One commenter strongly supported the alternative prong (iv) in the Further Proposed Guidance. Citadel stated that since the Dodd-Frank clearing and reporting requirements will mitigate systemic risk, increase transparency and promote competition, the U.S. person interpretation should encompass offshore collective investment vehicles that have a sufficient U.S. nexus.[142] If it did not, then a core, active portion of the swaps market would fall outside the scope of the transaction level requirements, including clearing, which would undermine central objectives of Dodd-Frank, create opportunities for regulatory arbitrage, and risk fragmenting the swaps markets.[143]

Other commenters argued that the entities that would be covered by the alternative prong (iv) should not be covered by the interpretation of "U.S. person," which should cover only entities that are directly majority-owned by U.S. persons. For example, SIFMA/CH/FSR stated that consideration of indirect ownership could require ongoing monitoring of ownership, which is burdensome or even impossible, and would not necessarily reflect a sufficient jurisdictional nexus to the United States.[144] SIFMA/CH/FSR also stated that if consideration of majority ownership is included in the interpretation, it should reflect an objective statement of the ownership level that the Commission would consider relevant to U.S.-person status, so as to exclude entities that are owned by U.S. persons only to a de minimis extent and allow an annual

---

[141] See Credit Suisse (Aug, 27, 2012) at 3-4.

[142] See Citadel (Feb. 6, 2013) at 1.

[143] See id.

[144] See SIFMA/CH/FSR (Feb. 6, 2013) at A8-9. See also IIB (Feb. 6, 2013) at 11 (systems to track indirect ownership would be difficult and expensive to implement).

consideration of ownership.[145] MFA/AIMA and the Investment Adviser Association ("IAA") also provided reasons that there is not a sufficient jurisdictional nexus with the United States to include in the Commission's interpretation of the term "U.S. person" collective investment vehicles that are indirectly majority-owned by U.S. persons.[146]

Some commenters stated that whether a collective investment vehicle would be included in the interpretation of U.S. person should depend on whether the fund or other collective investment vehicle is being offered to U.S. persons, arguing that the interpretation should cover collective investment vehicles that are targeted to the U.S. market or to U.S. investors by focusing on activities within the control of the vehicle's manager.[147]

---

[145] See SIFMA/CH/FSR (Feb. 6, 2013) at A8-9. ISDA stated that the lack of an objective policy regarding the interpretation of majority ownership would lead to arbitrary or indeterminate results for many collective investment vehicles due to their varied capital structures (citing, for example, structured finance vehicles, which merit further analysis due not only to their complex capital structures but also to practical difficulties in monitoring ownership of their securities), and the practical consequences of the alternative interpretations can be considered only following a more concrete proposal offered for public comment. See ISDA (Feb. 6, 2013) at 6-7.

[146] MFA/AIMA stated that since interactions between collective investment vehicles and registered swap dealers are expected to be covered by Dodd-Frank requirements or comparable foreign regulations, the inclusion of collective investment vehicles as "U.S. persons" is less important to achieve regulatory coverage. See MFA/AIMA (Feb. 6, 2013) at 7-8. MFA/AIMA also disputed whether the pooling of assets in a collective investment vehicle is a fundamental difference that denotes a greater U.S. nexus than the pooling of assets by corporations or other financial entities, and therefore it is problematic that alternative prong (iv) is more onerous (in MFA/AIMA's view) for non-U.S collective investment vehicles than alternative prong (ii) is for corporate or other financial entities. See id. IAA stated that it is inappropriate to define an entity as a U.S. person based on characteristics of investors in the entity rather than the characteristics of the entity itself. See IAA (Feb. 6, 2013) at 4.

[147] See Invesco Advisers Inc. ("Invesco") (Feb. 6, 2013) at 11 (manager of collective investment vehicle determines whether to make offering in the United States; subsequent purchases by non-U.S. persons who have relocated to the U.S. should not alone constitute offering in the U.S.); IIB (Feb. 6, 2013) at 11. Invesco, ICI and IAA each stated that the language at the end of alternative prong (iv) (if it is adopted) should be interpreted to cover collective investment vehicles that are "publicly-offered" only to non-U.S. persons, even if the vehicles are not publicly-traded. See Invesco (Feb. 6, 2013) at 2; ICI (Feb. 6, 2013) at 3; IAA (Feb. 6, 2013) at 4. See also ICI (Jul. 5, 2013) at 3 n. 9 ("There is an important distinction between publicly-traded funds and publicly-offered funds: publicly-offered funds are those that are broadly available to retail investors; publicly-traded funds are simply a subset of publicly-offered funds that trade on exchanges or other secondary markets. Excluding from the U.S. person definition only publicly-traded funds would capture only a subset of non-U.S. regulated funds. We note that, by contrast, hedge funds are neither publicly offered nor publicly traded and, unlike non-U.S. retail funds, are not subject to substantive government regulation and oversight similar in scope to that provided by the U.S. Investment Company Act.").

Commenters also stated that regardless of the policy adopted in this regard, in the consideration of whether an entity is a U.S. person, only information that is available to third parties or other parties should be considered relevant, and the Commission's policy should contemplate that market participants would rely on a representation of U.S. person status. Also, the Commission's policy should clarify how it would apply during the transition period immediately after expiration of the January Order.[148]

Addressing prong (v) relating to registered commodity pool operators, many commenters stated that the Commission should not adopt an interpretation that looks to the registration status of a fund's operator, because this interpretation could capture a non-U.S. fund that does not itself trigger registration as a commodity pool operator and has a minimal U.S. nexus.[149] A number of commenters urged the Commission not to adopt an interpretation that looks to the nationality of the fund's manager/operator since this would place U.S.-based investment managers at a competitive disadvantage, without addressing the Commission's regulatory objectives.[150] IIB generally agreed with these commenters and stated that the commodity pool operator registration prong would be over-inclusive because, under the Commission's current rules, an operator of a

---

ICI and IAA stated that the Commission should interpret whether an offer is made to U.S. persons in accordance with precedents under the SEC's Regulation S. See ICI (Feb. 6, 2013) at 4-5 n. 14; IAA (Feb. 6, 2013) at 4. ISDA stated that the Commission's interpretation should specifically exclude any collective investment vehicle that offers its securities in accordance with local law and customary documentation practices in a local market, as well as offerings conducted in accordance with the Regulation S. See ISDA (Feb. 6, 2013) at 7.

[148] See SIFMA/AMG (Feb. 14, 2013) at 4 n. 8; IIB (Feb. 6, 2013) at 7; ISDA (Feb. 6, 2013) at 7; Japanese Bankers Association (Feb. 6, 2013) at 5.

[149] See, e.g., SIFMA (Aug. 27, 2012) at A21; ICI (Aug. 23, 2012) at 3-7; IIB (Aug. 9, 2012) at 3; MFA/AIMA (Aug. 28, 2012) at 4-5; IIAC (Aug. 27, 2012) at 4, 5. As IIB explained, even a fund that lacks a sufficient U.S. connection can be considered a U.S. person where its commodity pool operator is required to register. IIB (Aug. 9, 2012) at 3. Under Commission regulation 3.10, the operator of a non-U.S. fund with even one U.S.-based owner is required to register as a commodity pool operator.

[150] See SIFMA (Aug. 27, 2012) at A13; ICI (Aug, 23, 2012) at 4; Cleary (Aug. 16, 2012) at 7; The Clearing House (Aug. 27, 2012) at 13-14.

foreign pool may be required to register as a commodity pool operator with less than 50 percent U.S. ownership; at the same time, the prong also would be under-inclusive because it would not cover funds whose operators are eligible for relief from commodity pool operator registration.

ICI recommended that the Commission, instead, interpret the term "U.S. person" to include a commodity pool, pooled account, or collective investment vehicle that is "offered publicly, directly or indirectly" by the manager/sponsor to U.S. persons.[151] As ICI explained, this alternative approach would base a fund's U.S. person status on more workable considerations, and not on changes in investor status that are beyond the control of a fund or its manager/operator. In the consideration of whether a fund is making a public offering to U.S. persons, ICI recommended that the Commission look to SEC Regulation S.[152]

IIAC recommended that prong (vi) relating to pension plans be modified so that pension plans designed exclusively for foreign employees of a U.S.-based entity are not within the interpretation of the term "U.S. person." Further, IIAC urged the Commission to clarify that U.S. investment advisers or other fiduciaries not be considered to be within the interpretation of the term "U.S. person" when they are acting on behalf of non- U.S. accounts.[153]

IIB stated that prong (vii) relating to an estate or trust should be replaced, explaining that market participants do not typically identify an estate's or trust's regulatory status on the basis of its tax status. Instead, it recommended that the Commission's interpretation look to the status of the executor, administrator, or trustee. Specifically, IIB recommended that the Commission's interpretation of the term "U.S. person" include an estate or trust that is organized in the United

---

[151] See ICI (Aug. 23, 2012) at 5-6.

[152] Id. at 6-7. Regulation S is codified at17 CFR 230.901 et seq.

[153] IIAC (Aug. 27, 2012) at 4.

States "unless (A) an executor, administrator or trustee that is not a U.S. person has sole or shared investment discretion with respect to the assets of the trust or estate, (B) in the case of an estate, the estate is governed by foreign law and (C) in the case of a trust, no beneficiary of the trust (and no settlor if the trust is revocable) is a U.S. person …."[154]

**c. Commenters' Proposed Alternatives**

A number of commenters provided substantially different alternative interpretations of the term "U.S. person."[155] Most notably, the commenters' alternatives would not encompass persons by virtue of "indirect" U.S. ownership. For example, SIFMA's proposed "U.S. person" interpretation would include only those commodity pools or collective investment vehicles that are organized or incorporated under U.S. law or are (1) directly majority owned by "U.S. persons" or, in the case of ownership by a pool, a pool that is organized in the United States and (2) not publicly offered.[156] IIB submitted an alternative "U.S. person" interpretation that generally tracked SIFMA's proposed interpretation.[157]

**d. Due Diligence**

Many commenters stated that the Commission's policy in this regard should contemplate that a firm would reasonably rely on counterparty representations regarding their U.S. person status.[158] For example, SIFMA stated that the Commission's policy should be consistent with a determination by the swap counterparty itself of its U.S.-person status, but in the alternative,

---

[154] IIB (Aug. 27, 2012) at 14.

[155] See, e.g., SIFMA (Aug. 27, 2012); IIB (Aug. 27, 2012); The Clearing House (Aug. 27, 2012).

[156] See SIFMA (Aug. 27, 2012) at A10-11.

[157] See IIB (Aug. 27, 2012) at 13-14.

[158] See, e.g., SIFMA (Aug. 27, 2012) at A16-17; Deutsche Bank (Aug. 27, 2012) at 4; Capital Markets (Aug. 24, 2012) at 5; SIFMA/AMG (Aug. 27, 2012) at 4-5.

SIFMA recommended that the Commission's policy contemplate reasonable reliance on counterparty representations.[159] According to these commenters, counterparty representations are the only practical means of determining counterparty status as firms do not currently collect the information necessary to evaluate counterparty status under the proposed interpretation. The commenters also were concerned that certain prongs of the proposed interpretation (e.g., "look-through" obligations associated with the "direct and indirect ownership" criterion in prong (iv)) would render it difficult, if not impossible, for market participants to directly consider whether their counterparties would be within the Commission's interpretation of the term "U.S. person." SIFMA and Cleary further pointed out that the Commission has accepted reasonable reliance on counterparty representations in the context of the external business conduct standards.[160]

**e. Non-U.S. Person that is Affiliated, Guaranteed, or Controlled by U.S. Person**

Viewed as a whole, the proposed interpretation of the term "U.S. person," would generally not include a non-U.S. affiliate of a U.S. person, even if all of such affiliate's swaps are guaranteed by the U.S. person.[161] The Commission, nevertheless, raised a concern regarding risks associated with a U.S. person providing a guarantee to its non-U.S. affiliates and requested comments on whether the term "U.S. person" should, in fact, be interpreted to generally include a non-U.S. affiliate guaranteed by a U.S. person.[162] In addition, the Commission sought

---

[159] SIFMA (Aug. 27, 2012) at A16-18.

[160] SIFMA/AMG (Aug. 27, 2012) at 4-5; Cleary (Aug. 16. 2012) at 6.

[161] See Proposed Guidance, 77 FR at 41218. For purposes of this Guidance, the Commission generally interprets the term "affiliates" to include an entity's parent entity and subsidiaries, if any, unless stated otherwise.

[162] Id.

comments on whether the term "U.S. person" also should be interpreted to generally include any non-U.S. persons controlled by or under common control with a U.S. person.[163]

Responding to the Commission's request for comments on this issue, many commenters stated that Title VII requires the Commission to interpret the term "U.S. person" to include foreign affiliates of U.S. persons, and U.S. affiliates of foreign persons, in order to protect U.S. taxpayers from the risks posed by the global swaps market.[164] Senator Levin urged that "[a]t a minimum, it is essential that [the Guidance] … include as a U.S. person any foreign affiliate or subsidiary under common control with a U.S. person."[165] He also agreed with statements in the Proposed Guidance that non-U.S. affiliates guaranteed by U.S. persons effectively transfer the risks of their swaps to the U.S. guarantor, and therefore the guaranteed non-U.S. affiliates should be subject to U.S. safeguards.[166] Public Citizen stated that not interpreting the term "U.S. person" to include a foreign affiliate of a U.S. person "hides the rabbit in the hat" for Title VII purposes.[167] It argued that Congress intended financial entities that are controlled by U.S. financial institutions or that could adversely impact the U.S. economy to be regulated as U.S. persons under Title VII in order to fully protect American taxpayers from the threat of "future financial bailouts."

Greenberger also expressed support for including foreign swap entities controlled by U.S. parents in the interpretation of the term "U.S. person." In his view, the Commission's distinction

---

[163] Id.

[164] See Public Citizen's Congress Watch ("Public Citizen") (Aug. 14, 2012) at 9-10; IATP (Aug. 27, 2012) at 4; Better Markets (Aug. 27, 2012) at 6.

[165] See Letter from Sen. Levin at 8.

[166] See id. (citing Proposed Guidance, 77 FR at 41218).

[167] Public Citizen (Aug. 14, 2012) at 3.

between guaranteed and non-guaranteed foreign subsidiaries is arbitrary, as the absence of a U.S. guarantee does not insulate the U.S. parent from risk exposure.[168] Other commenters argued that the Commission's interpretation of the term "U.S. person" should include foreign affiliates whose swaps are guaranteed by a U.S. person.[169]

Other commenters objected to including a non-U.S. entity in the interpretation of the term "U.S. person" solely on the basis of affiliation with a U.S. person or having its swaps guaranteed by a U.S. person. Sullivan & Cromwell argued that foreign operations of a U.S.-based bank do not have a "direct and significant connection with activities in, or effect on," U.S. commerce based solely on affiliation with or guarantee by a U.S. parent bank.[170] It stated that overseas operations usually have a non-U.S. orientation (i.e., transactions with non-U.S. counterparties for non-U.S. business purposes), and thus the connection to U.S. commerce is indirect and, further, transactions with non-U.S. counterparties will not have a significant effect on U.S. commerce. Other commenters raised similar concerns about the lack of jurisdictional nexus. For example, The Clearing House stated that the Commission must conclude that the risk to the U.S. entity is "significant" before designating a non-U.S. guaranteed entity a "U.S. person," and further stated that a non-U.S. entity that is subject to local capital rules or swap dealer registration should be excluded from the interpretation of "U.S. person."[171] SIFMA, addressing the control issue, objected to including a non-U.S. person that is controlled by, or under common control with,

---

[168] Greenberger (Aug. 27, 2012) at 6-7.

[169] See Better Markets (Aug. 27, 2012) at 6-7; Public Citizen (Aug. 14, 2012) at 3.

[170] See Sullivan & Cromwell (Aug. 13, 2012) at A2-3. See also Hong Kong Banks (Aug. 27, 2012) at 4.

[171] See The Clearing House (Aug. 27, 2012) at 17.

such person in the interpretation of the term "U.S. person" since such control is insufficient to satisfy the jurisdictional nexus required by section 2(i).[172]

Japanese Bankers Association did not agree that these situations effect a risk transfer to the U.S. person, arguing that the risk would ultimately be incurred by the non-U.S. person and not by the U.S. guarantor; thus, it believed that the term "U.S. person" should not be interpreted to include a non-U.S. person guaranteed by a U.S. person.[173] The Coalition for Derivatives End-Users ("End-Users Coalition") expressed concerns about competitive implications, stating that imputing U.S. status to a non-U.S. person guaranteed by a U.S. person may disadvantage the non-U.S. affiliates of U.S. end-users, since those non-U.S. affiliates may need to be guaranteed to enter into swaps with non-U.S. counterparties.[174]

**f. Foreign Branch of U.S. Person**

In the Proposed Guidance, the Commission stated that a foreign branch of a U.S. swap dealer should be included in the Commission's interpretation of the term "U.S. person" because it is a part, or an extension, of a U.S. person.[175] Several commenters agreed with the Commission's interpretation.[176] Senator Levin asserted that the "JP Morgan whale trades provide strong factual support for an inclusive definition of U.S. person, in particular when it

---

[172] See SIFMA (Aug. 27. 2012) at A20. See also Australian Bankers (Aug.27, 2012) at 4 (stating that the control concept should not be relevant in the definition of "U.S. person," and while common control may potentially indicate common risk, the Commission's focus on the ultimate location of the risk is a more relevant to the interpretation of the term "U.S. person.").

[173] See Japanese Bankers Association (Aug. 27. 2012) at 8.

[174] See End-Users Coalition (Aug. 27, 2012) at 3 (urging the Commission to exclude a foreign affiliate of a U.S. end-user, guaranteed by that end-user, from its interpretation).

[175] See Proposed Guidance, 77 FR at 41218.

[176] See, e.g., Public Citizen (Aug. 27, 2012) at 5; Greenberger (Aug. 27, 2012) at 3; Better Markets (Aug. 27, 2012) at 2, 6-7.

comes to the foreign branch or agency of a U.S. corporation."[177] Other commenters recommended that a foreign branch of a U.S. swap dealer be excluded from the interpretation. Sullivan & Cromwell argued that a foreign branch should not be included in the interpretation solely on the basis that it is a part of a U.S. bank.[178] Citi recommended that the Commission's policy should be that a foreign branch of a U.S. swap dealer is generally considered a non-U.S. person, so long as the branch remains subject to Entity-Level Requirements and obtains substituted compliance for Transaction-Level Requirements for transactions with non-U.S. persons.[179] In Citi's view, this would address comments by the foreign branch's non-U.S. clients that they would have to register as swap dealers or MSPs, while assuring that such non-U.S. clients' swaps with the foreign branch would generally be covered by the Transaction-Level Requirements or substituted compliance.

**g. Regulation S**

Some commenters believed that the Commission's policy should explicitly adopt the SEC's Regulation S definition of a "U.S. person." MFA/AIMA stated that Regulation S eliminates problems and inconsistencies in the Commission's proposed interpretation.[180] J.P. Morgan stated that Regulation S would facilitate compliance by non-U.S. market participants since they are familiar with the SEC's approach.[181] On the other hand, the Institute for

---

[177] See Letter from Sen. Levin at 7.

[178] See Sullivan & Cromwell (Aug. 13, 2012) at A6-7.

[179] See Citi (Aug. 27, 2012) at 2-4 (stating that foreign branches of U.S.-based swap dealers should not be considered "U.S. persons," but should still be subject to the Commission's Entity-Level and Transactional-Level Requirements). See also State Street (Aug. 27, 2012) at 3; IIB (Aug. 27, 2012) at 8.

[180] See MFA/AIMA (Aug. 28, 2012) at 8-9.

[181] See J.P. Morgan (Aug. 13, 2012) at 9.

Agriculture and Trade Policy ("IATP") argued against incorporating the Regulation S definition, stating that it predates the prominence of the swaps market.[182]

**h. Other Clarifications**

A number of commenters voiced concerns regarding potential expansion of the Commission's interpretation of the term "U.S. person," which they thought could result from the prefatory phrase "includes, but is not limited to," and requested that the Commission affirmatively state that non-U.S. persons are any persons that would not be covered by the interpretation of the term "U.S. person."[183] A non-exhaustive "U.S. person" interpretation, they contended, would create unnecessary uncertainty.

A number of commenters further stated that the interpretation of the term "U.S. person" should be applied only for purposes of the registration and regulation of swap dealers and MSPs.[184] The Futures Industry Association ("FIA") argued that the interpretation of the term "U.S. person" should not extend to those provisions of the CEA governing the activities of futures commission merchants ("FCMs") with respect to either exchange-traded futures (whether executed on a designated contract market or a foreign board of trade) or cleared swaps.[185] SIFMA similarly requested that the Commission clarify that the final interpretation of the term "U.S. person" does not override existing market practice as it relates to futures or FCMs,

---

[182] See IATP (Aug. 27, 2012) at 4.

[183] See SIFMA (Aug. 27, 2012) at A15; IIB (Aug. 27, 2012) at 11-12; EC (Aug. 24, 2012) at 1-2; Australian Bankers (Aug. 27, 2012) at 4.

[184] See, e.g., The Futures and Options Association Ltd. ("FOA") (Aug. 13, 2012) at 10-11; SIFMA (Aug. 27, 2012); IIB (Aug. 27, 2012); EC (Aug. 24, 2012).

[185] See FIA (Aug. 27, 2012) at 2-3.

including with respect to clearing.[186] SIFMA also requested that the Commission clarify that the final interpretation of the term "U.S. person" for cross-border swaps regulation is the single interpretation for all Dodd-Frank swaps regulation purposes.[187] Finally, SIFMA requested that supranational organizations, such as the World Bank and International Monetary Fund (and their affiliates) be excluded from the interpretation.[188]

### 3. **Commission Guidance**

The Commission has carefully reviewed and considered the comments received and is finalizing a policy that will generally set forth an interpretation of the term "U.S. person," as used in this Guidance, with certain modifications to the proposed definition as described below. As explained in the Proposed Guidance, the term "U.S. person," as used in the context of CEA section 2(i), generally encompasses those persons whose activities – either individually or in the aggregate – have the requisite "direct and significant" connection with activities in, or effect on, U.S. commerce within the meaning of section 2(i).[189] The various prongs of the Commission's interpretation are intended to identify persons for which, in practice, the connection or effects required by section 2(i) are likely to exist and thereby inform the public of circumstances in which the Commission expects that the swaps provisions of the CEA and the Commission's

---

[186] See SIFMA (Aug. 27, 2012) at A14-15.

[187] Id.

[188] Id. at A21.

[189]For purposes of this Guidance, the Commission interprets the term "U.S. person" by reference to the extent to which swap activities or transactions involving one or more such persons have the relevant jurisdictional nexus. For example, this interpretation would help determine whether non-U.S. persons engaging in swap dealing transactions with "U.S. persons" in excess of the de minimis level would be required to register and be regulated as a swap dealer. In addition, for the same reasons, the term "U.S. person" can be helpful in determining the level of U.S. interest for purposes of analyzing and applying principles of international comity when considering the extent to which U.S. transaction-level requirements should apply to swap transactions.

regulations would apply pursuant to the statute. In this respect, the Commission will consider not only a person's legal form and its domicile (or location of operation), but also the economic reality of a particular structure or arrangement, along with all other relevant facts and circumstances, in order to identify those persons whose activities meet the "direct and significant" jurisdictional nexus. Below, the Commission discusses each prong of its proposed interpretation of the term "U.S. person."

First, the Commission will include in its consideration the elements in prongs (i) and (ii)(A), as proposed, renumbered as prongs (i) and (iii).[190] These prongs of the "U.S. person" interpretation generally incorporate a "territorial" concept of a U.S. person.[191] That is, these are natural persons and legal entities that are physically located or incorporated within U.S. territory and, consequently, the Commission would generally consider swap activities involving such persons to satisfy the "direct and significant" test under section 2(i).[192] The Commission clarifies that it expects that prong (iii) would encompass legal entities that engage in non-profit activities, as well as U.S. state, county and local governments and their agencies and instrumentalities. Under prong (iii), the Commission would generally interpret the term "U.S. person" to include also a legal entity that is not incorporated in the United States if it has its "principal place of business" in the United States. The Commission intends that this

---

[190] For clarity, the Commission has reordered the prongs of its interpretation of the term "U.S. person."

[191] For purposes of this Guidance, the Commission would interpret the term "United States" to include the United States, its states, the District of Columbia, Puerto Rico, the U.S. Virgin Islands, and any other territories or possessions of the United States government, or enclave of the United States government, its agencies or instrumentalities.

[192] In this respect, the Commission declines to adopt a commenter's recommendation that IRS regulations should be relevant in considering whether a person is included in the interpretation of the term "U.S. person." The Commission believes that adopting the IRS's approach in the Commission's policy would be inappropriate; rather, consistent with CEA section 2(i), the Commission's interpretation of the term "U.S. person" focuses on persons whose swap activities meet the "direct and significant" nexus.

interpretation would generally include those entities that are organized outside the United States but have the center of direction, control, and coordination of their business activities in the United States.

The concept of an operating company having a principal place of business has been addressed by the Supreme Court. In a recent case, the Supreme Court described a corporation's principal place of business as the "place where the corporation's high level officers direct, control, and coordinate the corporation's activities."[193] The Supreme Court explained that "'principal place of business' is best read as referring to the place where a corporation's officers direct, control, and coordinate the corporation's activities. It is the place that Courts of Appeals have called the corporation's 'nerve center.' And in practice it should normally be the place where the corporation maintains its headquarters – provided that the headquarters is the actual center of direction, control and coordination, i.e., the 'nerve center,' and not simply an office where the corporation holds its board meetings."[194] The Commission notes that commenters on the Proposed Guidance and Further Proposed Guidance generally did not object to the inclusion in the interpretation of the term "U.S. person" of an entity that has its principal place of business in the United States.

The Commission is of the view that the application of the principal place of business concept to a collective investment vehicle may require consideration of additional factors beyond those applicable to operating companies. A collective investment vehicle is an entity or group of related entities created for the purpose of pooling assets of one or more investors and channeling

---

[193] See Hertz Corp. v. Friend, 559 U.S. 77, 80 (2010) (determining a corporation's principal place of business for purposes of diversity jurisdiction).

[194] Id. at 92-93.

these assets to trade or invest to achieve the investment objectives of the investor(s), rather than being a separate, active operating business.[195] In this context, the determination of where the collective investment vehicle's "high level officers direct, control, and coordinate the [vehicle's] activities" – to apply the Hertz decision noted above – can involve several different factors.[196]

The Commission is aware that the formation and structure of collective investment vehicles involve a great deal of variability, including with regard to the formation of the legal entities that will hold the relevant assets and enter into transactions (including swaps) in order to achieve the investors' objectives. Legal, regulatory, tax and accounting considerations may all play a role in determining how the collective investment vehicle is structured and the jurisdictions in which the legal entities will be incorporated.[197] Many legal jurisdictions around the world have promulgated specialized regimes for the formation of collective investment vehicles, which offer various legal, regulatory, tax and accounting efficiencies.[198]

In view of these circumstances, the Commission believes that for a collective investment vehicle, the locations where the relevant legal entities have registered offices, hold board

---

[195] See Further Proposed Guidance, 78 FR at 913.

[196] As mentioned in the Introduction, Long-Term Capital Portfolio LP, a Cayman Islands hedge fund advised by LTCM, collapsed in 1998, leading a number of creditors to provide LTCM substantial financial assistance under the supervision of the Federal Reserve Bank of New York. High level officers at LTCM's offices in Greenwich, Connecticut, directed, controlled and coordinated the activities of Long-Term Capital Portfolio LP. This hedge fund, with approximately $4 billion in capital and a balance sheet of just over $100 billion had a swap book in excess of $1 trillion notional. Federal Reserve Chairman Alan Greenspan testified that "[h]ad the failure of LTCM triggered the seizing up of markets, substantial damage could have been inflicted on many market participants, including some not directly involved with the firm, and could have potentially impaired the economies of many nations, including our own." Systemic Risks to the Global Economy and Banking System from Hedge Fund Operations: Hearing Before the House Banking and Fin. Services Comm., 105th Cong., 2nd sess. (Oct. 1, 1998) (statement of Alan Greenspan, Chairman, Federal Reserve), available at 1998 WL 694498.

[197] This discussion regarding the location of a collective investment vehicle's principal place of business is solely for purposes of applying Commission swaps regulations promulgated under Title VII. The Commission does not intend to address here the interpretation of "principal place of business" for any other purpose.

[198] See Gerald T. Lins, et al., Hedge Funds and Other Private Funds: Regulation and Compliance § 9:1 (Thomson Reuters 2012-2013 ed. 2012).

meetings or maintain books and records are generally not relevant in determining the principal place of business of the collective investment vehicle. Instead, as stated in the Hertz case cited above, the determination should generally depend on the location of the "actual center of direction, control and coordination," i.e., the "nerve center," of the collective investment vehicle.

Hertz focuses on the place where the "high level officers direct, control, and coordinate" the entity's activities.[199] In this regard, the Commission believes that the focus should not necessarily be on the persons who are named as directors or officers of the legal entities that comprise the collective investment vehicle.[200] As noted above, these legal entities are merely the legal structure through which the investment objectives of the collective investment vehicle are implemented. Rather, the analysis should focus on the persons who are the equivalent for the collective investment vehicle to the "high level officers" of an operating company because they direct, control and coordinate key functions of the vehicle, such as formation of the vehicle or its trading and investment.

The "high level officers [who] direct, control and coordinate" the collective investment vehicle may be those senior personnel who implement the investment and trading strategy of the collective investment vehicle and manage its risks, and the location where they conduct the activities necessary to implement the investment strategies of the vehicle may be its center of direction, control and coordination. In this regard, the Commission notes that the achievement of the investment objectives of a collective investment vehicle typically depends upon investment

---

[199] See note 193 and accompanying text, supra.

[200] In many cases, the entities that comprise the collective investment vehicle may not have "high level officers" as contemplated by Hertz, and the directors of the entities may be individuals who are affiliated with a firm that is the legal counsel or administrator of the collective investment vehicle and who may serve as directors for many different vehicles. See Lins, supra note 198, at § 9:4.

performance and risk management. Investors in a collective investment vehicle seek to maximize the return on their investment while remaining within their particular tolerance for risk. Thus, the key personnel relevant to this aspect of the analysis are those senior personnel responsible for implementing the vehicle's investment strategy and its risk management. Depending on the vehicle's investment strategy, these senior personnel could be those responsible for investment selections, risk management decisions, portfolio management, or trade execution.[201]

The achievement of a collective investment vehicle's investment objectives may be closely linked to its formation. Decisions made in the structuring and formation of the collective investment vehicle may have a significant effect on the performance of the vehicle. Thus, for purposes of identifying the vehicle's principal place of business, the Commission may also consider the location of the senior personnel who direct, control and coordinate the formation of the vehicle (i.e., the promoters).[202] The location of the promoters of the collective investment

---

[201] The Commission understands that the collective investment vehicle may obtain the services of the relevant personnel through a variety of arrangements, including contracting with an asset manager that employs the personnel, contracting with other employers, or retaining the personnel as independent contractors. Thus, in this analysis, the Commission would generally expect to consider the location of the personnel who undertake the relevant activities, regardless of their particular employment arrangements.

[202] The promoters who form a collective investment vehicle may be integral to the ongoing success of the collective investment vehicle. In fact, the importance of the role played by the promoters of a legal entity has long been recognized. See generally 1A Fletcher Cyc. Corp. § 189. For example, in Old Dominion Copper Mining & Smelting Co. v. Bigelow, the court drew upon English law in describing the promoters as follows:

> In a comprehensive sense promoter includes those who undertake to form a corporation and to procure for it the rights, instrumentalities and capital by which it is to carry out the purposes set forth in its charter, and to establish it as fully able to do its business. Their work may begin long before the organization of the corporation, in seeking the opening for a venture and projecting a plan for its development, and it may continue after the incorporation by attracting the investment of capital in its securities and providing it with the commercial breath of life.

203 Mass. 159, 177 (1909), aff'd, 225 U.S. 111 (1912).

Modern law continues to refer to the responsibility of promoters of legal entities. See, e.g., SEC Form D, instructions to Item 3 (requiring information regarding the "promoters" of a securities issuer). See also In Re

vehicle is relevant, particularly where the vehicle has a specialized structure or where the promoters of the vehicle continue to be integral to the ongoing success of the fund, including by retaining overall control of the vehicle. The location where the promoters of the collective investment vehicle act to form the vehicle and bring it to commercial life is relevant in determining the center of direction, control and coordination of the vehicle, and those promoters may be the "high level officers" of the vehicle referred to in Hertz.[203]

Accordingly, the Commission will generally consider the principal place of business of a collective investment vehicle to be in the United States if the senior personnel responsible for either (1) the formation and promotion of the collective investment vehicle or (2) the implementation of the vehicle's investment strategy are located in the United States, depending on the facts and circumstances that are relevant to determining the center of direction, control and coordination of the vehicle.

Since the Commission recognizes that the structures of collective investment vehicles vary greatly, the Commission believes it is useful to provide examples to illustrate how the Commission's approach could apply to a consideration of whether the "principal place of business" of a collective investment vehicle is in the United States in particular hypothetical

---

Charles Schwab Corp. Sec. Litig., 2010 WL 1261705 (N.D. Cal. Mar. 30, 2010) (discussing responsibility of "fund managers and promoters" to operate a collective investment vehicle in accordance with its formation documents).

The Commission generally does not intend that when the promoters of a collective investment vehicle serve an administrative, purely ministerial function of handling the flow of funds from investors into the vehicle, the location of these personnel would be relevant in this context.

[203] The Commission is aware that the boards of directors (or equivalent corporate bodies) of the legal entities that comprise a collective investment vehicle typically have the authority to appoint or remove the legal entity's investment manager, administrator, and auditor, and to approve major transactions involving the legal entity and the legal entity's audited financial statements. But since these functions are not key to the actual implementation of the investment objectives of the collective investment vehicle, and noting that Hertz focuses on the "high level officers" of the entity rather than its directors, the Commission would generally not view the boards of directors of the legal entities to be key personnel for the collective investment vehicle.

situations. However, because of variations in the structure of collective investment vehicles as well as the factors that are relevant to the consideration of whether a collective investment vehicle has its principal place of business in the United States under this Guidance, these examples are for illustrative purposes only. In addition, these examples are not intended to be exclusive or to preclude a determination that any particular collective investment vehicle has its principal place of business in the United States.

Example 1. An asset management firm located in the United States establishes a collective investment vehicle outside the United States ("Fund A").[204] Typically, the formation of the collective investment vehicle by the personnel of the asset management firm involves the selection of firms to be the administrator, prime broker, custodian and placement agent for the collective investment vehicle.[205] The legal entities comprising the collective investment

---

[204] The collective investment vehicle could be a hedge fund, a private equity fund, or other type of investment fund. The Commission is aware that the asset management firm may use any of a variety of structures to form the collective investment vehicle, which may involve one or more legal entities. In a common hedge fund structure, the asset management firm forms a legal entity outside the United States which holds the collective investment vehicle's assets and is the legal counterparty in its investment transactions, including swaps (a "master fund"). If this structure is used, then typically the equity of the master fund is held by several "feeder funds," each of which is a separate legal entity formed by the asset management firm with characteristics that are important to a different type of investor. Each investor in the collective investment vehicle obtains an equity interest in one of the feeder funds and thereby holds an indirect interest in the master fund. The Commission intends that this Example 1 would encompass, but not be limited to, a collective investment vehicle using a master/feeder structure such as this.

[205] The collective investment vehicle's administrator generally handles day-to-day administrative activities, such as operating the vehicle's bank account, issuing payment instructions, providing net asset calculations, calculating fees, receiving and processing subscriptions, preparing accounts, maintaining the shareholder register, arranging payments of redemption proceeds, coordinating communications with shareholders, and overseeing anti-money laundering compliance. See id. at § 9:6. The prime broker facilitates the execution of the vehicle's investment transactions, including swaps. The custodian is responsible for holding the vehicle's assets. The placement agent markets and sells shares to investors.

The Commission generally considers all of these functions, although important to the collective investment vehicle, to be ministerial functions that are generally not relevant to the determination of the location of a collective investment vehicle's principal place of business. Thus, even if all of these firms and all the personnel performing

vehicle enter into agreements retaining the asset management firm as investment manager. Personnel of the asset management firm who are located in the United States will be responsible for implementing Fund A's investment and trading strategy and its risk management. Based on the above facts, the Commission would be inclined to view the principal place of business of Fund A as being in the United States,[206] and therefore each of the legal entities that comprise Fund A would be within the interpretation of the term "U.S. person."

Example 2. An asset management firm located outside the United States establishes a collective investment vehicle located outside the United States

---

these functions were outside the United States, the Commission would nonetheless be inclined to view the principal place of business of Fund A as within the United States.

Additional elements that could be relevant to the determination include the location of the collective investment vehicle's primary assets, and the location of the collective investment vehicle's counterparties. However, the Commission believes that the location of these additional elements outside the United States should generally not preclude an interpretation that the collective investment vehicle's principal place of business is in the United States.

[206] The Commission notes that elements of Example 1 are similar to the facts of a recent court case involving a similar issue – the location of a collective investment vehicle's "center of main interest" for purposes of bankruptcy law. See Bear Stearns, note 7 and accompanying text, supra. In Bear Stearns, the collective investment vehicle's "center of main interest" was found to be in the United States even though its registered office was in the Cayman Islands, because it had no employees or managers in the Cayman Islands, and its investment manager was located in New York. Id., 374 B.R. at 129-30. The court further observed that the administrator that ran the back-office operations was in the United States, the collective investment vehicle's books and records were in the United States before the foreign proceedings began, and all of its liquid assets were located in the United States. Id. at 130. In addition, investor registries were maintained in Ireland; accounts receivables were located throughout Europe and the United States; and counterparties to master repurchase and swap agreements were based both inside and outside the United States – but none were claimed to be in the Cayman Islands. Id.

The Commission believes that Bear Stearns aligns with its view that the principal place of business of a collective investment vehicle should not be determined based on where it is organized or has its registered office, but rather should be based on an analysis of the relevant facts and circumstances. However, the Commission notes that under bankruptcy law various factors, particularly factors relating to the debtor's assets and creditors, may be relevant to the determination of where a debtor has its "center of main interest" for purposes of determining whether a U.S. bankruptcy court has jurisdiction over the matter. See, e.g., In re SPhinX, Ltd., 351 B.R. 103 (Bankr. S.D.N.Y. 2006) (including various factors in the determination of center of main interest, including the location of the debtor's primary assets and the location of the majority of the debtor's creditors). The Commission believes that the factors that are relevant in such bankruptcy jurisdictional cases differ from those that are relevant to the consideration of whether a collective investment vehicle has its principal place of business in the United States for purposes of this Guidance.

("Fund B"). Personnel of the asset management firm who are located outside the United States will be responsible for implementing Fund B's investment and trading strategy and its risk management. However, personnel in two offices of the asset management firm – one of which is located outside the United States and the other of which is located in the United States – will be involved in managing Fund B's investment portfolio. Although the personnel in the U.S. office may act autonomously on a day-to-day basis, they will be under the direction of senior personnel in the non-U.S. office regarding how they are implementing the investment objectives of Fund B. In terms of the asset management firm's internal organization, the personnel in the U.S. office report to the personnel in the non-U.S. office, who also generally hold higher positions within the firm. Because the personnel located inside the United States merely facilitate the implementation of the investment objectives of Fund B, for which senior personnel outside the United States are responsible, the Commission would be inclined to view the principal place of business of Fund B as not being in the United States.[207] As a result, assuming that Fund B is not majority-owned by U.S. persons (as discussed further below), Fund B would not be within the interpretation of the term "U.S. person," and none of the legal entities that

[207] The Commission expects that in this example, this result would be the same if the asset management firm entered into a subadvisory agreement with an independent firm that employed the personnel in the U.S. office described in this example. That is, regardless of whether the U.S. personnel are employed by the asset management firm or a third party employer, the relevant issue is whether the personnel who fulfill the key functions relating to its formation or the achievement of its investment objectives are located in, or outside of, the United States.

comprise Fund B would be U.S. persons (unless the legal entity was actually incorporated or organized in the United States).

Example 3. A financial firm located in the United States establishes a collective investment vehicle outside the United States ("Fund C"). The collective investment vehicle includes a single legal entity organized outside the United States, the assets of which are segregated into several separate classes.[208] The U.S. financial firm arranges with several unaffiliated investment management firms to manage the assets in the various classes; an investment management firm affiliated with the U.S. financial firm may also manage the assets in one or more of the classes. Some of these investment management firms are located in, and others outside, the United States. Under the terms of the contracts between Fund C, the U.S. financial firm and these investment management firms, Fund C has delegated responsibility for the overall control of its investment strategies to the U.S. financial firm that established Fund C, and the U.S. financial firm will have rights to reallocate Fund C's assets among the investment management firms for various reasons, including the U.S. financial firm's discretion regarding Fund C's investment strategies. Based on the above facts, the Commission would be inclined to view the principal place of business of Fund C as being in the United States, even though some of the investment managers involved in implementing Fund C's investment and trading strategy

[208] Legal entities that may be formed with separate classes are known in various jurisdictions as segregated portfolio companies, protected cell companies or segregated accounts companies. A collective investment vehicle with a structure such as this is typically referred to as a "hedge fund platform" or an "umbrella" or "multi-series" hedge fund.

are located outside the United States. Therefore, Fund C (including each of the legal entities that comprise Fund C) would be within the interpretation of the term "U.S. person."[209]

The Commission recognizes that the structures of collective investment vehicles are complex and varied, and it does not intend to establish bright line tests for when the principal place of business of a collective investment vehicle would or would not be within the United States. Rather, the Commission's examples above are intended to illustrate the considerations that would be relevant to whether a collective investment vehicle's principal place of business is in the United States, within the framework of reviewing all the relevant facts and circumstances.[210]

The Commission also understands that non-U.S. individuals, institutions, pension plans or operating companies may retain asset management firms in the United States to provide a range of asset management and other investment-related services. Where the individual, institution, pension plan or operating company is not within any prong of the interpretation of the term "U.S. person" described in this Guidance (including prongs (iii) and (vi) which relate to collective investment vehicles), then the Commission generally believes that the person would

---

[209] The Commission expects that the result would generally be the same where the assets of Fund C are not segregated into separate classes.

[210] The Commission believes that Commission regulation 140.99, which provides for persons to request that the staff of the Commission provide written advice or guidance, would be an appropriate mechanism for a collective investment vehicle to seek guidance as to whether the principal place of business of the vehicle is in the United States for purposes of applying the Commission swaps regulations promulgated under Title VII.

not come within the "U.S. person" interpretation solely because it retains an asset management firm located in the United States to manage its assets or provide other financial services.[211]

Second, the Commission will include in its consideration the elements in the alternative version of prong (ii)(B) that was described in the Further Proposed Guidance (and renumbered in the Guidance as prong (vii)). The relevant elements in the alternative version are whether a legal entity is directly or indirectly majority-owned by one or more U.S. persons,[212] in which one or more of these U.S. person(s) bears unlimited responsibility for the obligations and liabilities of such legal entity, and the entity is not a corporation, limited liability company, limited liability partnership or similar entity where shareholders, members or partners have limited liability.

In response to comments on the Proposed Guidance, the Commission intends that this prong would cover entities that are directly or indirectly majority-owned by U.S. person(s), but not those legal entities that have negligible U.S. ownership interests. In the Commission's view, where the structure of an entity is such that the U.S. owners are ultimately liable for the entity's obligations and liabilities, the connection to activities in, or effect on, U.S. commerce would generally satisfy section 2(i), irrespective of the fact that the ownership is indirect. The Commission expects that this "look-through" aspect of the interpretation also would serve to discourage persons from engaging in activities outside of the Dodd-Frank regulatory regime by creating such indirect ownership structures.

---

[211] However, this policy (that non-U.S. persons generally do not become U.S. persons solely by retaining U.S. asset management firms) would not apply to the legal entities comprising a collective investment vehicle that is within the interpretation of the term "U.S. person." Rather, those legal entities would be within the interpretation of the term "U.S. person" for other reasons (e.g., because the vehicle has its principal place of business in the United States or a majority of its direct or indirect owners are U.S. persons) – not solely because they had retained a U.S. asset management firm.

[212] In this context, the term "U.S. person" refers to those natural persons or legal entities that meet prong (i), (ii), (iii), (iv), or (v) of the interpretation of "U.S. person."

In the Commission's view, where one or more U.S. owners has unlimited responsibility for losses or nonperformance by its majority-owned affiliate, there is generally a direct and significant connection with activities in, or effect on, commerce of the United States within the meaning of section 2(i). Therefore, for purposes of section 2(i), the majority-owned entity would appropriately be considered a "U.S. person."[213] Unlimited liability corporations where U.S. persons have direct or indirect majority ownership and any such U.S. persons have unlimited liability for the obligations and liabilities of the entity would generally be covered under this prong.[214] By contrast, a limited liability corporation or limited liability partnership would generally not be covered under this prong; the Commission also clarifies, in response to comments on the Further Proposed Guidance, that it intends that entities in other jurisdictions that are similar to limited liability corporations or limited liability partnerships in that none of the owners of such entities bear unlimited liability for the entity's obligations and liabilities would generally be excluded from this prong.

The Commission has considered the comments requesting that the interpretation include consideration of whether the U.S. person majority owners have unlimited responsibility for "all of" the obligations and liabilities of the entity in connection with this prong of the interpretation.

---

[213] When Lehman Brothers collapsed in 2008, it had a complex web of affiliates. This included LBIE, an unlimited liability company in London. At that time, it had more than 300 outstanding creditor and debtor balances with its affiliates amounting to more than $21 billion in total. What happened to LBIE is directly relevant to the current discussions about cross-border application of swaps reforms, as LBIE had more than 130,000 swaps contracts outstanding when it failed. Many of the Lehman Brothers entities were guaranteed by the parent, Lehman Brothers Holdings, in the United States. More than $28 billion in client assets and money were caught up in the bankruptcy of the UK entity. This uncertainty led, further, to a run on many other financial institutions when customers feared for their positions and collateral housed in overseas affiliates of other U.S. financial institutions. See Lehman Brothers Progress Report, note 6 and accompanying text, supra.

[214] Unlimited liability corporations include, solely by way of example, entities such as an unlimited company formed in the U.K., see Brian Stewart, Doing Business in the United Kingdom § 18.02[2][c], or an unlimited liability company formed under the law of Alberta, British Columbia, or Nova Scotia, see Richard E. Johnston, Doing Business in Canada § 15.04[5].

The Commission believes that even if there are some potential obligations and liabilities of the entity that may not flow to the U.S. persons, the risk of unlimited responsibility for other obligations and liabilities would generally be a sufficient nexus to the United States for purposes of section 2(i). Similarly, it would generally not be necessary for all the U.S. persons who are majority owners to bear unlimited responsibility (as some commenters suggested). Rather, if any of the U.S. persons who are direct or indirect majority owners bears unlimited responsibility for the obligations and liabilities of the entity, it would generally be covered by this prong of the interpretation.

In response to requests from commenters on the Proposed Guidance, the Commission clarifies that it does not intend that prong (vii) would cover legal entities organized or domiciled in a foreign jurisdiction but whose swaps obligations are guaranteed by a U.S. person.[215] To be clear, the Commission remains concerned, as explained in the Proposed Guidance, about the risks to a U.S. guarantor that flow from its guarantee of the swaps obligations of an entity that is organized or domiciled abroad.[216] Yet, a guarantee does not necessarily provide for "unlimited responsibility for the obligations and liabilities of the guaranteed entity" in the same sense that the owner of an unlimited liability corporation bears such unlimited liability.[217] The Commission believes, therefore, that its concern regarding the risks associated with guarantee

---

[215] Also, the Commission does not interpret section 2(i) to require that it treat a non-U.S. person as a "U.S. person" solely because it is controlled by or under common control with a U.S. person.

[216] See, e.g., Letter from Sen. Levin at 10 ("If a U.S.-based parent company provides an implicit or explicit guarantee, regardless of the form of the guarantee, to a non-U.S. subsidiary or affiliate, the risk is effectively transferred to the U.S. person. In such circumstances, the exact form of the guarantee should not prevent the CFTC from demanding compliance with the CFTC's derivatives safeguards.").

[217] Since a guarantee is treated in law as a contract, a guarantor may be protected by legal defenses to the enforcement of the contract. Also, in some circumstances, a guarantee may not be enforceable with respect to underlying obligations that are materially altered without the guarantor's consent. See, e.g., Debtor-Creditor Law § 44.04 (Theodore Eisenberg ed., Matthew Bender 2005).

arrangements can, consistent with CEA section 2(i) and in the interests of international comity, appropriately be addressed in a more targeted fashion without broadly treating such guaranteed entities as U.S. persons at this time.

Thus, for example, as set forth below, where a non-U.S. affiliate of a U.S. person has its swap dealing obligations with non-U.S. counterparties guaranteed by a U.S. person,[218] the guaranteed affiliate generally would be required to count those swap dealing transactions with non-U.S. counterparties (in addition to its swap dealing transactions with U.S. persons) for purposes of determining whether the affiliate exceeds a de minimis amount of swap dealing activity and must register as a swap dealer. The Commission notes that where a non-U.S. affiliate of a U.S. person has its swap dealing obligations with non-U.S. counterparties guaranteed by a U.S. person, the guarantee creates a significant risk transfer into the United States. In the absence of such guarantees, non-U.S. counterparties may be unwilling to enter into swaps with such non-U.S. affiliates. As for the substantive swaps requirements, as discussed below, Transaction-Level Requirements generally would apply to swaps between a non-U.S. swap dealer or non-U.S. MSP on the one hand, and a U.S.-guaranteed affiliate on the other hand, though such swaps may be subject to substituted compliance, as appropriate. The Commission generally expects that, in considering international comity and the factors set forth in the Restatement (e.g., the character of the activity to be regulated, the existence of justified expectations, the likelihood of conflicts with regulation by foreign jurisdictions), this approach

[218] See note 267 and accompanying text, supra, for guidance regarding the Commission's interpretation of the term "guarantee."

would strike a reasonable balance in assuring that the swaps market is brought under the new regulatory regime as directed by Congress, consistent with section 2(i) of the CEA.

Third, the Commission will include in its interpretation of the term "U.S. person" the elements in prong (iii), (renumbered as prong (viii)), substantially as proposed. Commenters did not comment on, nor object to, this prong. The Commission clarifies that it expects that this prong would encompass a joint account where any one of the beneficial owners is a U.S. person.

Fourth, the Commission will include in its interpretation of the term "U.S. person" the elements in the alternative prong (iv) that was described in the Further Proposed Guidance (renumbered in the Guidance as prong (vi)), with some modifications. The Commission understands from commenters that the determination by some collective investment vehicles of whether they are majority-owned by U.S. persons may pose practical difficulties. In response to these practical difficulties, the Commission has eliminated the reference to "indirect" majority ownership in this prong. As revised, this prong no longer refers to "direct or indirect" majority ownership by U.S. persons.

Under alternative prong (vi), any commodity pool, pooled account, investment fund or other collective investment vehicle that is majority-owned by one or more U.S. person(s)[219] would be deemed a U.S. person. For purposes of this prong, majority-owned means the beneficial ownership of more than 50 percent of the equity or voting interests in the collective investment vehicle. The Commission expects that the collective investment vehicle would: (1) determine whether its direct beneficial owners are U.S. persons described in prong (i), (ii), (iii),

---

[219] The term "U.S. person," as used in this context, refers to those natural persons or legal entities that meet (i), (ii), (iii), (iv), or (v) of the interpretation of "U.S. person."

(iv), or (v) of the term “U.S. person,” and (2) “look-through” the beneficial ownership of any other legal entity invested in the collective investment vehicle that is controlled by or under common control with the collective investment vehicle in determining whether the collective vehicle is majority-owned by U.S. persons.

For example, a limited company is formed under the laws of the Cayman Island as a collective investment vehicle that engages in swap transactions. It has a single investor, which is an investment company registered with the Securities and Exchange Commission under the Investment Company Act of 1940. Shares in the registered investment company are only owned by United States persons and both the Cayman Island limited company and the registered investment company are sponsored by the same investment adviser. The Cayman Island limited company would be viewed as a "controlled foreign corporation" of the registered investment company. Because the Cayman Island limited company is controlled by the same investment adviser as the investor registered investment company, the Cayman Island limited company would be required to "look through" the registered investment company and would be considered majority owned by U.S. persons. Therefore, under revised prong (vi), the Cayman Island limited company generally would be a U.S. person, subject to consideration of all the facts and circumstances.

As another example, a limited company is formed under the laws of the Cayman Island by an investment manager as a collective investment vehicle that engages in swap transactions as part of its investment strategy ("Master Fund"). It has two investors, which are also collective investment vehicles that were formed by the same investment manager for the purpose of investing in the Master Fund. One investor collective investment vehicle is formed under the laws of the state of Delaware and the other investor collective investment vehicle is a limited

company formed under the laws of the Cayman Island. Because Master Fund and the two investor collective investment vehicles are under common control by the investment manager, the Master Fund is required to "look through" the two investor vehicles to their beneficial owners to determine whether it is majority owned by U.S. persons. Whether the Master Fund is a U.S. person will require the assessment of whether the majority of its equity is held indirectly by U.S. persons through the two investor vehicles.

However, where a collective investment vehicle is owned in part by an unrelated investor collective investment vehicle, the collective investment vehicle need not "look through" the unrelated investor entity, but may reasonably rely upon written, bona fide representations from the unrelated investor entity regarding whether it is a U.S. person, [220] unless the investee collective investment vehicle has reason to believe that such unrelated investor entity was formed or is operated principally for the purpose of avoiding looking through to the ultimate beneficial owners of that entity.[221] The Commission expects that the collective investment vehicle would take reasonable "due diligence" steps with respect to its investors in making this determination, along the lines of the verifications that the collective investment vehicle may conduct in connection with other regulatory requirements.[222]

---

[220] The ability of the collective investment vehicle to rely on the bona fide representation of the unrelated investor entity does not affect the due diligence that the unrelated investor entity should conduct in order to make such representation to the collective investment vehicle.

[221] The Commission has applied similar anti-evasion standards in other contexts. See, e.g., 17 CFR 4.7(a)(1)(iv)(D) (providing that a passive investment vehicle will be considered a non-U.S. person for purposes of section 4.7 under certain circumstances provided that the entity was "not formed principally for the purpose of facilitating investment by persons who do not qualify as Non-United States persons in a pool" whose operator is claiming relief under that section).

[222] See the discussion of due diligence below, which the Commission believes is generally applicable to the "due diligence" required by the collective investment vehicle in this context.

The Commission is also including a minor modification to clarify that it expects that the interpretation in prong (vi) would apply irrespective of whether the collective investment vehicle is organized or incorporated in the United States. Similar to the Commission's analysis with respect to prong (vii) discussed above, the Commission's policy is that the place of a collective investment vehicle's organization or incorporation would not necessarily be determinative of its status as a "U.S. person" for purposes of CEA section 2(i). As noted above, collective investment vehicles are created for the purpose of pooling assets from investors and channeling these assets to trade or invest in line with the objectives of the investors. In the Commission's view, these are generally passive investment vehicles that serve as a means to achieve the investment objectives of their beneficial owners, rather than being separate, active operating businesses. As such, the beneficial owners would be directly exposed to the risks created by the swaps that their collective investment vehicles enter into.[223] Therefore, the Commission's policy is that if U.S. persons beneficially own more than 50 percent of the equity or voting interests in a collective investment vehicle, then the collective investment vehicle would ordinarily satisfy the "direct and significant" standard of CEA section 2(i).

---

[223] A collective investment vehicle is an arrangement pursuant to which funds of one or more investors are pooled together and invested on behalf of such investors by a manager. Typically, investors do not have day-to-day control over the management or operation of the vehicle and are essentially passive, beneficial owners of the vehicle's assets. Prior to participating in a collective investment vehicle, an investor enters into an arrangement with the vehicle which governs the fees collected by the manager of the vehicle and the investor's payout from the vehicle, which may include periodic payments. Typically a limited liability entity such as a corporation, limited partnership or limited liability company is used as part of the arrangement so that investor liability is limited to the investor's beneficial interest in the vehicle's assets.

With respect to a swap between a collective investment vehicle and a non-U.S. swap dealer, the Commission believes that losses borne by the vehicle upon a default by the non-U.S. swap dealer are better seen as losses incurred by the investors in the collective investment vehicle rather than by the vehicle itself. In contrast with a collective investment vehicle, when an operating company enters into a swap with a non-U.S. swap dealer, losses borne by the operating company upon a default by the non-U.S. swap dealer are better seen as losses incurred by the operating company and only indirectly by its shareholders. Therefore, prong (vi) only relates to collective investment vehicles and does not extend to operating companies.

The Commission is also revising its interpretation in prong (vi) to exclude non-U.S. publicly-offered, as opposed to publicly-traded, collective investment vehicles. That is, a collective investment vehicle that is publicly offered to non-U.S. persons, but not offered to U.S. persons, would generally not be included within the interpretation of the term U.S. person. This revision is intended to address comments that publicly-traded funds are only a subset of non-U.S. regulated collective investment vehicles and that ownership verification is expected to be particularly difficult for pools, funds, and other collective investment vehicles that are publicly offered.[224]

In addition, a collective investment vehicle that is publicly offered only to non-U.S. persons and not offered to U.S. persons generally would not fall within any of the prongs of the interpretation of the term "U.S. person."

Fifth, the Commission will not include in its interpretation of the term "U.S. person" the elements in proposed prong (v), which related to registered commodity pool operators. The Commission agrees with commenters that neither the location (nor the nationality), nor the registration status, of the pool operator would normally, without more, be determinative of whether the underlying pool(s) should be included in its interpretation of the term "U.S. person." The Commission has further considered that, as discussed above, the relevant elements for a commodity pool or other collective investment vehicle would generally be whether or not its principal place of business is in the United States or it is majority owned by U.S. persons. The

---

[224] The publicly-offered collective investment vehicle could be a UCITS (Undertakings for Collective Investment in Transferable Securities). See Directive 2009/65/EC of the European Parliament and of the Council (Jul. 13, 2009), available at http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:302:0032:0096:EN:PDF. Under the Commission's interpretation of section 2(i), a UCITS would not be included in the term "U.S. person," provided it is not offered, directly or indirectly, to U.S. persons.

Commission believes that proposed prong (v) could be overly broad and have the effect of capturing commodity pools with minimal participation of U.S. persons and a minimal U.S. nexus.

Sixth, the Commission will include in its interpretation of the term "U.S. person" the elements in prong (vi) (renumbered as prong (iv)) relating to pension plans. In response to comments, though, the Commission is clarifying that it does not intend that its interpretation encompass pension plans that are primarily for foreign employees of U.S.-based entities described in prong (iii) of the interpretation. Also, as noted above in the discussion of collective investment vehicles, the Commission does not generally expect that a pension plan which is not a U.S. person would become a U.S. person simply because some of the individuals or entities that manage the investments of the pension plan are located or organized in the United States.

Finally, the Commission will include in its interpretation of the term "U.S. person" the elements in prong (vii) (renumbered as prongs (ii) and (v)) pertaining to an estate or trust, with certain modifications to take into account the views of commenters who addressed this issue, and the legal and practical considerations that are relevant to the treatment of estates and trusts for purposes of the Dodd-Frank Act. The Commission agrees with the commenters who stated that treatment of an estate or trust should generally not depend on whether the income of the estate or trust is subject to U.S. tax. The Commission understands that whether income is subject to U.S. tax can depend on a variety of factors, including the source of the income, which may not be relevant to whether the Dodd-Frank Act should apply to swaps entered into by the estate or trust.

After further consideration, the Commission will include in its interpretation of the term "U.S. person" (a) an estate if the decedent was a U.S. person at the time of death and (b) a trust if it is governed by the law of a state or other jurisdiction in the United States and a court within the

United States is able to exercise primary supervision over the administration of the trust. For what it expects to be the relatively few estates that would use swaps (most likely for purposes of investment hedging), the Commission believes that the treatment of such swaps should generally be the same as for swaps entered into by the decedent during life. If the decedent was a party to any swaps at the time of death, then those swaps should generally continue to be treated in the same way after the decedent's death, when the swaps would most likely pass to the decedent's estate. Also, the Commission expects that this element of the interpretation will be predictable and easy to apply for natural persons planning for how their swaps will be treated after death, for executors and administrators of estates, and for the swap counterparties to natural persons and estates.

With respect to trusts, the Commission expects that its approach would be in line with how trusts are treated for other purposes under law. The Commission has considered that each trust is governed by the laws of a particular jurisdiction, which may depend on steps taken when the trust was created or other circumstances surrounding the trust. The Commission believes that if a trust is governed by U.S. law (i.e., the law of a state or other jurisdiction in the United States), then it would generally be reasonable to treat the trust as a U.S. person for purposes of the Dodd-Frank Act. Another relevant element in this regard would be whether a court within the United States is able to exercise primary supervision over the administration of the trust.[225] The Commission expects that including this element of the interpretation would generally align

[225] The Commission is aware that one element applied by the Internal Revenue Service to determine if a trust is a U.S. person for tax purposes depends on whether a court within the United States is able to exercise primary supervision over the administration of the trust. See 26 CFR 301.7701-7(a)(1)(i). The Commission believes that precedents developed under tax law could be relevant, as appropriate, in applying this aspect of its interpretation of the term "U.S. person." However, the Commission does not intend to formally adopt the Internal Revenue Service test for this purpose.

the treatment of the trust for purposes of the Dodd-Frank Act with how the trust is treated for other legal purposes. For example, the Commission expects that if a person could bring suit against the trustee for breach of fiduciary duty in a U.S. court (and, as noted above, the trust is governed by U.S. law), then treating the trust as a U.S. person would generally be in line with how it is treated for other purposes.

The Commission disagrees with commenters that the status of an estate or trust should be based solely on the status of the executor, administrator or trustee.[226] For one thing, this would mean that the treatment of the estate or trust could change if, for example, the executor or trustee relocates its offices. The Commission also does not believe it would be appropriate that the treatment of a trust would depend solely on the identity of the beneficiaries to the trust because, among other reasons, the beneficiaries may be described as a class of persons, rather than particular persons. In the Commission's view, more important considerations in formulating its policy are whether the treatment of the estate or trust is predictable and whether it is in line with how the entity is treated for other purposes. The Commission would also consider other facts and circumstances related to the estate or trust that could be relevant to whether the entity should be within the interpretation of the term "U.S. person" in the context of section 2(i).

**a. Due Diligence**

As described above, many commenters indicated that the information necessary to accurately assess the status of their counterparties as U.S. persons may not be available, or may be available only through overly burdensome due diligence, particularly where the interpretation

[226] The Commission does not intend to preclude considerations relating to the trustee in determining whether the trust is governed by U.S. law or subject to the jurisdiction of U.S. courts, if any such considerations are relevant. Rather, the Commission believes that the status of the trustee would generally not be directly relevant to determining if a trust should be treated as a U.S. person.

includes a "look-through" element that considers "direct and indirect" ownership. For this reason, these commenters requested that the Commission's policy contemplate reasonable reliance on counterparty representations as to the relevant elements of the interpretation of the term "U.S. person."

The Commission agrees with the commenters that a party to a swap should generally be permitted to reasonably rely on its counterparty's written representation in determining whether the counterparty is within the Commission's interpretation of the term "U.S. person." In this context, the Commission's policy is to interpret the "reasonable" standard to be satisfied when a party to a swap conducts reasonable due diligence on its counterparties, with what is reasonable in a particular situation to depend on the relevant facts and circumstances. The Commission notes that under the External Business Conduct Rules, a swap dealer or MSP generally meets its due diligence obligations if it reasonably relies on counterparty representations, absent indications to the contrary.[227] As in the case of the External Business Rules, the Commission believes that allowing for reasonable reliance on counterparty representations encourages objectivity and avoids subjective evaluations, which in turn facilitates a more consistent and foreseeable determination of whether a person is within the Commission's interpretation of the

---

[227] See Business Conduct Standards for Swap Dealers and Major Swap Participants with Counterparties, 77 FR 9734 (Feb. 17, 2012) ("External Business Conduct Rules"). Consistent with the "reasonable reliance" standard in the External Business Conduct Rules, a swap dealer or MSP may rely on the written representations of a counterparty to satisfy its due diligence requirements. However, a swap dealer or MSP should not rely on a written representation if it has information that would cause a reasonable person to question the accuracy of the representation. In other words, a swap dealer or MSP should not ignore red flags when relying on written representations to satisfy its due diligence obligations. Further, if agreed to by the counterparty, the written representations may be included in counterparty relationship documentation. However, a swap dealer or MSP may only rely on such representations in the counterparty relationship documentation if the counterparty agrees to timely update any material changes to the representations. In addition, the Commission expects swap dealers and MSPs to review the written representations on a periodic basis to ensure that they remain appropriate for the intended purpose.

term "U.S. person" and the extent to which the Title VII requirements apply to certain cross-border activities.[228]

**b. Foreign Branch of U.S. Person**

The Commission is confirming its interpretation, as proposed, that a foreign branch of a U.S. person is itself a "U.S. person." As the Commission explained in the Proposed Guidance, a branch does not have a legal identity separate from that of its principal entity. In this respect, the Commission notes that branches are neither separately incorporated nor separately capitalized and, more generally, the rights and obligations of a branch are the rights and obligations of its principal entity (and vice versa). Under these circumstances, the Commission views the activities of a foreign branch as the activities of the principal entity, and thus a foreign branch of a U.S. person is a U.S. person.

Accordingly, the Commission declines to recognize foreign branches of U.S. persons separately from their U.S. principal for purposes of registration. That is, if the foreign branch were to be a swap dealer or MSP, as discussed further below, the U.S. person would be required to register, and the registration would encompass the foreign branch. Upon consideration of principles of international comity and the factors set forth in the Restatement, though, the Commission has calibrated the requirements otherwise applicable to such foreign branches in respects other than broadly excluding them from the U.S. person interpretation. For example, as discussed further below, foreign branches of U.S. persons may comply with Transaction-Level Requirements through substituted compliance, where appropriate, with respect to swaps with

[228] This approach is generally consistent with suggestions provided by commenters. For example, SIFMA suggested that the determination of whether a counterparty is a U.S. person should be made at the inception of the swap transaction based on the most recent representation from the counterparty, which should be renewed by the counterparty once per calendar year. See SIFMA (Aug. 27, 2012) at A17.

foreign counterparties, as well as with a foreign branch of another U.S. person. Further, non-U.S. persons may exclude swaps with foreign branches of registered swap dealers for purposes of determining whether they have exceeded the de minimis level of swap dealing activity under the swap dealer definition.

The types of offices the Commission would consider to be a "foreign branch" of a U.S. bank, and the circumstances in which a swap is with such foreign branch, are discussed further below in section C below.

**c. Regulation S**

The Commission has considered the recommendation by several commenters that the Commission follow, entirely or to some extent, the definition of "U.S. person" in the SEC's Regulation S.[229] With respect to the treatment of foreign branches in particular, Regulation S excludes from its definition of "U.S. person" any agency or branch of a U.S. person located outside the United States if (1) the agency or branch operates for valid business reasons; and (2) the agency or branch is engaged in the business of insurance or banking, and is subject to substantive insurance or banking regulation in the jurisdiction where it is located.[230] As the Commission noted in the Proposed Guidance, however, Regulation S addresses the level of activities (i.e., offerings of securities) conducted within the United States, and related customer protection issues.[231] As such, the regulation's territorial approach to determining U.S. person

---

[229] See, e.g., MFA/AIMA (Aug. 28, 2012) at 4, 8-9; IIAC (Aug. 27, 2012) at 3; J.P. Morgan (Aug. 27, 2012) at 3, 8-9; SocGen (Aug. 8, 2012) at 5; ISDA (Aug. 10, 2012) at 9. See also IIB (Aug. 9, 2012) at 3 (noting that the proposed interpretation is more expansive than other Commission and SEC definitions of "U.S. person" and makes it difficult to assess U.S. person status). Regulation S is codified at 17 CFR 230.901 et seq.

[230] See 17 CFR 230.902(k)(2)(v).

[231] See Offshore Offers and Sales, 55 FR 18306 (May 2, 1990).

status is, in the Commission's view, unsuitable for purposes of interpreting section 2(i), which addresses the connection with activities in and the risks to U.S. commerce arising from activities outside the United States.

Similarly, Regulation S and the Dodd-Frank swaps provisions also serve fundamentally different regulatory objectives with respect to the treatment of collective investment vehicles. Under Regulation S, the SEC will consider certain investment funds and securities issuers that are organized in foreign jurisdictions, but owned by U.S. investors, to be U.S. persons unless the U.S. investors are accredited investors.[232] The accredited investor condition provides a level of assurance that U.S. investors are entities that understand the consequences of investing through a foreign entity and, in effect, may be deemed to have waived the benefits of the U.S. securities laws. In contrast, the focus of Title VII is not limited to customer protection. Whether or not the investors in a collective investment vehicle are accredited investors, in the Commission's view, is irrelevant; rather, under section 2(i), the focus is whether the swap activities of a collective investment vehicle have a direct and significant connection with activities in, or effect on, U.S. commerce.

The Commission understands that the Regulation S definition of "U.S. person" is generally understood and applied by market participants. However, as the foregoing examples demonstrate, the Regulation S definition of "U.S. person" could fail to capture persons whose activities, the Commission believes, meet the "direct and significant" jurisdictional test of CEA section 2(i) – and whose activities present the type of risk that Congress addressed in Title VII.

---

[232] See 17 CFR 230.902(k)(1)(viii). Also, the exception from the Regulation S definition of "U.S. person" is not available if any of such accredited investors are natural persons, estates or trusts. Id.

This potential for underinclusion, together with the fact that the Commission has addressed commenter concerns by providing further details and guidance about its interpretation of the term "U.S. person," which the Commission expects will facilitate a more consistent understanding of that term among market participants, provides the basis for not importing the Regulation S definition into the Commission's interpretation of CEA section 2(i).

**d. Other Clarifications**

The Commission continues to include the prefatory phrase "include, but not be limited to" in its interpretation of the term "U.S. person," as it appeared in the Proposed Guidance. While the Commission's policy generally is to limit its interpretation of this term, for purposes of this Guidance, to persons encompassed within the several prongs discussed above, the Commission also expects that there may be circumstances that are not fully addressed by those prongs, or other situations where the interpretation discussed above does not appropriately resolve whether a person should be included in the interpretation of the term "U.S. person." Thus, the Commission continues to include the prefatory phrase to indicate that there may be situations where a person not fully described in the interpretation above is appropriately treated as a "U.S. person" for purposes of this Guidance in view of the relevant facts and circumstances and a balancing of the various regulatory interests that may apply. In these situations, the Commission anticipates that the relevant facts and circumstances may generally include the strength of the connections between the person's swap-related activities and U.S. commerce; the extent to which such activities are conducted in the United States; the importance to the United States (as compared to other jurisdictions where the person may be active) of regulating the

person's swap-related activities; the likelihood that including the person within the interpretation of "U.S. person" could lead to regulatory conflicts; and considerations of international comity.[233] The Commission anticipates that it would also likely be helpful to consider how the person (and in particular its swap activities) is currently regulated, and whether such regulation encompasses the person's swap activities as they relate to U.S. commerce.

Finally, in response to commenters' requests for clarification regarding the scope of the applicability of the "U.S. person" interpretation,[234] the Commission confirms that its policy is to apply its interpretation of the term "U.S. person" only to swaps regulations promulgated under Title VII, unless provided otherwise in any particular regulation. Therefore, for example, the Commission does not intend that this Guidance address how the term "person" or "U.S. person" should be interpreted in connection with any other CEA provisions or Commission regulations promulgated thereunder.

4. **Summary**

In summary, for purposes of the application of CEA section 2(i), the Commission will interpret the term "U.S. person" generally to include, but not be limited to[235]:

(i) any natural person who is a resident of the United States;

---

[233] These factors are among those relevant to whether a country has a basis to assert jurisdiction over an activity under the Restatement. See generally note 86 and accompanying text, supra.

[234] See, e.g., Goldman (Aug. 27, 2010) at 3, FOA (Aug. 13, 2012) at 10-11; SIFMA (Aug. 27, 2012) at A14-15, FIA (Aug. 27, 2012) at 2-5.

[235] The Commission believes that Commission regulation 140.99, which provides for persons to request that the staff of the Commission provide written advice or guidance, would be an appropriate mechanism for a person to seek guidance as to whether it is a U.S. person for purposes of applying the Commission swaps regulations promulgated under Title VII.

(ii) any estate of a decedent who was a resident of the United States at the time of death;

(iii) any corporation, partnership, limited liability company, business or other trust, association, joint-stock company, fund or any form of enterprise similar to any of the foregoing (other than an entity described in prongs (iv) or (v), below) (a "legal entity"), in each case that is organized or incorporated under the laws of a state or other jurisdiction in the United States or having its principal place of business in the United States;

(iv) any pension plan for the employees, officers or principals of a legal entity described in prong (iii), unless the pension plan is primarily for foreign employees of such entity;

(v) any trust governed by the laws of a state or other jurisdiction in the United States, if a court within the United States is able to exercise primary supervision over the administration of the trust;

(vi) any commodity pool, pooled account, investment fund, or other collective investment vehicle that is not described in prong (iii) and that is majority-owned by one or more persons described in prong (i), (ii), (iii), (iv), or (v), except any commodity pool, pooled account, investment fund, or other collective investment vehicle that is publicly offered only to non-U.S. persons and not offered to U.S. persons;

(vii) any legal entity (other than a limited liability company, limited liability partnership or similar entity where all of the owners of the entity have limited liability) that is directly or indirectly majority-owned by one or more persons

described in prong (i), (ii), (iii), (iv), or (v) and in which such person(s) bears unlimited responsibility for the obligations and liabilities of the legal entity; and

(viii) any individual account or joint account (discretionary or not) where the beneficial owner (or one of the beneficial owners in the case of a joint account) is a person described in prong (i), (ii), (iii), (iv), (v), (vi), or (vii).

Under this interpretation, the term "U.S. person" generally means that a foreign branch of a U.S. person would be covered by virtue of the fact that it is a part, or an extension, of a U.S. person.

For convenience of reference, this Guidance uses the terms "U.S. swap dealer" and "U.S. MSP" to refer to swap dealers and MSPs, respectively, that are within the Commission's interpretation of the term "U.S. person" under this Guidance. The terms "non-U.S. swap dealer" and "non-U.S. MSP" refer to swap dealers and MSPs, respectively, that are not within the Commission's interpretation of the term "U.S. person" under this Guidance; and the term "non-U.S. person" refers to a person that is not within the Commission's interpretation of the term "U.S. person" under this Guidance.

### B. Registration

#### 1. Proposed Guidance

Under section 2(i) of the CEA, the Dodd-Frank swaps provisions, including the swap dealer and MSP registration provisions, do not apply to activities overseas unless such activities have a "direct and significant connection with activities in, or effect on," U.S. commerce. In the Proposed Guidance, the Commission addressed the general manner in which a person's overseas swap dealing activities or positions may require registration as a swap dealer or MSP, respectively. Specifically, under the Proposed Guidance, the Commission would expect that a

non-U.S. person whose swap dealing transactions with U.S. persons exceed the de minimis threshold would register as a swap dealer.[236] Likewise, under the Proposed Guidance, the Commission would expect that a non-U.S. person who holds swaps positions where one or more U.S. persons are counterparties above the specified MSP thresholds would register as an MSP.[237] As explained in the Proposed Guidance, the Commission believes that, consistent with section 2(i), the level of swap dealing or positions that is sufficient to require a person to register as a swap dealer or MSP when conducted by a person located in the United States would generally also meet the "direct and significant" nexus when such activities are conducted by a non-U.S. person with a U.S. person and in some other limited circumstances.

In the consideration of whether a non-U.S. person is engaged in more than a de minimis level of swap dealing, the Proposed Guidance would generally include the notional value of any swaps between such non-U.S. person (or any of its non-U.S. affiliates under common control) and a U.S. person (other than a foreign branch of a registered swap dealer).[238] Further, where the potential non-U.S. swap dealer's obligations are guaranteed by a U.S. person, the Commission would expect that the non-U.S. person would register with the Commission as a swap dealer when the aggregate notional value of its swap dealing activities (along with the swap dealing activities of its non-U.S. affiliates that are under common control and also guaranteed by a U.S. person) with U.S. persons and non-U.S. persons exceeds the de minimis threshold. Additionally, the Proposed Guidance clarified that the Commission would not expect a non-U.S. person without a guarantee from a U.S. person to register as a swap dealer if it does not engage in swap

---

[236] See Proposed Guidance, 77 FR at 41218-19.

[237] Id.

[238] Id. at 41218-20.

dealing with U.S. persons as part of "a regular business" with U.S. persons, even if the non-U.S. person engages in dealing with non-U.S. persons.

Following a similar rationale, under the Proposed Guidance if a non-U.S person holds swaps positions above the requisite threshold, the Commission would expect such non-U.S. person to register as an MSP. In considering whether a non-U.S. person that is a potential MSP meets the applicable threshold, under the Proposed Guidance, the non-U.S. person would have included the notional value of: (1) any swaps entered into between such non-U.S. person and a U.S. person (provided that if the non-U.S. person's swaps are guaranteed by a U.S. person, then such swaps will be attributed to the U.S. guarantor and not the potential non-U.S. MSP); and (2) any swaps between another non-U.S. person and a U.S. person if the potential non-U.S. MSP guarantees the obligations of the other non-U.S. person thereunder.[239]

2. **Comments**

In general, commenters on the Proposed Guidance did not raise concerns or objections to the Commission's interpretation that non-U.S. persons who engage in more than a de minimis level of swap dealing with U.S. persons should be expected to register as swap dealers.[240] A number of commenters argued, however, that a non-U.S. person should not be expected to register as a swap dealer solely by reason of being guaranteed by a U.S. person.[241] SIFMA stated

---

[239] Id. at 41221.

[240] One commenter, Japanese Bankers Association, stated that the cross-border application of Dodd-Frank is overbroad because it would capture even hedging transactions made by a non-U.S. swap dealer with a U.S. swap dealer that is making a market. The definition of "dealing activity" is ambiguous, this commenter asserted, and might require the non-U.S. swap dealer to register. See Japanese Bankers Association (Aug. 27, 2012) at 1.

[241] See, e.g., Goldman (Aug. 27, 2012) at 5; ISDA (Aug. 10, 2012) at 12 (stating that, in the typical case, an intra-group guarantee allocates risks and activities within the corporate group and is not a dealing activity of the non-U.S. person); CEWG (Aug. 27, 2012) at 6-7 (stating that the Proposed Guidance should not include swap guarantees for aggregation purposes because it is contrary to the Final Entities Rules; jurisdiction should not be extended to

that the "connection between a non-U.S. swap dealing entity and its U.S. guarantor creates too tenuous a nexus to justify registration on the basis of this relationship alone."[242] As an alternative, SIFMA posited that only guarantees by a U.S. person for which there is a material likelihood of payment by the U.S. guarantor should be counted towards the de minimis calculation. To implement this recommendation, SIFMA suggested that the Commission establish how to determine whether the likelihood of payment is remote, such as a comparison of the aggregate contingent liability of the U.S. person guarantor to the net equity of that guarantor.[243]

Similarly, Goldman argued that it would be inconsistent with the Dodd-Frank Act to expect non-U.S. persons to register as swap dealers solely on the basis of guarantees by a U.S. parent, absent any showing of a "direct and significant" jurisdictional nexus. Goldman recommended that any concerns regarding potential evasion of the registration requirement be addressed through the Commission's exercise of its anti-evasion authority.[244] ISDA agreed, suggesting that rather than protecting the U.S. guarantor by encouraging swap dealer registration of the guaranteed non-U.S. person, a better course is addressing the question of when (if ever)

---

transactions between two non-U.S. persons if the swaps obligations of one party are guaranteed by a U.S. person because U.S. jurisdiction in these circumstances is not supported by law or existing conventions of international jurisdiction).

[242] SIFMA (Aug. 27, 2012) at A29.

[243] Id. at A29-30.

[244] Goldman (Aug 27, 2012) at 5. See also CEWG (Aug. 27, 2012) 6-7 (stating that because there is no legal basis under section 2(i) for asserting jurisdiction based on a guaranty, the Commission should amend the Proposed Guidance to clarify that a non-U.S. person is not subject to Commission regulation, even where a U.S. person guarantees either counterparty; swap dealing activity outside the United States that does not involve a U.S. person should not be subject to the Commission's jurisdiction; guarantees do not alter the location of activity, nor should they alter a participant's residency); Hong Kong Banks (Aug. 27, 2012) at 8 (arguing that swaps between non-U.S. persons should be excluded from the de minimis determination regardless of whether a counterparty is guaranteed).

the U.S. guarantor must register as a swap dealer.[245] Australian Bankers stated that the considerations relevant to whether a non-U.S. person (without a guarantee from a U.S. affiliate) is expected to register as a swap dealer should relate to the aggregate notional amount of swap dealing activities with U.S. persons within a particular asset class.[246]

IIAC requested that the Commission confirm that a guarantee by a foreign holding company would not be deemed to be a guarantee by all of its subsidiaries, including U.S. entities, solely as a result of the indirect ownership.[247] J.P. Morgan raised concerns regarding the scope of the interpretation of the term a "guarantee." Specifically, it argued that the term "guarantee" should not be interpreted to include keepwells and liquidity puts because these agreements do not create the same types of third-party rights as traditional guarantees and may be unenforceable by third parties.[248] CEWG objected to the broader interpretation of the term "guarantee" in the Proposed Guidance than under the Final Product Definitions Rules,[249] stating that the Commission "must undertake a more thorough regulatory analysis with respect to guarantees of swaps obligations."[250]

On the other hand, Senator Levin stated that guarantees are central to concerns regarding cross-border swaps, and that any guarantee, implicit or explicit, by a U.S. parent company to its

---

[245] ISDA (Aug. 10, 2012) at 12.

[246] Australian Bankers (Aug. 27, 2012) at 4.

[247] IIAC (Aug. 27, 2012) at 6, 8.

[248] J.P. Morgan (Aug. 27, 2012) at 10.

[249] See Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping; Final Rule, 77 FR 48208 (Aug. 13, 2012) ("Final Swap Definition").

[250] CEWG (Aug. 27, 2012) at 5.

non-U.S. affiliates effectively transfers risk to the U.S. parent.[251] Therefore, Senator Levin stated that the exact form of the guarantee should not limit compliance with Dodd-Frank requirements, and the list of relevant guarantee arrangements should be expanded to include arrangements involving total return swaps, credit default swaps or customized options that result in the foreign affiliate's activities creating off balance sheet liabilities for a U.S. person.[252] Eight Senators commented that focusing on whether affiliates are explicitly "guaranteed" by a U.S. affiliate does not go far enough. They expressed concern that market pressures cause U.S. parent firms to stand behind their foreign affiliates even if explicit guarantees are not in place. The Senators suggested that other factors be considered to determine whether risk is effectively guaranteed such as: limitations on permissible transactions between the parent and affiliate; explicit non-guarantee disclosures to investors, regulators and counterparties; restrictions on operating under a common name or sharing employees and officers; and whether comprehensive resolution protocols exist in the foreign jurisdiction.[253]

AFR stated that the Commission's failure to clarify its interpretation of when affiliates of a "U.S. person" would be treated as guaranteed, or to capture "the large grey area" between explicit and informal guarantees, among other things, creates opportunities to escape Dodd-Frank regulations by shifting business overseas.[254] AFR stressed that the Commission should clarify in the guidance that it "intends to follow through on properly implementing these principles and will not enable a 'race to the bottom' in which incentives are created for

---

[251] Letter from Sen. Levin at 10.

[252] Id. at 11.

[253] Letter from Senators Blumenthal, Boxer, Feinstein, Harkin, Levin, Merkley, Shaheen, and Warren (Jul. 3, 2013).

[254] AFR (Aug. 27, 2012) at 4.

derivatives affiliates of global banks … to relocate to areas of lax regulation to take advantage of an inadequate 'substituted compliance' regime."[255]

### 3. Commission Guidance

#### a. Registration Thresholds for U.S. Persons and Non-U.S. Persons, Including Those Guaranteed by U.S. Persons

Under the Final Entities Rules, a person is required to register as a swap dealer if its swap dealing activity activities over the preceding 12 months exceeds the de minimis threshold of swap dealing. In addition, Commission regulation 1.3(ggg)(4) requires that a person include, in determining whether its swap dealing activities exceed the de minimis threshold, the aggregate notional value of swap dealing transactions entered by its affiliates under common control.[256]

For purposes of determining whether a U.S. person is required to register as a swap dealer, a U.S. person should count all of its swap dealing activity, whether with U.S. or non-U.S. counterparties. This interpretation reflects that swaps markets are global, and therefore, in the Commission's view, all of a U.S. person's swap dealing activities, whether with U.S. persons or non-U.S. persons, have the requisite jurisdictional nexus and potential to impact the U.S. financial system. Similarly, the Commission believes that all of the swap dealing activities of a non-U.S. person that is an affiliate of a U.S. person and that is guaranteed by a U.S. person (a "guaranteed affiliate"),[257] or that is an "affiliate conduit" of a U.S. person,[258] have the requisite

---

[255] Id. at 4.

[256] As discussed in greater detail below, in light of the global nature of the swaps markets, the Commission's policy is to interpret the aggregation requirement in Commission regulation 1.3(ggg)(4) in a manner that applies the same aggregation principles to all affiliates in a corporate group, whether they are U.S. or non-U.S. persons.

[257] See note 267 and accompanying text, supra, for guidance regarding the Commission's interpretation of the term "guarantee."

statutory nexus and potential to impact the U.S. financial system. Therefore, under the Commission's interpretation of 2(i), a guaranteed or conduit affiliate[259] should count swap dealing transactions towards the de minimis threshold for swap dealer registration in the same manner as a U.S. person. That is, in light of the global nature of the swaps markets, a guaranteed or conduit affiliate should count all of its swap dealing transactions, whether with U.S. or non-U.S. counterparties, towards the de minimis threshold for swap dealer registration.

However, under the Commission's interpretation of section 2(i), a more circumscribed registration policy applies to non-U.S. persons that are not guaranteed or conduit affiliates. In this case, the Commission believes that the non-U.S. person should count only its swap dealing transactions with U.S. persons (other than foreign branches of swap dealers that are registered with the Commission), and with guaranteed affiliates towards the de minimis thresholds for swap dealer registration, with three exceptions, which are described below. Non-U.S. persons that are not guaranteed or conduit affiliates are not required to count swaps with a conduit affiliate towards the swap dealer de minimis calculation.

Similarly, for purposes of determining whether a U.S. person is required to register as an MSP, as the Commission interprets section 2(i), a U.S. person and a guaranteed or conduit

---

[258] When a non-U.S. person generally would be considered to be an affiliate conduit is discussed below in section G. As discussed below, for the purposes of the Commission's interpretation of CEA section 2(i), the Commission believes that certain factors are relevant to considering whether a non-U.S. person is an "affiliate conduit." Such factors include whether: the non-U.S. person is a majority-owned affiliate of a U.S. person; the non-U.S. person is controlling, controlled by or under common control with the U.S. person; the financial results of the non-U.S. person are included in the consolidated financial statements of the U.S. person; and the non-U.S. person, in the regular course of business, engages in swaps with non-U.S. third-parties for the purpose of hedging or mitigating risks faced by, or to take positions on behalf of, its U.S. affiliate(s), and enters into offsetting swaps or other arrangements with its U.S. affiliate(s) in order to transfer the risks and benefits of such swaps with third-parties to its U.S. affiliates. The term "conduit affiliate" generally would not include swap dealers or affiliates thereof.

[259] This Guidance uses the term "guaranteed or conduit affiliate" to refer to a non-U.S. person whose swap obligations are guaranteed by a U.S. person or that is an affiliate conduit.

affiliate should include all of swap positions with counterparties, whether they are U.S. or non-U.S. persons. With respect to whether a non-U.S. person must calculate whether its swap positions create exposures above the relevant MSP thresholds, the Commission believes, for policy reasons and consistent with principles of international comity, that CEA section 2(i) should not be interpreted to require non-U.S. persons that are not financial entities to include for MSP calculation purposes certain swap positions as explained below.

As the Commission explained in the Proposed Guidance, in the event of a default or insolvency of a non-U.S. swap dealer with more than a de minimis level of swap dealing with U.S. persons, or a non-U.S. MSP with more than the threshold level of swaps positions with U.S. persons, the swap dealer's or MSP's U.S. counterparties could be adversely affected. Such an event may adversely affect numerous persons engaged in commerce within the United States, disrupt such commerce, and increase the risk of a widespread disruption to the financial system in the United States.

Similar effects on U.S. persons and on the U.S. financial system may occur in the event of a default or insolvency of certain non-U.S. person with respect to swap dealing transactions in excess of the de minimis level, or swaps positions above the MSP threshold, entered into such non-U.S. persons with other non-U.S. persons whose swaps obligations are guaranteed by a U.S. person. The Commission interprets section 2(i) of the CEA to encompass swaps entered into by guaranteed or conduit affiliates in addition to encompassing swaps entered into by U.S. persons. In the final rule to further define the term "swap," the Commission found that a guarantee of a swap is a term of that swap that affects the price or pricing attributes of that swap, and that when

a swap has the benefit of a guarantee, the guarantee is an integral part of that swap.[260] The Commission therefore interprets the term "swap" (that is not a security-based swap or mixed swap) "to include a guarantee of such swap, to the extent that a counterparty to a swaps position would have recourse to the guarantor in connection with the position."[261] Because a guarantee of a swap is an integral part of the swap, and counterparties may not otherwise be willing to enter into a swap with the guaranteed affiliate, the affiliate would not have significant swap business if not for the guarantee. The Commission believes that swap activities outside the United States that are guaranteed by U.S. persons would generally have a direct and significant connection with activities in, or effect on, U.S. commerce in a similar manner as the underlying swap would generally have a direct and significant connection with activities in, or effect on, U.S. commerce if the guaranteed counterparty to the underlying swap were a U.S. person.[262] Similarly, the Commission believes that swap activities outside the United States of an affiliate conduit would

---

[260] See Final Swap Definition, 77 FR at 48225-26. The Commission explained that when a swap counterparty typically uses a guarantee as credit support for its swaps obligations, the guarantor's resources are added to the analysis of the swap because "the market will not trade with that counterparty at the same price, on the same terms, or at all without the guarantee." Id. The Commission stated that it viewed a guarantee as, generally, "a collateral promise by a guarantor to answer for the debt or obligation of a counterparty obligor under a swap." Id.

[261] Id. at 48226 n. 187. In response to a comment that guarantees are contingent obligations that do not necessarily replicate the economics of the underlying swap, the Commission stated:

> The CFTC is persuaded that when a swap (that is not a security-based swap or mixed swap) has the benefit of a guarantee, the guarantee and related guaranteed swap must be analyzed together. The events surrounding the failure of [AIGFP] highlight how guarantees can cause major risks to flow to the guarantor. The CFTC finds that the regulation of swaps and the risk exposures associated with them, which is an essential concern of the Dodd- Frank Act, would be less effective if the CFTC did not interpret the term "swap" to include a guarantee of a swap.

Id. at 48226.

[262] Congress has recognized the significance of guarantees of swaps obligations with respect to the activities of financial entities in section 210(c)(16) of the Dodd-Frank Act. There, Congress specifically addressed guarantees in the context of a Title II resolution proceeding. Section 210(c)(16) provides that, where a financial institution is in FDIC receivership, a "qualified financial contract" (or "QFC," which includes swaps) with a subsidiary of that financial institution that is guaranteed by the financial institution cannot be terminated by a counterparty facing that subsidiary pursuant to the QFC based solely on the insolvency or receivership of the financial institution if certain conditions are satisfied.

generally have a direct and significant connection with activities in, or effect on, U.S. commerce in a similar manner as would be the case if the affiliate conduit's U.S. affiliates entered into the swaps directly.

Accordingly, under section n2(i), the Commission intends to interpret section 2(i) as applying the swaps provisions of the CEA to swaps that are entered into by guaranteed or conduit affiliates in a manner similar to how section 2(i) would apply if a U.S. person had entered into the swap (subject to appropriate considerations of international comity for non-guaranteed, non-U.S. persons facing such guaranteed or conduit affiliates, as discussed below).

Thus, in the case of a guaranteed or conduit affiliate, the Commission interprets CEA section 2(i) to provide that the guaranteed or conduit affiliate is expected to count toward the swap dealer de minimis threshold all of its swap dealing activities.[263] Following a similar rationale, the Commission interprets CEA section 2(i) to provide that a guaranteed or conduit affiliate, in calculating whether the applicable MSP threshold is met, would be expected to include, and attribute to the U.S. guarantor, the notional value of: (1) all swaps with U.S. and non-U.S. counterparties, and (2) any swaps between another non-U.S. person and a U.S. person

---

[263] The Commission notes that the SEC Cross-Border Proposal agrees that "[i]n a security-based swap transaction between two non-U.S. persons where the performance of at least one side of the transaction is guaranteed by a U.S. person, … the guarantee creates risk to the U.S. financial system and counterparties (including U.S. guarantors) to the same degree as if the transaction were entered into directly by a U.S. person." SEC Cross-Border Proposal, 78 FR at 30986. However, the SEC does not propose to address the risk posed by the guarantee through requiring the non-U.S. guaranteed affiliate to register as a security-based swap dealer, but rather through the application of principles of attribution in the major security-based swap participant definition. See id. at 31006.

The Commission believes that while the SEC's proposed approach may be appropriate for the securities-based swaps market, it would not be desirable to follow a similar approach for the swaps markets within the Commission's jurisdiction. Due to the differing characteristics of the markets, such as the involvement of a much larger and more diverse number of commercial companies using swaps as compared to security-based swaps, the risks that may be transmitted through the interconnected financial system from the non-U.S. guaranteed affiliate operating as a swap dealer to the U.S. swaps market may not be adequately managed by the MSP structure, which has relatively high exposure thresholds before registration is required.

or guaranteed affiliate, if the potential non-U.S. MSP guarantees the obligations of the other non-U.S. person thereunder.

In the Final Swap Definition, the Commission also acknowledged that a "full recourse" guarantee would have a greater effect on the price of a swap than a "limited" or "partial recourse" guarantee, yet nevertheless determined that the presence of any guarantee with recourse, no matter how robust, is price forming and an integral part of a guaranteed swap.[264] Moreover, as the recent financial crisis has demonstrated, in a moment of crisis – whether at the firm-level or more generally, market-wide – it matters little whether the parent guarantees are capped or otherwise qualified. In the face of solvency concerns, the parent guarantor will find it necessary to assume the liabilities of its affiliates.[265] For these reasons, the Commission declines to incorporate in the Guidance commenters' suggestions that only certain types of guarantees (e.g., under which there is a material likelihood of liability) should be considered for purposes of registration determinations for non-U.S. persons.

Finally, with respect to the Japanese Bankers Association's concern about potential constraints on their hedging activities, the Commission contemplates that swaps that are between foreign branches of U.S. swap dealers and dealing non-U.S. persons generally will be excluded

---

[264] Final Swap Definition, 77 FR at 48226.

[265] According to one commenter, these concerns may be present even where a guarantee is implicit, but not explicitly provided:

> A recent example of the importance of implicit guarantees is the collapse of Bear Stearns, which was brought down by the failure of non-guaranteed hedge fund affiliates. These hedge funds were foreign affiliates technically not guaranteed by the parent, and the investment by the parent company in the funds was minimal. However, the firm was forced to try to save the funds for reputational reasons and also because a fire sale of subsidiary assets could have seriously impacted correlated positions held by the parent company…. The example of Bear Stearns is only one among many instances where parent companies have been forced to rescue failing affiliates even in the absence of an explicit guarantee.

AFR (Aug. 27, 2012) at 8. See also Letter from Sen. Levin, note 216, supra.

from the swap dealer registration determination, as further described below. The Commission believes that under section 2(i) of the CEA, it would generally be appropriate for non-U.S. market participants, such as members of the Japanese Bankers Association, to engage in hedging activities with foreign branches of U.S. swap dealers without being expected to count such transactions for purposes of the swap dealer registration determination.

The Commission also is affirming that, for purposes of this Guidance, the Commission would interpret the term "guarantee" generally to include not only traditional guarantees of payment or performance of the related swaps, but also other formal arrangements that, in view of all the facts and circumstances, support the non-U.S. person's ability to pay or perform its swap obligations with respect to its swaps.[266] The Commission believes that it is necessary to interpret the term "guarantee" to include the different financial arrangements and structures that transfer risk directly back to the United States. In this regard, it is the substance, rather than the form, of the arrangement that determines whether the arrangement should be considered a guarantee for purposes of the application of section 2(i).[267]

**b. Aggregation**

Commission regulation 1.3(ggg)(4) requires that a person include, in determining whether its swap dealing activities exceed the de minimis threshold, the aggregate notional value

---

[266] See Proposed Guidance, 77 FR at 41221 n. 47.

[267] Thus, for example, while keepwells and liquidity puts, certain types of indemnity agreements, master trust agreements, liability or loss transfer or sharing agreements, and any other explicit financial support arrangements may provide for different third-party rights and/or address different risks than traditional guarantees, the Commission does not believe that these differences would generally be relevant for purposes of section 2(i). Under these agreements or arrangements, one party commits to provide a financial backstop or funding against potential losses that may be incurred by the other party, either from specific contracts or more generally. In the Commission's view, this is the essence of a guarantee.

of swap dealing transactions entered by its affiliates under common control.[268] Additionally, under the Proposed Guidance, a non-U.S. person, in determining whether its swap dealing transactions exceed the de minimis threshold, would include the aggregate notional value of swap dealing transactions entered into by its non-U.S. affiliates under common control but would not include the aggregate notional value of swap dealing transactions entered into by its U.S. affiliates.

Numerous commenters objected to the aggregation interpretation regarding swap dealer registration in the Proposed Guidance.[269] IIB and Cleary, while acknowledging the Commission's evasion concerns, contended that the aggregation interpretation in the Proposed Guidance would effectively eliminate the de minimis exemption for any affiliate of a registered swap dealer.[270] IIB further stated that the proposed aggregation interpretation would require a significant amount of coordination among entities within a corporate group in order to gather the relevant information and to reconfigure their registration plans. These difficulties, according to IIB, would be compounded by uncertainties in the proposed interpretation of the term "U.S. person."[271]

---

[268] For purposes of this Guidance regarding the application of Commission regulation 1.3(ggg)(4), the Commission construes the phrase "affiliates under common control" with respect to affiliates as stated in the Final Entities Rules, which defines control as "the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract or otherwise." See Final Entities Rules, 77 FR at 30631 n. 437. Thus, for purposes of this Guidance, a reference to "affiliates under common control" with a person includes affiliates that are controlling, controlled by, or under common control with such person.

[269] See, e.g., Cleary (Aug. 16, 2012) at 9-10; IIB (Aug. 27, 2012) at 22-24; FOA (Aug. 13, 2012) at 11-12; ISDA (Aug. 10, 2012) at 11-12; SocGen (Aug. 8, 2012) at 8; Deutsche Bank (Aug. 27, 2012) at 4-5, FSR (Aug. 27, 2012) at 4-6.

[270] Cleary (Aug. 16, 2012) at 9-10; IIB (Aug. 27, 2012) at 22.

[271] IIB (Aug. 9, 2012) at 6.

Cleary argued that the positions of a registered swap dealer should be excluded from the de minimis calculation by its affiliate and further added that such aggregation relief should be available to any U.S. or non-U.S. affiliates of any U.S.- or non-U.S. registered swap dealer.[272] FOA recommended that the Commission consider a policy that would permit non-U.S. persons to not aggregate the swap dealing activities of their non-U.S. swap dealing affiliates under common control and to require aggregation only where there is evidence that a group of non-U.S. swap dealing affiliates sufficiently coordinate their swap dealing activities.[273] ISDA asserted that the proposed asymmetric application of aggregation (i.e., U.S. affiliates aggregate the entire worldwide group, but non-U.S. affiliates aggregate only non-U.S. affiliates) would produce arbitrary results, citing, as an example, a group that has a U.S. affiliate with $500 million of swaps and a non-U.S. affiliate with $7.6 billion of swaps with non-U.S. persons. In that scenario, the U.S. affiliate must register; the non-U.S. affiliate is not required to register.[274]

In the Further Proposed Guidance, the Commission proposed an alternative interpretation of the aggregation requirement in Commission regulation 1.3(ggg)(4). Under this alternative, a non-U.S. person would be expected, in the consideration of whether its swap dealing transactions exceed the de minimis threshold, to include the aggregate notional value of swap dealing transactions entered into by all its affiliates under common control (i.e., both non-U.S. affiliates

---

[272] Cleary (Aug. 16, 2012) at 9-10.

[273] FOA (Aug. 13, 2012) at 11-12. FOA argued that the Proposed Guidance would have a disproportionate effect by providing that a non-U.S. person engaging in a de minimis amount of U.S.-facing swap dealing activities should register as a swap dealer simply because its other non-U.S. affiliates under common control, in the aggregate, exceed the de minimis threshold, even though there is no coordinated effort. Id.

[274] ISDA (Aug. 10, 2012) at 12 (noting that if an exclusion from aggregation for an affiliated swap dealer's swaps were in place, then the group in the above example could decide which entity registers and thereby bring the swaps attributable to the other entity under the threshold).

and U.S. affiliates), but not include the aggregate notional value of swap dealing transactions of any non-U.S. affiliate under common control that is registered as a swap dealer.[275] The Commission noted that the application of the aggregation requirement in Commission regulation 1.3(ggg)(4) to non-U.S. affiliates of non-U.S. swap dealers may, in certain circumstances, impose significant burdens on such non-U.S. affiliates without advancing significant regulatory interests of the Commission. Because the conduct of swap dealing business through locally-organized affiliates may in some cases be required in order to comply with legal requirements or business practices in foreign jurisdictions, such non-U.S. affiliates may be numerous and it could be impractical to require all such non-U.S. affiliates to register as swap dealers. Further, the Commission's interest in registration may be reduced for a non-U.S. affiliate of a registered non-U.S. swap dealer where the non-U.S. affiliate (or group of such affiliates) engages in only a small amount of swap dealing activity with U.S. persons.

On the other hand, the Commission also noted in the Further Proposed Guidance that, given the borderless nature of swap dealing activities, a swap dealer may conduct swap dealing activities through various affiliates in different jurisdictions, which suggests that its interpretation should take into account the applicable swap dealing transactions entered by all of a non-U.S. person's affiliates under common control worldwide. Otherwise, affiliated persons may not register solely because their swap dealing activities are divided, such that each affiliate falls below the de minimis level. The Commission noted its concern that a policy under which such affiliates whose swap dealing activities individually fall below the de minimis level, but whose

[275] Also, under this alternative approach, a non-U.S. person would not be expected to include the aggregate notional value of swap dealing transactions of any of its non-U.S. affiliates under common control where the counterparty to such affiliate is also a non-U.S. person.

swap dealing activities in the aggregate exceed the de minimis level, would not register as swap dealers could provide an incentive for firms to spread their swap dealing activities among several unregistered affiliates rather than centralize their swap dealing in registered firms. Such a result would increase systemic risks to U.S. market participants and impede the Commission's ability to protect U.S. markets.

Two commenters supported the alternative interpretation of the aggregation requirement set out in the Further Proposed Guidance. Greenberger/AFR stated that the aggregation requirement helps to prevent the spreading of risk, because without aggregation U.S. persons could avoid registration as swap dealers by routing their swap activity through non-U.S. affiliates and thereby remain under the de minimis threshold.[276] Better Markets supported the alternative interpretation in the Further Proposed Guidance because it contemplates that non-U.S. persons would aggregate all swap dealing of all affiliates, including U.S. affiliates, except where the affiliate is registered as a swap dealer.[277]

Other commenters were opposed to the alternative interpretation in the Further Proposed Guidance. SIFMA/CH/FSR stated that aggregation of swap dealing activity across affiliates is not appropriate in any circumstance.[278] ISDA stated that application of the aggregation principle to non-U.S. affiliates may impose significant burdens on the non-U.S. affiliates without

---

[276] Greenberger/AFR (Feb. 6, 2013) at 8-9.

[277] Better Markets (Feb. 15, 2013) at 8-9.

[278] SIFMA/CH/FSR (Feb. 6, 2013) at A2-3

advancing significant regulatory interests, and expanding the scope of aggregation to include swaps of U.S. affiliates would exacerbate this disproportionality.[279]

Mitsubishi UFJ Financial Group Inc. ("Mitsubishi UFJ") asked the Commission to clarify its interpretation of the term "control" in the context of a non-U.S. joint venture where only one owner controls and operates, and financially consolidates, the joint venture entity.[280] Mitsubishi UFJ stated that in this case the joint venture should be linked for aggregation purposes to the owner that has operational control, provided that the owner has at least one affiliate that is a registered swap dealer.[281]

In the Further Proposed Guidance, the Commission asked commenters to address several questions regarding the aggregation provision. In particular, the Commission asked whether the alternative interpretation of the aggregation requirement should apply to non-U.S. persons that are guaranteed by a U.S. person with respect to their swaps obligations in the same way that it applies to non-U.S. persons that are not so guaranteed, and if so, should the Commission continue to construe the term "guarantee" for this purpose to mean any collateral promise by a guarantor to answer for the debt or obligation of an obligor under a swap and should the term include arrangements such as keepwells and liquidity puts.

---

[279] ISDA (Feb. 6, 2013) at 3-4 (relevant affiliates are unlikely to have systems to monitor U.S. person status of swap counterparties). See also European Federation of Energy Traders ("EFET") (Feb. 6, 2013) at 3-4 (arguing that cost of system to monitor aggregation would be substantial and relative benefits of requiring aggregation are small, given that equivalent regulation already applies, or soon will apply, in non-U.S. jurisdictions). ISDA, IIB and CEWG all stated that the treatment in the January Order of grandfathered affiliates (i.e., those affiliates engaged in swap dealing with U.S. persons on December 21, 2012) should be made permanent in order to avoid disrupting established transactional relationships. See ISDA (Feb. 6, 2013) at 3; IIB (Feb. 6, 2013) at 6; CEWG (Feb. 25, 2013) at 2-4.

[280] Mitsubishi UFJ (Feb. 1, 2013) at 3-4.

[281] Id. at 5.

Greenberger/AFR replied to this question affirmatively, stating that the Commission should establish a rebuttable presumption that foreign affiliates are guaranteed by the parent company, and require clear evidence that the market has been explicitly informed that the parent will not stand behind affiliate liabilities in the event of a default or bankruptcy.[282] To do otherwise, they stated, would encourage swap activity through non-U.S. affiliates rather than U.S. persons.[283]

Other commenters stated that the alternative interpretation should not apply to non-U.S. persons that are guaranteed by a U.S. person in the same way that it applies to non-U.S. persons that are not so guaranteed. SIFMA/CH/FSR stated that a guarantee by a U.S. person is not, in itself, a sufficient nexus for jurisdiction under section 2(i) of the CEA, since swaps may be guaranteed for a number of reasons that do not necessarily implicate U.S. jurisdiction.[284] Thus, there may be no importation of risk to the United States through the guarantee and, in any event, concern about importation of risk is appropriately addressed where the guarantor is a prudentially regulated entity, and the Commission should rely on its anti-evasion authority to prevent use of guarantees to evade registration requirements.[285] ISDA also stated that a guarantee constitutes an insufficient jurisdictional nexus, and that it would be consistent with international comity and regulatory reciprocity to regulate swaps between two non-U.S. persons primarily under non-U.S. regulation.[286] Regarding the potential for risk transfer across borders,

---

[282] Greenberger/AFR (Feb. 6, 2013) at 5-6.

[283] Id. at 6.

[284] SIFMA/CH/FSR (Feb. 6, 2013) at A4.

[285] Id.

[286] ISDA (Feb. 6, 2013) at 2-3.

ISDA stated that much of the regulation applicable to swap dealers is not relevant to this concern – external and internal business conduct rules, for example, cannot assure the ultimate solvency of a swap dealer, and it is unclear that encouraging further capitalization of overseas affiliates of a U.S. guarantor, causing financial resources to be contributed overseas, would advance the stability of the U.S. financial system.[287] The Financial Services Agency, Government of Japan ("Japan FSA") also thought that a guarantee from a U.S. person should not, in itself, cause swaps with a non-U.S. person to be included in the de minimis calculation.[288]

The Commission also asked if non-U.S. persons should not be expected to include in the de minimis calculation the swap dealing transactions of their U.S. affiliates under common control, or, alternatively, should the policy of the Commission contemplate that they would exclude from the de minimis calculation the swap dealing transactions of their U.S. affiliates under common control that are registered as swap dealers.

Responding to this question, Greenberger/AFR stated it is important in any case to require aggregation across all non-U.S. affiliates of a global bank, in order to effectively capture transactions spread across multiple foreign affiliates; otherwise, it would be much easier to avoid registration as a swap dealer.[289] They believe that the second alternative – excluding only the swap dealing transactions of U.S. affiliates that are registered as swap dealers – is much preferable to the first, because the first alternative would permit two groups of affiliates, one within the U.S. and another non-U.S., to both engage in swap dealing up to the de minimis level, which would create an incentive to split a swap dealing business between U.S. and non-U.S.

---

[287] Id. at 3.

[288] Japan FSA (Feb. 6, 2013) at 2.

[289] Greenberger/AFR (Feb. 6, 2013) at 9.

affiliates.[290] The second alternative would effectively allow a group of affiliates that individually and collectively fall below the de minimis threshold to forego registration, which they believed could be a sensible compromise, so long as aggregation across foreign affiliates is maintained.[291]

Several commenters were opposed to a policy under which non-U.S. persons would aggregate the swap dealing activities of U.S. affiliates that are registered swap dealers. CEWG argued that this policy could lead to registration of non-U.S. persons as swap dealers because of the activities of their U.S. affiliates, which it asserted would be contrary to the separation sometimes maintained between U.S. and non-U.S. affiliates and unsupported by any policy rationale.[292] ISDA and SIFMA/CH/FSR were of the view that all persons (both U.S. and non-U.S.) should be able to exclude from their de minimis calculations the swaps of any affiliate (whether U.S. or non-U.S.) that is registered with the Commission as a swap dealer, because swaps by a registered swap dealer are subject to Dodd-Frank protections and no purpose would be served by attributing them to affiliated entities in order to impose swap dealer registration on those affiliates.[293]

The Mizuho Corporate Bank, Ltd. ("Mizuho") and Sumitomo submitted a joint letter arguing that the swap dealing activity of U.S. affiliates that are registered as swap dealers should be excluded from aggregation because otherwise the de minimis exception would be effectively unavailable to non-U.S. based firms that conduct U.S.-facing swap dealing activity through a

---

[290] Id.

[291] Id.

[292] CEWG (Feb. 25, 2013) at 2-4.

[293] ISDA (Feb. 6, 2013) at 4; SIFMA/CH/FSR (Feb. 6, 2013) at B11-12. CEWG and ISDA also both stated that U.S. persons should in no event be required to aggregate swaps of non-U.S. affiliates with non-U.S. persons, because such swaps have insufficient nexus to the United States. CEWG (Feb. 25, 2013) at 2; ISDA (Feb. 6, 2013) at 4.

U.S. affiliate that is registered as a swap dealer.[294] This result, in turn, would inappropriately disfavor these firms as compared to firms that conduct the same business through non-U.S. affiliates registered as swap dealers; the Commission's interpretation should encourage, rather than disfavor, registration of U.S. affiliates as swap dealers.[295] IIB stated that the policy reasons for allowing the exclusion of swap dealing by non-U.S. affiliates registered as swap dealers also applies to the dealing activity of U.S affiliates that are registered.[296]

Other commenters went further, stating that non-U.S. persons should not be required to aggregate the swap dealing activities of any of their U.S. affiliates. The Japanese Bankers Association stated U.S. affiliates should be excluded from the non-U.S. person's calculations because the U.S. persons are already subject to Dodd-Frank regulation as warranted by their activities.[297] EDF Trading stated that non-U.S. persons that maintain minimal contacts with the United States should not be required to register as swap dealers due to the activities of their U.S. affiliates, because such a requirement would be inconsistent with the jurisdictional limitation in section 2(i) of the CEA; result in duplicative and potentially inconsistent regulatory requirements of multiple jurisdictions applying to the same swap activity; and encourage commercial firms to

---

[294] Mizuho/Sumitomo (Feb. 6, 2013) at 3.

[295] Id. See also Japan FSA (Feb. 6, 2013) at 2 (arguing that the swap dealing activity of U.S. affiliates that are registered as swap dealers should be excluded because the affiliates are subject to supervision by the Commission).

[296] IIB (Feb. 6, 2013) at 5-6.

[297] Japanese Bankers Association (Feb. 6, 2013) at 2-3. See also Japan FSA (Feb. 6, 2013) at 2 (arguing that all affiliates of Japanese financial institutions should be excluded from the de minimis calculation because the affiliates are supervised by Japan FSA on a consolidated basis).

cease potential swap dealing activity in the U.S., resulting in reduced U.S. swaps market liquidity and fragmentation of the global swaps markets.[298]

Last, the Commission solicited commenters' views on whether a person engaged in swap dealing activities could take advantage of an interpretation of the aggregation provision that allows a person to exclude the swap dealing activities of one or more of its affiliates under common control. The Commission asked whether, under such an interpretation, a person could spread its swap dealing activities into multiple affiliates, each under the de minimis threshold, and therefore avoid the registration requirement, even though the aggregate level of swap dealing by the affiliates exceeds the de minimis threshold. In this regard, the Commission asked if any such interpretation should include any conditions or limits on the overall amount of swap dealing engaged in by unregistered persons within an affiliated group.

Greenberger/AFR opined that any approach that did not require significant aggregation of swap dealing activities across affiliates would create the danger of risk spreading outlined in the Further Proposed Guidance.[299] They stated that financial institutions could easily remain under the de minimis threshold and thereby avoid registration by routing swaps through their non-U.S. affiliates.[300]

---

[298] EDF Trading (Feb. 6, 2013) at 1-4. See also Brigard & Urrutia Abogados (Feb. 6, 2013) at 2 (non-U.S. persons should be allowed to exclude from the de minimis calculation the swap dealing activities of U.S. affiliates, and of any affiliate (U.S. or non-U.S.) that is a registered swap dealer).

[299] Greenberger/AFR (Feb. 6, 2013) at 8-9.

[300] See id. (citing press reports that U.S. banks such as Morgan Stanley and Goldman Sachs are using foreign entities "in seriatim fashion to avoid going over the $ 8 billion test"). Making a similar point, Better Markets emphasized that market participants may be expected to implement the lowest-cost structure, considering all regulatory costs. Better Markets (Feb. 6, 2013) at 15.

The Japanese Bankers Association stated that while the approach in the Further Proposed Guidance could potentially prevent evasion, it would do so at the cost of requiring multiple non-U.S. affiliates to register as swap dealers even if the group of affiliates concentrated its U.S. swap dealing activity in one U.S. entity.[301] In fact, they argued, concentrating U.S. swap dealing activity in a U.S. entity should be encouraged because it facilitates Commission supervision of that activity.[302] Further, they stated that to expect non-U.S. persons to register as swap dealers as a result of dealing activity by their U.S. affiliates undermines the regulatory independence of different jurisdictions and international understandings on regulatory harmonization.[303] Similarly, EDF Trading stated that expecting multiple entities within a corporate group to register as swap dealers would be burdensome and may not advance regulatory interests, and the alternative in the Further Proposed Guidance would merely increase economic and regulatory burdens without achieving a significant reduction in systemic risk, because it would encourage the concentration of swap dealing activity in non-U.S affiliates.[304]

SIFMA/CH/FSR were of the view that it would be burdensome for market participants to use multiple affiliates to avoid swap dealer registration, because moving swap dealing activity between affiliates requires a significant legal, technological and operational investment, and fragmenting the activity among affiliates may make it harder for a multinational institutions to manage risk efficiently.[305] Along the same lines, IIB stated that where one entity in a corporate

---

[301] Japanese Bankers Association (Feb. 6, 2013) at 3.

[302] Id.

[303] Id. at 3-4.

[304] EDF Trading (Feb. 6, 2013) at 5.

[305] SIFMA/CH/FSR (Feb. 6, 2013) at A3.

group is registered as a swap dealer, there are substantial commercial and credit risk incentives to centralize swap dealing in the registered entity, because doing so maximizes the potential to net offsetting transactions, uses capital more efficiently, and is operationally efficient.[306] On the other hand, IIB stated that using unregistered entities for swap dealing would not reduce the fixed costs incurred in registration and that the unregistered entities in the group would still be subject to swap costs such as clearing, reporting and trade execution.[307]

Based on the comments received on the Proposed Guidance and the Further Proposed Guidance, and its further review of issues related to the aggregation requirement, the Commission's policy is to interpret the aggregation requirement in Commission regulation 1.3(ggg)(4) in a manner that applies the same aggregation principles to all affiliates in a corporate group, whether they are U.S. or non-U.S. persons. Further, the Commission will generally apply the aggregation principle (as articulated in the Final Entities Rules) such that, in considering whether a person is engaged in more than a de minimis level of swap dealing, a person (whether U.S. or non-U.S.) should generally include all relevant dealing swaps of all its U.S. and non-U.S. affiliates under common control,[308] except that swaps of an affiliate (either U.S. or non-U.S.) that is a registered swap dealer are excluded, as discussed below. The Commission notes that this policy would ensure that the aggregate notional value of applicable

---

[306] IIB (Feb. 6, 2013) at 3.

[307] Id.

[308] For purposes of this Guidance, the Commission clarifies that a reference to "affiliates under common control" with a person includes affiliates that are controlling, controlled by, or under common control with such person. See note 268, supra. Further, in response to a question from a commenter, the Commission clarifies that for this purpose, the term "affiliates under common control" includes parent companies and subsidiaries, and is not limited to "sister companies" at the same organizational level. See David Mu (Jan. 8, 2013).

swap dealing transactions of all such unregistered U.S. and non-U.S. affiliates does not exceed the de minimis level.

Stated in general terms, the Commission's interpretation allows both U.S. persons and non-U.S. persons in an affiliated group to engage in swap dealing activity up to the de minimis threshold. When the affiliated group meets the de minimis threshold in the aggregate, one or more affiliate(s) (inside or outside the United States) would generally have to register as swap dealer(s) so that the relevant swap dealing activity of the unregistered affiliates remains below the threshold.

The Commission recognizes the borderless nature of swap dealing activities, in which a dealer may conduct swap dealing business through its various affiliates in different jurisdictions, and the Commission believes that its policy on aggregation outlined above addresses the concern that an affiliated group of U.S. and non-U.S. persons with significant swap dealing transactions with U.S. persons or guaranteed affiliates may not be required to register solely because such swap dealing activities are divided between affiliates that each fall below the de minimis level.

#### c. Exclusion of Certain Swaps by Non-U.S. Persons from the Swap Dealer De Minimis Threshold

The Proposed Guidance would generally allow a non-U.S. person to exclude from its de minimis threshold calculation its swaps with foreign branches of U.S. swap dealers. This exclusion was intended to allow non-U.S. persons to continue their inter-dealer swap activities with foreign branches of U.S. swap dealers without exceeding the de minimis threshold, thereby triggering a requirement to register as a swap dealer.

Commenters on the Proposed Guidance, such as Goldman Sachs, argued that the rationale for this exclusion is equally applicable when non-U.S. persons that are banks or broker-

dealers engage in swap dealing transactions with U.S. swap dealers that do not conduct overseas business through foreign branches. Absent a similar interpretation in these circumstances, the commenters argued, U.S. swap dealers would be at a competitive disadvantage vis-à-vis foreign branches of U.S. swap dealers since non-U.S. persons would be incentivized to limit their dealing activities to foreign branches of U.S. swap dealers.[309]

The Commission's policy is to generally allow non-U.S. persons that are not guaranteed or conduit affiliates of U.S. persons not to count toward their de minimis thresholds their swap dealing transactions with (i) a foreign branch of a U.S. swap dealer, (ii) a guaranteed affiliate of a U.S. person that is a swap dealer, and (iii) a guaranteed or conduit affiliate that is not a swap dealer and itself engages in de minimis swap dealing activity and which is affiliated with a swap dealer.[310] The Commission believes that where the guaranteed affiliate of a U.S. person is registered as a swap dealer, or where the foreign branch is included within the swap dealer registration of its U.S. home office, then it is appropriate to generally permit such non-U.S. not to count its swap dealing transactions with those entities against the non-U.S. person's de minimis threshold, because in these cases one counterparty to the swap is a swap dealer subject to comprehensive swap regulation and operating under the oversight of the Commission.

The Commission understands that commenters are concerned that foreign entities, in order to avoid swap dealer status, may decrease their swap dealing business with foreign branches of U.S. registered swap dealers and guaranteed affiliates that are swap dealers.

---

[309] Goldman (Aug. 27, 2012) at 5-6.

[310] Note that if a non-U.S. person that is not a guaranteed or conduit affiliate of a U.S. person engages in a swap dealing transaction with another non-U.S. person that is not a guaranteed affiliate of a U.S. person (including such non-U.S. person that is a swap dealer), then such swap dealing transaction does not count toward the de minimis threshold of the unregistered, swap dealing party.

Therefore, the Commission's policy, based on its interpretation of section 2(i) of the CEA, will be that swap dealing transactions with a foreign branch of a U.S. swap dealer or with guaranteed affiliates that are swap dealers should generally be excluded from the de minimis calculations of non-U.S. persons that are not guaranteed or conduit affiliates.[311] However, the Commission is not persuaded that similar concerns arise regarding foreign entities that may engage in swap dealing business with such persons.[312]

With regard to non-U.S. persons that are not guaranteed or conduit affiliates of U.S. persons, such non-U.S. persons also generally would not count toward their de minimis thresholds their swap dealing transactions with a guaranteed affiliate that is not a swap dealer and itself engages in de minimis swap dealing activity and which is affiliated with a swap dealer. This interpretation reflects the Commission's view that when the aggregate level of swap dealing by a non-U.S. person that is not a guaranteed affiliate, considering both swaps with U.S. persons and swaps with unregistered guaranteed affiliates (together with any swap dealing transactions that the non-U.S. person aggregates for purposes of the de minimis calculation as described below) exceeds the de minimis level of swap dealing, the non-U.S. person's swap dealing transactions have the requisite "direct and significant connection with activities in, or effect on, commerce of the United States."[313] The Commission believes, however, that where the

---

[311] The types of offices the Commission would generally consider in this regard to be a "foreign branch" of a U.S. bank, and the circumstances in which a swap would generally be treated as being with such foreign branch, are discussed further in section C, infra.

[312] See Goldman (Aug. 27, 2012) at 3-4.

[313] In the Proposed Guidance, the Commission asked whether the place of execution or clearing is relevant to the determination of whether a non-U.S. person should be required to register as a swap dealer. The Commission's policy is that a person generally would not be required to register as a swap dealer if the person's only connection to the United States is that the person uses a U.S.-registered swap execution facility ("SEF")or designated contract market ("DCM") in connection with its swap dealing activities.

counterparty to a swap is a guaranteed affiliate and is not a registered swap dealer, the Commission's regulatory concerns are addressed because the guaranteed affiliate engages in a level of swap dealing below the de minimis threshold and is part of an affiliated group with a swap dealer.

In addition, non-U.S. persons that are not guaranteed or conduit affiliates of U.S. persons also generally would not count toward their de minimis thresholds their swap dealing transactions with a guaranteed affiliate where the guaranteed affiliate is guaranteed by a non-financial entity.[314] This exception is appropriate given that the risks to the U.S. financial markets are mitigated because the U.S. guarantor is a non-financial entity.

The Commission notes that under its interpretation of section 2(i), a non-U.S. person that is not a guaranteed or conduit affiliate would not have to count its swap dealing transactions with other non-U.S. persons that are not guaranteed affiliates because, in the Commission's view, such swap dealing activity would not have the requisite "direct and significant connection with activities in, or effect on, U.S. commerce."

**d. Exclusion of Certain Swaps by Non-U.S. Persons from the MSP Calculation**

Related to their discussion of the swap dealer de minimis threshold, some commenters, such as SIFMA and Citi, stated that a non-U.S. person should not have to include swaps with foreign branches of U.S. swap dealers towards the MSP calculation.[315]

---

[314] See CEA section 2(h)(7)(C) for a definition of financial entity.

[315] See SIFMA (Aug. 27, 2012) at A28-29; Citi (Aug. 27, 2012) at 2-3.

The Commission has considered whether, under section 2(i), the swaps that a non-U.S. person that is not a guaranteed or conduit affiliate enters into with a foreign branch of a U.S. swap dealer or a guaranteed affiliate that is a swap dealer should be excluded from the calculation of the non-U.S. person's MSP registration threshold. The Commission notes that its policy regarding such swaps for purposes of the MSP registration may reasonably be distinguished from its policy for purposes of the swap dealer registration threshold calculation. As described in the Final Entities Rules, MSP registration is required for non-dealers with swaps positions so large as to pose systemic risk. This is in contrast to swap dealer registration, which is a functional test focused on the nature of activities conducted by a potential registrant. Consequently, if all swaps between a non-U.S. person and foreign branches of U.S. swap dealers or swap dealers that are guaranteed affiliates were generally excluded under the Commission's policy with respect to MSP registration, a market participant that poses systemic risk within the meaning of the MSP definition could potentially be relieved of the requirement to register as an MSP. The Commission believes that such an outcome could undermine the MSP registration scheme. However, the Commission is persuaded that it is possible to control the potential risk of the non-U.S. person's risk with foreign branches of U.S. swap dealers and guaranteed affiliates that are swap dealers under certain limited circumstances and therefore that limited interpretive relief from the MSP calculation requirement is appropriate.[316] Thus, a non-U.S. person that is not a guaranteed affiliate of a U.S. person and is a financial entity generally does not have to count toward its MSP threshold its exposure under swaps with foreign branches of a U.S. swap

[316] The interpretation applies to non-U.S. persons that are not guaranteed by U.S. persons. Non-U.S. financial entities would be required to include swaps positions with foreign branches and guaranteed affiliates of U.S. persons unless they choose to comply with voluntary margining requirements, discussed below.

dealer or guaranteed affiliates that are swap dealers; provided, that the swap is either cleared, or the documentation of the swap requires the foreign branch or guaranteed affiliate to collect daily variation margin, with no threshold, on its swaps with such non-U.S. person. When this condition is met, the Commission believes that it would generally be appropriate for the non-U.S. person not to count its exposure under such swaps against its MSP threshold.

The Commission notes that a non-U.S. person's swaps positions with guaranteed affiliates that are swap dealers and foreign branches of U.S. swap dealers must be addressed in the latter entities' risk management programs. Such programs must account for, among other things, overall credit exposures to non-U.S. persons.[317] Second, the Commission notes that a non-U.S. person's swaps with a guaranteed affiliate that is a swap dealer would be included in exposure calculations and attributed to the U.S. guarantor for purposes of determining whether the U.S. guarantor's swap exposures are systemically-important on a portfolio basis and therefore require the protections provided by MSP registration.[318]

Finally, a non-U.S. person that is not a guaranteed affiliate and is not a financial entity[319] would generally not have to count toward its MSP thresholds its exposure under swaps with a foreign branch of a U.S. swap dealer or guaranteed affiliate that is a swap dealer. This exclusion

---

[317] See Commission regulation 23.600(c)(4)(ii), requiring SDs and MSPs to have credit risk policies and procedures that account for daily measurement of overall credit exposure to comply with counterparty credit limits, and monitoring and reporting of violations of counterparty credit limits performed by personnel that are independent of the business trading unit. See also Commission regulation 23.600(c)(1)(i), requiring the senior management and the governing body of each swap dealer and MSP to review and approve credit risk tolerance limits for the swap dealer or MSP.

[318] See Final Entities Rules at 30689, stating the Commission's interpretation that "an entity's swap . . . positions in general would be attributed to a parent, other affiliate or guarantor for purposes of the major participant analysis to the extent that the counterparties to those position would have recourse to that other entity in connection with the position." The Commission stated further that "entities will be regulated as major participants when they pose a high level of risk in connection with the swap . . . positions they guarantee."

[319] See CEA section 2(h)(7)(C) for a definition of financial entity.

reflects the Commission's recognition of the more modest risk to the U.S. financial markets from swaps activities with non-financial entities organized outside the United States.[320] Further, the Commission notes that the Basel Committee on Banking Supervision ("BCBS") and the International Organization of Securities Commissions ("IOSCO") have recently issued a second consultative document under which, if finalized, would not apply margin requirements to the non-centrally cleared derivatives of non-financial entities, given that such transactions are viewed as posing little or no systemic risk and are exempt from clearing mandates in most jurisdictions.[321]

#### e. Exclusion of Certain Swaps Executed Anonymously on a SEF, DCM, or Foreign Board of Trade ("FBOT") and Cleared

The Commission believes that when a non-U.S. person that is not guaranteed by a U.S. person enters into swaps anonymously on a registered DCM, SEF, or FBOT[322] and such swaps are cleared, the non-U.S. person would generally not have to count such swaps against its de

---

[320] Based on data the Bank for International Settlements obtained from thirteen reporting countries (Australia, Belgium, Canada, France, Germany, Italy, Japan, the Netherlands, Spain, Sweden, Switzerland, the United Kingdom and the United States), at the end of December 2012, notional amounts outstanding for OTC foreign exchange derivatives, interest rate derivatives, and credit default swaps with non-financial customers accounted for an average of less than 8 percent of the total aggregate amounts outstanding for these asset classes. See Bank for International Settlements, Statistical release: OTC derivatives statistics at end-December 2012 (May 2013), available at http://www.bis.org/publ/otc_hy1305.pdf.

[321] See BCBS IOSCO, Margin Requirements for Non-Centrally Cleared Derivatives, Second Consultative Document, at 7 (issued for comment March 15, 2013), available at http://www.bis.org/publ/bcbs242.pdf.

[322] As used herein, a registered FBOT means an FBOT that is registered with the Commission pursuant to part 48 of the regulations in order to permit direct access to the FBOT's order entry and trade matching system from within the U.S. Among others, 16 FBOTs that currently permit direct access for the trading of futures and option contracts, but not swaps, pursuant to no-action relief letters issued by Commission staff have submitted complete applications for registration. In light of the fact that registered FBOTs can also list swaps for trading by direct access and in view of the time required to properly assess registration applications and the interest on the part of certain FBOTs operating pursuant to the no-action relief in listing swaps for trading by direct access, the Division of Market Oversight has determined to amend the 16 no-action letters to permit those FBOTs, subject to certain conditions, to also list swaps for trading by direct access. Accordingly, all provisions in this document that apply to registered FBOTs also apply to the 16 FBOTs permitting trading by direct access pursuant to the amended no-action relief.

minimis threshold. The Commission understands that in these circumstances, the non-U.S. person would not have any prior information regarding its counterparty to the swap. Also, as discussed below, the Commission is interpreting CEA section 2(i) such that, where a swap between a non-U.S. swap dealer and a U.S. person is executed anonymously on a registered DCM, SEF, or FBOT and cleared the non-U.S. swap dealer will satisfy all of the applicable Category A Transaction-Level Requirements[323] that pertain to such a swap transaction. The Commission believes that the regulatory interest in including such swaps in the non-U.S. person's de minimis calculation is outweighed by the practical difficulties involved in determining whether the non-U.S. person should include the swap in the calculation, given that the non-U.S. person would have no information regarding its swap counterparty prior to execution of the swap.

The Commission also believes that when a non-U.S. person that is not a guaranteed or conduit affiliate clears a swap through a registered derivatives clearing organization ("DCO"), such non-U.S. person would generally not have to count the resulting swap (i.e., the novated swap) against its swap dealer de minimis threshold or MSP threshold.[324] Where a swap is created by virtue of novation, such swap does not implicate swap dealing, and therefore it would not be appropriate to include such swaps in determining whether a non-U.S. person should register as a swap dealer.

---

[323] The Commission notes that while the real-time reporting requirement will be satisfied for cleared swaps executed anonymously on a DCM or SEF, absent further affirmative actions by an FBOT, the requirement will not be satisfied through FBOT execution alone. See section G, infra

[324] A swap that is submitted for clearing is extinguished upon novation and replaced by new swap(s) that result from novation. See Commission regulation 39.12(b)(6). See also Derivatives Clearing Organization General Provisions and Core Principles, 76 FR 69334, 69361 (Nov. 8, 2011).

### f. MSP-Parent Guarantees

While under the Proposed Guidance swaps conducted by a non-U.S. person, where guaranteed by a U.S. person, would generally be attributed only to the U.S. person in determining who must register as an MSP, the Commission did not expressly address a guarantee by a non-U.S. person of the swaps obligations of its U.S. subsidiary. In SIFMA's view, the Proposed Guidance created ambiguity as to the treatment of guarantees between other types of entities (e.g., where a U.S. person is guaranteed by a non-U.S. person or where a non-U.S. person is guaranteed by a non-U.S. person).[325] In addition, Cleary noted that the Commission determined in the Final Entities Rules not to include a parental guarantee of a subsidiary's swaps in the computation of the parent's outward exposure under the MSP definition where the subsidiary is subject to capital oversight by the Commission, SEC, or an appropriate banking regulator. They asked that the Commission consider extending comparable treatment for parental guarantees where the non-U.S. subsidiary is subject to Basel-compliant capital oversight by another G20 prudential supervisor.[326]

Under the Commission's interpretation of section 2(i) of the CEA, the discussion in the Final Entities Rules regarding attribution of swaps positions of guaranteed persons for purposes of the MSP definition should generally apply to non-U.S. persons. That is, as applied to non-U.S. persons, where there is no guarantee or recourse to another person under the swap, the swap should generally be attributed to the person who enters into the swap, and there generally would

---

[325] SIFMA (Aug. 27, 2012) at A32. Along similar lines, IIB commented that there might be circumstances under which a wholly-owned subsidiary of a person already registered as a swap dealer enters into swaps with U.S. persons where its obligations are guaranteed by the swap dealer. IIB (Aug. 27, 2012) at 25.

[326] Cleary (Aug. 16, 2012) at 12.

be no attribution or aggregation of the swaps position with the swaps positions of the person's affiliates.[327] On the other hand, where the counterparty to the swap would have recourse to another person, such as a parent guarantor, the swap should generally be attributed to the person to whom there is recourse. Thus, if a U.S. person enters into a swap guaranteed by a non-U.S. person, the swap should generally be attributed to the non-U.S. person, and if a non-U.S. person enters into a swap guaranteed by a U.S. person, the swap should generally be attributed to the U.S. person.

However, the Commission is also cognizant that, as a matter of international comity, regulation of non-U.S. persons can be less preferable where the same regulatory outcomes can be achieved by regulating an affiliated U.S. person. So where the swaps of a U.S. person are guaranteed by a non-U.S. person, the Commission would consider the possibility that registration of the non-U.S. person would not be required if the U.S. person registers as an MSP, and there may be circumstances where registration of the U.S. person would be preferable. Also, the same considerations of international comity suggest that regulation of non-U.S. persons should be effected in a manner that generally does not interfere with non-U.S. regulation. Thus, the Commission would be willing to consider that the swaps positions of non-U.S. persons that are guaranteed by other non-U.S. persons may be attributed to either the non-U.S. guarantor or the guaranteed non-U.S. person so long as all of the swaps positions that would trigger MSP registration are subject to the MSP registration and regulatory requirements. Thus, in IIB's scenario, the non-U.S.-based bank may consult with the Commission and decide to register itself – or its subsidiaries – as an MSP. The Commission would generally not expect both the parent

---

[327] See Final Entities Rules, 77 FR at 30689.

guarantor bank and the guaranteed bank to register as MSPs. In the Commission's view, the related risk concerns should be adequately addressed by requiring either the guarantor or the guaranteed person to register, provided that the swap activities giving rise to MSP registration are regulated under Dodd-Frank.

As to Cleary's request regarding comparable treatment for certain parental guarantees, the Commission agrees that, as a matter of policy, it would generally be appropriate to extend similar treatment to parental guarantees of a subsidiary that is subject to comparable and comprehensive capital oversight by a G20 prudential supervisor. In this respect, the Commission views Basel-compliant capital standards as sufficiently comparable and comprehensive to capital oversight by the Commission, SEC, or banking regulator. Thus, where a subsidiary is subject to Basel-compliant capital standards and oversight by a G20 prudential supervisor, the subsidiary's positions would generally not be attributed to a parental guarantor in the computation of the parent's outward exposure under the MSP definition

4. **Summary**

The Commission's policy under this Guidance may be summarized as follows.

The Commission will generally apply the aggregation principle (as articulated in the Final Entities Rules) such that, in considering whether a person is engaged in more than a de minimis level of swap dealing, a person (whether U.S. or non-U.S.) should generally include all relevant dealing swaps of all its U.S. and non-U.S. affiliates under common control, except that swaps of an affiliate (either U.S. or non-U.S.) that is a registered swap dealer are excluded. For this purpose, consistent with the Commission's policy on counting swap transactions towards the de minimis threshold for swap dealer registration detailed above, the dealing swaps of an affiliate under common control with such person would include:

(i) in the case of a U.S. person or a guaranteed or conduit affiliate, all its swap dealing transactions; and

(ii) in the case of a non-U.S. person that is not a guaranteed or conduit affiliate:

a. all dealing swaps with counterparties who are U.S. persons (other than foreign branches of U.S. swap dealers); and

b. all dealing swaps with guaranteed affiliates except:

i. guaranteed affiliates that are swap dealers;

ii. guaranteed affiliates that are not swap dealers but which are affiliated with a swap dealer and where the guaranteed affiliate itself engages in de minimis swap dealing activity;

iii. guaranteed affiliates that are guaranteed by a non-financial entity.

In addition, a non-U.S. affiliate that is not a guaranteed or conduit affiliate may exclude any swaps that are entered into anonymously on a registered DCM, SEF, or FBOT and cleared, as more fully discussed above.

The Commission's interpretation would allow both U.S. persons and non-U.S. persons in an affiliated group to engage in unregistered swap dealing activity up to the de minimis level for the entire group. When the affiliated group nears the de minimis threshold in the aggregate, it would have to register a number of affiliates (inside or outside the United States) as swap dealers sufficient to maintain the relevant dealing swaps of the unregistered affiliates below the threshold.

In determining whether a non-U.S. person holds swap positions above the MSP thresholds, the non-U.S. person should consider the aggregate notional value of:

(i) any swap position between it and a U.S. person;

(ii) any swap position between it and a guaranteed affiliate (but its swap positions where its own obligations thereunder are guaranteed by a U.S. person should be attributed to that U.S. person and not included in the non-U.S. person's determination); and

(iii) any swap position between another (U.S. or non-U.S.) person and a U.S. person or guaranteed affiliate, where it guarantees the obligations of the other person thereunder.

A non-U.S. person that is not a guaranteed affiliate of a U.S. person and is a financial entity would generally not have to count toward its MSP thresholds its exposure under swaps with foreign branches of U.S. swap dealers or guaranteed affiliates that are swap dealers, provided that the swap is either cleared, or the documentation of the swap requires the foreign branch or guaranteed affiliate to, and the swap dealer actually does, collect daily variation margin, on its swaps with the non-U.S. person.

In addition, a non-U.S. person that is not a guaranteed affiliate and is not a financial entity[328] would generally not have to count toward its MSP thresholds its exposure under swaps with a foreign branch or guaranteed affiliate, in each case that is a swap dealer.

[328] See CEA section 2(h)(7)(C) for a definition of financial entity.

### C. Interpretation of the Term "Foreign Branch;" When a Swap Should be Considered to be with the Foreign Branch of a U.S. Person that is a Swap Dealer or MSP

#### 1. Interpretation of the Term "Foreign Branch" and Treatment of Foreign Branches

As discussed above, the Commission considers a foreign branch of a U.S. person to be a part of the U.S. person. Thus, in the Proposed Guidance, the Commission proposed that the U.S. person would be legally responsible for complying with all applicable Entity-Level Requirements. Under this approach, the foreign branch of the U.S. person would not register separately as a swap dealer. The Commission believes that this approach is appropriate because a foreign branch of a U.S. swap dealer is an integral part of a U.S. swap dealer and not a separate legal entity.

In the Proposed Guidance, the Commission also proposed interpreting 2(i) so that where a swap is with a foreign branch of a U.S.-based swap dealer, irrespective of whether the counterparty is a U.S. person or non-U.S. person, the foreign branch would be expected to comply with most of the Transaction-Level Requirements. The Commission stated that this proposed approach is appropriate in light of the Commission's strong supervisory interests in entities that are a part or an extension of a U.S.-based swap dealer. The Commission also proposed interpreting 2(i) so that swaps between a foreign branch of a U.S. person and a non-U.S. person counterparty (irrespective of whether that non-U.S. person counterparty's obligations under the swap are guaranteed by a U.S. person or not) would be eligible for substituted compliance with respect to Category A Transaction-Level Requirements. As discussed further below, where the counterparty to a swap with a foreign branch is a non-U.S.

person (whether or not swaps such non-U.S. person is guaranteed or otherwise supported by, or is an affiliate conduit of, a U.S. person), the Commission continues to be of the view that the swap should be eligible for substituted compliance with respect to Category A Transaction-Level Requirements, to the extent applicable, in light of the supervisory interest of the foreign jurisdiction in the execution and clearing of trades occurring in that jurisdiction. As discussed further in section F below, the Commission's recognition of substituted compliance would be based on an evaluation of whether the requirements of the home jurisdiction are comparable and comprehensive to the applicable requirement(s) under the CEA and Commission regulations based on a consideration of all relevant factors, including among other things: (i) the comprehensiveness of the foreign regulator's supervisory compliance program and (ii) the authority of such foreign regulator to support and enforce its oversight of the registrant's branch or agency with regard to such activities to which substituted compliance applies.

In the January Order, the Commission gave exemptive relief from Transaction-Level Requirements during the pendency of the January Order for swaps between a foreign branch of a U.S. swap dealer or U.S. MSP and a non-U.S. counterparty (including a non-U.S. swap dealer or non-U.S. MSP). Thus, notwithstanding the Commission's view that the foreign branch of a U.S. swap dealer is a U.S. person, the Commission granted temporary relief during the pendency of the January Order for swaps between a foreign branch of a U.S. registrant and a non-U.S. swap dealer, allowing the non-U.S. swap dealer to treat the foreign branch as a non-U.S. person.

In the January Order, the Commission also stated that because it believes a swap between two foreign branches of U.S. registrants is a swap between two U.S. persons, such swaps are fully subject to the Transaction-Level Requirements. Nevertheless, during the pendency of the January Order, the Commission determined it would be appropriate to permit foreign branches of

U.S. registrants to comply only with transaction-level requirements required in the location of the foreign branch while the Commission further considered, and worked with international regulators regarding, the treatment of foreign branches of U.S. registrants. However, for purposes of this relief, the Commission stated that for a swap between foreign branches of U.S. registrants, the swap would be treated as with the foreign branch of a U.S. person when: (i) the personnel negotiating and agreeing to the terms of the swap are located in the jurisdiction of such foreign branch; (ii) the documentation of the swap specifies that the counterparty or "office" for the U.S. person is such foreign branch; and (iii) the swap is entered into by such foreign branch in its normal course of business (collectively the "January Order Criteria"). If the swap failed to satisfy all three of the January Order Criteria, the Commission stated that the swap would be treated as a swap of the U.S. person and not as a swap of the foreign branch of the U.S. person, and would not be eligible for relief from transaction-level requirements under the January Order.[329]

The Commission also stated in the January Order that as part of the Commission's further consideration of this issue, additional factors may be relevant to the consideration of whether a swap is with the foreign branch of a U.S. person. These factors could include, for example, that:

(i) the foreign branch is the location of employment of the employees negotiating the swap for the U.S. person or, if the swap is executed electronically, the employees managing the execution of the swap;

(ii) the U.S. person treats the swap as a swap of the foreign branch for tax purposes,

---

[329] See the January Order, 78 FR at 873 n. 123.

(iii) the foreign branch operates for valid business reasons and is not only a representative office of the U.S. person; and

(iv) the branch is engaged in the business of banking or financing and is subject to substantive regulation in the jurisdiction where it is located (collectively the "Additional Factors").[330]

The Commission also sought comment from market participants and other interested parties regarding whether it is appropriate to include these or other factors in the consideration of when a swap is with the foreign branch of a U.S. person.

2. **Comments**

The Commission received several comments on how the Commission should determine whether a swap is "with a foreign branch," both with regard to swaps between a foreign branch and a non-U.S. swap dealer and swaps between two foreign branches of U.S. swap dealers. In addition, several organizations commented on the term "foreign branch" of a U.S. bank.

Commenters stated that in determining whether a swap between a non-U.S. swap dealer and a non-U.S. branch of a U.S. bank is bona fide with the non-U.S. branch, the Commission should look to whether the swap is booked in the foreign branch (as defined in Regulation K), and that the four additional factors that the Commission stated it was considering are unnecessary.[331] These commenters stated that the first Additional Factor being considered (i.e., that the foreign branch is the location of employment of the employees negotiating the swap for the U.S. person or, if the swap is executed electronically, the employees managing the execution

---

[330] Id. at 873.

[331] See SIFMA/CH/FSR (Feb. 6, 2013) at B18-20; State Street (Feb. 6, 2013) at 2-4.

of the swap) should be deleted because employees that negotiate and agree to the terms of a swap may be located outside of the non-U.S. branch that books the trade for a variety of valid reasons.[332] Similar arguments were made with regard to the first prong of the January Order Criteria (i.e., that the personnel negotiating and agreeing to the terms of the swap are located in the jurisdiction of such foreign branch).[333] As noted above, State Street stated that in a global economy, foreign exchange swaps are negotiated 24 hours a day, by parties in various locations. Therefore, the physical location of employees has little connection to the legal jurisdiction of the branch in which the swaps are booked. Determination of the branch in which the swap is booked is influenced by a number of factors, including the convenience of the swap counterparty and agreements between counterparties to book swaps to mutually agreeable and preferred locations. State Street further stated that limiting the ability to book transactions to a foreign branch would be inappropriate for U.S. dealers in foreign exchange because foreign exchange transactions are typically negotiated in large blocks, which combine the orders of a variety of asset owners, and which can include both U.S. persons and non-U.S. persons. Once negotiated and executed, these blocks are allocated to the various asset owners, and booked to the location preferred by the asset owner or in some cases the dealer's non-U.S. branch. This allows managers to trade foreign exchange more efficiently, using a single point of dealer contact, and ensures that all asset owners on whose behalf they are trading receive the same price. State Street also stated that the approach outlined in proposal would place U.S. businesses at a competitive disadvantage, as

---

[332] See, e.g., SIFMA/CH/FSR (Feb. 6, 2013) at B18.

[333] Id. at B17.

non-U.S. owners would be unwilling to do business that would subject them to the U.S. regulatory requirements.[334]

A commenter stated that it does not strongly object to prongs 2, 3 and 4 of the Additional Factors (that the swap is treated as a swap of the foreign branch for tax purposes, that the branch operates for valid business reasons and is not only a representative office, and that the branch is engaged in banking or financing and subject to substantive local regulation) since they could "be reasonable indicia of a *bona fide* non-U.S. branch of a U.S. swap dealer." However, this commenter stated that each of these prongs may be challenging to properly define and evaluate.[335]

With respect to the proposed tax prong (prong 2 of the Additional Factors), other commenters stated that the income from a swap that is booked in a foreign branch of a U.S. person is subject to taxation in the local jurisdiction in which the foreign branch is resident, which demonstrates that such swaps are bona fide with the non-U.S. branch. The commenters further noted that a foreign tax credit is generally allowed for income taxes paid locally.[336]

With regard to prong 3 of the Additional Factors (that the branch operates for valid business reasons and is not only a representative office), as noted earlier, SIFMA/CH/FSR argued that the only criteria that is relevant in determining whether a swap is bona fide with a foreign branch of a U.S. swap dealer is whether the swap is booked in the foreign branch (as reflected in the trade confirm), with the term "foreign branch" defined with reference to Regulation K. These commenters stated that the definition of a foreign branch in Regulation K

---

[334] State Street (Feb. 6, 2013) at 3-4.

[335] State Street (Feb. 6, 2013) at 2.

[336] See SIFMA/CH/FSR (Feb. 6, 2013) at B18; State Street (Feb. 6, 2013) at 2.

makes it clear that a foreign branch of a U.S. bank is not a "representative office." In addition, Regulation K is a comprehensive regulation of the Federal Reserve Board that ensures that foreign branches operate for valid reasons.[337]

With regard to prong 4 of the Additional Factors (that the branch is engaged in banking or financing and subject to substantive local regulation), SIFMA/CH/FSR argue that this prong is unnecessary because, in addition to being regulated under Regulation K by the Federal Reserve, foreign branches are also subject to substantive local regulation and supervision, including licensing requirements and potentially local derivatives rules that the Commission could find to constitute substituted compliance. Although these commenters acknowledged that the nature and scope of these regulations will vary by jurisdiction, they state that many foreign jurisdictions require the same level of compliance with local regulations that U.S. regulators require of U.S. branches of foreign banks with regards to U.S. laws and regulations. They also stated that requiring foreign branches to show that they are subject to substantive regulation in their local jurisdiction so as to determine whether each swap they enter into is bona fide would be overly burdensome and unnecessary. In their view, the only relevant factor that the Commission should consider is whether the swap has been booked into the foreign branch, which the trade confirm would reflect.[338]

Conversely, one commenter argued that, consistent with clear evidence from the last crisis that the risks accrued by foreign branches, guaranteed subsidiaries, and even non-guaranteed subsidiaries all flow back to the parent entity, foreign branches of U.S. persons

---

[337] See SIFMA/CH/FSR (Feb. 6, 2013) at B19.

[338] See id. at B19-20.

should under no circumstances be subject to weaker regulation than the parent company. This commenter also argues that there is no substantive difference between a branch and a subsidiary of a U.S. person in terms of covering derivatives losses, and that both must be held to the same high standards as apply to the U.S. person itself. Otherwise, the U.S. taxpayer will be exposed to the risk of another massive bailout.[339] In addition, this commenter stated that claims made by industry groups that foreign branches of U.S. entities should not be classified as U.S. persons or they will find no foreign counterparties willing to do business with them are absurd and unsubstantiated, and taken literally, seem to suggest that the Commission should exempt all overseas swap activity from the requirements of Title VII of the Dodd-Frank Act, which would directly violate Congress's clear intent.

### 3. Commission Guidance

In preparing the Guidance, the Commission has carefully considered commenters' concerns and recommendations related to both the appropriate scope of the term "foreign branch" for purposes of this Guidance and Commission consideration of when a swap should be considered to be "with the foreign branch" of a U.S. bank that is a swap dealer or MSP.

#### a. Scope of the Term "Foreign Branch"

The Commission notes that foreign branches of a U.S. bank are part of a U.S. bank rather than a separate legal entity, and are therefore "U.S. persons." Nevertheless, as a policy matter, the Commission believes that CEA section 2(i) should be interpreted so as to exclude swap dealing transactions with a foreign branch of a U.S. swap dealer from the de minimis calculations for swap dealer or MSP registration. In addition, the Commission believes that CEA

---

[339] Better Markets (Feb. 15, 2013) at 2, 4-5.

section 2(i) should be interpreted so that swaps between a foreign branch of a U.S. swap dealer or MSP and a non-U.S. person should be eligible for substituted compliance with regard to Category A Transaction-Level Requirements.[340] The Commission believes that CEA section 2(i) should be interpreted in this manner in order to avoid the potential result that foreign entities would cease doing swap dealing business with foreign branches of U.S. registered swap dealers. However, the Commission notes that interpreting CEA section 2(i) in this manner creates a distinction between swaps with foreign branches of U.S. banks and swaps with the U.S. principal bank. Therefore, the Commission also believes that Commission consideration of both the scope of the term "foreign branch" and when a swap is with the foreign branch of a U.S. bank should be construed under CEA section 2(i) in a manner that does not create unnecessary distinctions between otherwise similar activities.

Therefore, the Commission interprets CEA section 2(i) such that, for purposes of this Guidance, the Commission will generally consider a "foreign branch" of a U.S. swap dealer or U.S. MSP to be any "foreign branch" (as defined in the applicable banking regulation) of a U.S. bank that is: (i) subject to Regulation K[341] or the FDIC International Banking Regulation,[342] or

---

[340] As discussed further in section G, under the Commission's interpretation of 2(i), in the case of a swap with a U.S. swap dealer or U.S. MSP (including an affiliate of a non-U.S. person, and including a foreign branch of a U.S. bank that is a swap dealer or MSP), the parties to the swap generally would not be not eligible for substituted compliance with one exception – where the swap is between the foreign branch of a U.S. bank that is a swap dealer or MSP and a non-U.S. person (regardless of whether the non-U.S. person is guaranteed or otherwise supported by, or is an affiliate conduit of, a U.S. person).

[341] Regulation K is a regulation issued by the Board of Governors of the Federal Reserve ("Federal Reserve Board") under the authority of the Federal Reserve Act ("FRA") (12 U.S.C. 221 et seq.); the Bank Holding Company Act of 1956 ("BHC Act") (12 U.S.C. 1841 et seq.and the International Banking Act of 1978 ("IBA") (12 U.S.C. 3101 et seq.). Regulation K sets forth rules governing the international and foreign activities of U.S. banking organizations, including procedures for establishing foreign branches to engage in international banking.

Under Regulation K, 12 CFR part 211, a "foreign branch" is defined as "an office of an organization (other than a representative office) that is located outside the country in which the organization is legally established and at which a banking or financing business is conducted." See 17 CFR 211.2(k).

otherwise designated as a "foreign branch" by the U.S. bank's primary regulator, (ii) maintains accounts independently of the home office and of the accounts of other foreign branches with the profit or loss accrued at each branch determined as a separate item for each foreign branch,[343] and (iii) subject to substantive regulation in banking or financing in the jurisdiction where it is located (the "Foreign Branch Characteristics"). However, in addition to the foregoing Foreign Branch Characteristics, the Commission will consider other relevant facts and circumstances in considering whether a foreign office of a U.S. bank is a "foreign branch" of a U.S. bank for purposes of this Guidance.

Further, for purposes of this Guidance, the Commission interprets CEA section 2(i) so that generally a foreign branch of a U.S. bank could include an office of a foreign bank that satisfies the foregoing Foreign Branch Characteristics. However, a foreign branch of a U.S. bank would generally not include an affiliate of a U.S. bank that is incorporated or organized as a separate legal entity.

In considering the scope of the term "foreign branch," the Commission agrees with commenters that stated that Regulation K of the Federal Reserve Board's regulations provides a useful reference because Regulation K provides a comprehensive regime for regulation of foreign branches that ensures that foreign branches of U.S. banks operate for valid reasons and

---

[342] 12 CFR part 347 is a regulation issued by the Federal Deposit Insurance Corporation under the authority of the Federal Deposit Insurance Act (12 U.S.C. 1828(d)(2)), which sets forth rules governing the operation of foreign branches of insured state nonmember banks ("FDIC International Banking Regulation"). Under 12 CFR 347.102(j), a "foreign branch" is defined as "an office or place of business located outside the United States, its territories, Puerto Rico, Guam, American Samoa, the Trust Territory of the Pacific Islands, or the Virgin Islands, at which banking operations are conducted, but does not include a representative office."

[343] The Commission notes that national banks operating foreign branches are required under section 25 of the Federal Reserve Act, 12 U.S.C. 604a, to conduct the accounts of each foreign branch independently of the accounts of other foreign branches established by it and of its home office, and are required at the end of each fiscal period to transfer to its general ledger the profit or loss accrued at each branch as a separate item.

are not "representative offices." Similarly, the Commission believes that the FDIC International Banking Regulation provides a useful reference for U.S. banks that have foreign branches which are subject to FDIC jurisdiction.[344]

In addition, regardless of a foreign branch of a U.S. bank is subject to Regulation K or the FDIC International Banking Regulation or is otherwise designated as a "foreign branch" by the U.S. bank's primary regulator, the Commission believes that CEA section 2(i) should be interpreted so that, for purposes of this Guidance, a foreign branch of a U.S. bank should generally also be subject to substantive regulation in banking or financing in the jurisdiction where it is located. Finally, the Commission believes that in order for a foreign office of a U.S. bank to be viewed as a "foreign branch" for purposes of this Guidance, another factor should generally be present – the foreign branch should maintain its accounts independently of the home office and of the accounts of other foreign branches, and at the end of each fiscal period the U.S. bank should transfer to its general ledger the profit or loss accrued at each branch as a separate item.[345]

---

[344] See notes 341 and 342 above and accompanying text for additional information regarding the definition of a "foreign branch" in Regulation K and the FDIC International Banking Regulation.

[345] The Commission notes that section 25 of the Federal Reserve Act, 12 U.S.C. 604a, states that national banking associations with $1 million or more in capital and surplus may file an application with the Board of Governors of the Federal Reserve System for permission to exercise certain powers, including establishment of foreign branches. In addition, section 25(9) requires that every national banking association operating foreign branches conduct the accounts of each foreign branch independently of the accounts of other foreign branches established by it and of its home office, and at the end of each fiscal period transfer to its general ledger the profit or loss accrued at each branch as a separate item.

### b. Commission Consideration of Whether a Swap is With a Foreign Branch of a U.S. Bank

With regard to Commission consideration of whether a swap by a U.S. bank through a foreign office should be considered to be "with a foreign branch" of the U.S. person for purposes of the de minimis calculations for swap dealer and MSP registration[346] or application of the Transaction-Level Requirements[347] under this Guidance, the Commission has carefully considered the comments submitted on this question.

SIFMA/CH/FSR stated that the only criteria that is relevant in determining whether a swap is bona fide with a foreign branch of a U.S. swap dealer is whether the swap is booked in the foreign branch (as reflected in the trade confirmation ), with the term "foreign branch" defined with reference to Regulation K. However, the Commission's view is that the trade confirmation generally is not relevant for purposes of determining whether to treat a swap as being with a foreign branch of a U.S. bank rather than with the U.S. principal bank. In reality, because the foreign branch of a U.S. bank is not a separate legal entity, the U.S. principal bank would generally be the party that is ultimately responsible for a swap with its foreign branch. The Commission's view is that a foreign branch of a U.S. bank should be considered a "U.S. person" under this Guidance because it is a part of the U.S. bank. Moreover, Better Markets has argued that foreign branches of U.S. banks as well as foreign subsidiaries and affiliates should be treated exactly the same as U.S. persons in all respects under this Guidance.

---

[346] See section B, supra.

[347] See section G, infra.

However, in light of principles of international comity and giving consideration to comments that state that foreign branches of U.S. banks will be at a competitive disadvantage if foreign branches of U.S. banks are not treated the same as non-U.S. persons, the Commission believes that in considering whether a swap should be considered as being with the foreign branch of a U.S. bank under this Guidance, all of the facts and circumstances are relevant. In particular, the Commission's view is that if all of the following factors are present, generally the swap should be considered to be with the foreign branch of a U.S. bank for purposes of this Guidance:

(i) the employees negotiating and agreeing to the terms of the swap (or, if the swap is executed electronically, managing the execution of the swap), other than employees with functions that are solely clerical or ministerial, are located in such foreign branch or in another foreign branch of the U.S. bank;

(ii) the foreign branch or another foreign branch is the office through which the U.S. bank makes and receives payments and deliveries under the swap on behalf of the foreign branch pursuant to a master netting or similar trading agreement, and the documentation of the swap specifies that the office for the U.S. bank is such foreign branch;

(iii) the swap is entered into by such foreign branch in its normal course of business;

(iv) the swap is treated as a swap of the foreign branch for tax purposes; and

(v) the swap is reflected in the local accounts of the foreign branch.

However, if material terms of the swap are negotiated or agreed to by employees of the U.S. bank located in the United States, the Commission believes that generally the swap should

be considered to be with the U.S. principal bank, rather than its foreign branch, for purposes of this Guidance.

The Commission also believes that the factors enumerated above would be relevant both to an analysis of whether a swap should be considered to be between a foreign branch of a U.S. bank and a non-U.S. swap dealer and an analysis of whether a swap should be considered to be between two foreign branches of U.S. banks. The Commission discusses each of the enumerated factors in more detail below.

The first of the five factors enumerated above is similar to prong 1 of the Additional Factors (whether the employees negotiating the swap for the U.S. person are located in the foreign branch, or if the swap is executed electronically, the employees managing the execution of the swap); however, the first factor above considers whether the employees negotiating and agreeing to the terms of the swap are located in any foreign branch of the U.S. bank. This modification addresses the objection of commenters that stated that employees that negotiate and agree to swaps are often located outside the foreign branch for bona fide reasons.[348] However, to the extent that material terms of the swap are negotiated or agreed by employees of the U.S. bank located in the United States, the Commission believes that generally the swap should be considered to be with the U.S. principal bank for purposes of this Guidance.

The second factor above is similar to prong (ii) of the January Order Criteria (that the documentation of the swap specifies that the counterparty or "office" for the U.S. person is such foreign branch). However, because a foreign branch of a U.S. bank is not a separate legal entity, the Commission believes that the U.S. principal bank generally should be considered to be the

---

[348] See, e.g., SIFMA/CH/FSR (Feb. 6, 2013) at B18; State Street (Feb. 6, 2013) at 2-4.

counterparty for purposes of this Guidance irrespective of whether the foreign branch is named as the counterparty in the swap documentation. Therefore, the Commission has modified the second factor, consistent with its other interpretations of section 2(i), so that it makes no reference to the foreign branch as counterparty. Rather, the second factor above relates to whether the foreign branch or another foreign branch is the office through which the U.S. bank makes and receives payments and deliveries under the swap on behalf of the foreign branch pursuant to a master netting or similar trading agreement, and whether the documentation of the swap specifies that the office for the U.S. bank is such foreign branch. This modification is consistent with the ISDA Master Agreement, which requires that each party specify an "office" for each swap, which is where a party "books" a swap and/or the office through which the party makes and receives payments and deliveries.

The third factor above (whether the swap is entered into by such foreign branch in its normal course of business) is the same as prong (iii) in the January Order Criteria discussed above. The Commission is concerned about the material terms of a swap being negotiated or agreed by employees of the U.S. bank that are located in the United States and then routed to a foreign branch in order for the swap to be treated as a swap with the foreign branch for purposes of the de minimis calculations for swap dealer and MSP registration or application of the Transaction-Level Requirements under this Guidance.

The fourth factor above (whether the swap is treated as a swap of the foreign branch for tax purposes) is the same as prong 2 of the Additional Factors. The Commission notes that State Street stated that it does not strongly object to prongs 2, 3 and 4 of the Additional Factors (that the swap is treated as a swap of the foreign branch for tax purposes, that the branch operates for valid business reasons and is not only a representative office, and that the branch is engaged in

banking or financing and subject to substantive local regulation) since they could "be reasonable indicia of a bona fide non-U.S. branch of a U.S. swap dealer." However, State Street stated that each of these prongs may be challenging to properly define and evaluate.[349] Other commenters stated that the income from a swap that is booked in a foreign branch of a U.S. person is subject to taxation in the local jurisdiction in which the foreign branch is resident, which demonstrates that such swaps are bona fide with the non-U.S. branch.[350] The Commission notes that the fourth factor above only refers to whether the tax treatment of the swap is consistent with the swap being treated as a swap of the foreign branch for tax purposes.

The fifth factor above focuses on whether the swap is reflected in the accounts of the foreign branch. The Commission believes that where a swap is bona fide with the foreign branch of a U.S. bank, it generally would be reflected in the foreign branch's accounts.

### D. Description of the Entity-Level and Transaction-Level Requirements

Title VII of the Dodd-Frank Act establishes a comprehensive new regulatory framework for swap dealers and MSPs that Congress enacted with the goal of reducing systemic risk and enhancing market transparency. Under this framework, a swap dealer or MSP must, among other things, comport with certain standards (and regulations as the Commission may promulgate) governing risk management, internal and external business conduct, and reporting. Further, swap dealers and MSPs are required to comply with all of the requirements applicable to swap dealers and MSPs for all their swaps, not just the swaps that make them a swap dealer or MSP.

---

[349] See State Street (Feb. 6, 2013) at 2.

[350] See, e.g., SIFMA/CH/FSR (Feb. 6, 2013) at B18.

Even before the Commission published the Proposed Guidance, a number of commenters recommended that the Commission, in interpreting the cross-border applicability of the Dodd-Frank Act swaps provisions, should distinguish between requirements that apply at an entity level (i.e., to the firm as a whole) as compared to those that apply at a transactional level (i.e., to the individual swap transaction or trading relationship).[351] These commenters argued that requirements that relate to the core operations of a firm and should be applied to the entity as a whole would include the capital and related prudential requirements and recordkeeping, as well as certain risk mitigation requirements (e.g., information barriers and the designation of a chief compliance officer). The commenters stated that other requirements, such as margin, should apply on transaction-by-transaction basis and only to swaps with U.S. counterparties.

Commenters on the Proposed Guidance generally supported the division of Dodd-Frank's swaps provisions (and Commission regulations thereunder) into Entity-Level and Transaction-Level Requirements.[352] Certain of these commenters, however, made specific recommendations for reclassification of some of these Requirements, which are discussed in section E below.

The Commission agrees with the commenters that the various Dodd-Frank Act swaps provisions applicable to swap dealers and MSPs can be conceptually separated into Entity-Level Requirements, which apply to a swap dealer or MSP firm as a whole, and Transaction-Level Requirements, which apply on a transaction-by-transaction basis. Descriptions of each of the Entity-Level Requirements under this Guidance are set out immediately below, followed by

---

[351] See, e.g., SIFMA (Feb. 3, 2011); ISDA (Jan. 24, 2011); Cleary (Sept. 20, 2011); Barclays Bank PLC, BNP Paribas S.A., Deutsche Bank AG, Royal Bank of Canada, The Royal Bank of Scotland Group PLC, Societe Generale, and UBS AG (Jan. 11, 2011); Barclays Bank PLC, BNP Paribas S.A., Credit Suisse AG, Deutsche Bank AG, HSBC, Nomura Securities International, Inc., Rabobank Nederland, Royal Bank of Canada, The Royal Bank of Scotland Group PLC, Societe Generale, The Toronto-Dominion Bank, and UBS AG (Feb. 17, 2011).

[352] See, e.g., SocGen (Aug. 8, 2012) at 6; IIB (Aug. 27, 2012) at 2; Clearing House (Aug. 27, 2012) at 22.

descriptions of the Transaction-Level Requirements. Additional information related to the categorization of Entity-Level and Transaction-Level Requirements is discussed in section E.

### 1. Description of the Entity-Level Requirements

The Entity-Level Requirements under Title VII of the Dodd-Frank Act and the Commission's regulations promulgated thereunder relate to: (i) capital adequacy; (ii) chief compliance officer; (iii) risk management; (iv) swap data recordkeeping; (v) swap data repository reporting ("SDR Reporting"); and (vi) physical commodity large swaps trader reporting ("Large Trader Reporting"). The Entity-Level Requirements apply to registered swap dealers and MSPs across all their swaps without distinctions as to the counterparty or the location of the swap (although under this Guidance in some circumstances the availability of substituted compliance may vary based on whether the counterparty is a U.S. person or a non-U.S. person).

The Entity-Level Requirements are split into two categories. The first category of Entity-Level Requirements includes capital adequacy, chief compliance officer, risk management, and swap data recordkeeping under Commission regulations 23.201 and 23.203 (except certain aspects of swap data recordkeeping relating to complaints and sales materials) ("First Category"). The second category of Entity-Level Requirements includes SDR Reporting, certain aspects of swap data recordkeeping relating to complaints and marketing and sales materials under Commission regulations 23.201(b)(3) and 23.201(b)(4) and Large Trader Reporting ("Second Category").

Each of the Entity-Level Requirements is discussed in the subsections that follow.

### a. First Category of Entity-Level Requirements

#### i. Capital adequacy

Section 4s(e)(2)(B) of the CEA specifically directs the Commission to set capital requirements for swap dealers and MSPs that are not subject to the capital requirements of U.S. prudential regulators (hereinafter referred to as "non-bank swap dealers or MSPs").[353] With respect to the use of swaps that are not cleared, these requirements must: "(1) [h]elp ensure the safety and soundness of the swap dealer or major swap participant; and (2) [be] appropriate for the risk associated with the non-cleared swaps held as a swap dealer or major swap participant."[354] Pursuant to section 4s(e)(3), the Commission proposed regulations, which would require non-bank swap dealers and MSPs to hold a minimum level of adjusted net capital (i.e., "regulatory capital") based on whether the non-bank swap dealer or MSP is: (i) also a FCM; (ii) not an FCM, but is a non-bank subsidiary of a bank holding company; or (iii) neither an FCM

---

[353] See 7 U.S.C. 6s(e)(2)(B). Section 4s(e) of the CEA explicitly requires the adoption of rules establishing capital and margin requirements for swap dealers and MSPs, and applies a bifurcated approach that requires each swap dealer and MSP for which there is a U.S. prudential regulator to meet the capital and margin requirements established by the applicable prudential regulator, and each swap dealer and MSP for which there is no prudential regulator to comply with the Commission's capital and margin regulations. See 7 U.S.C. 6s(e). Further, systemically important financial institutions ("SIFIs") that are not FCMs would be exempt from the Commission's capital requirements, and would comply instead with Federal Reserve Board requirements applicable to SIFIs, while nonbank (and non-FCM) subsidiaries of U.S. bank holding companies would calculate their Commission capital requirement using the same methodology specified in Federal Reserve Board regulations applicable to the bank holding company, as if the subsidiary itself were a bank holding company. The term "prudential regulator" is defined in CEA section 1a(39) as the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Farm Credit Administration, and the Federal Housing Finance Agency. See 7 U.S.C. 1a(39). In addition, in the proposed capital regulations for swap dealers and MSPs, the Commission solicited comment regarding whether it would be appropriate to permit swap dealers and MSPs to use internal models for computing market risk and counterparty credit risk charges for capital purposes if such models had been approved by a foreign regulatory authority and were subject to periodic assessment by such foreign regulatory authority. See Capital Requirements of Swap Dealers and Major Swap Participants, 76 FR 27802 (May 12, 2011) ("Proposed Capital Requirements").

[354] See 7 U.S.C. 6s(e)(3)(A).

nor a non-bank subsidiary of a bank holding company.[355] The primary purpose of the capital requirement is to reduce the likelihood and cost of a swap dealer's or MSP's default by requiring a financial cushion that can absorb losses in the event of the firm's default.

ii. Chief compliance officer

Section 4s(k) requires that each swap dealer and MSP designate an individual to serve as its chief compliance officer ("CCO") and specifies certain duties of the CCO.[356] Pursuant to section 4s(k), the Commission adopted regulation 3.3, which requires swap dealers and MSPs to designate a CCO who would be responsible for administering the firm's compliance policies and procedures, reporting directly to the board of directors or a senior officer of the swap dealer or MSP, as well as preparing and filing with the Commission a certified report of compliance with the CEA. The chief compliance function is an integral element of a firm's risk management and oversight and the Commission's effort to foster a strong culture of compliance within swap dealers and MSPs.

iii. Risk management

Section 4s(j) of the CEA requires each swap dealer and MSP to establish internal policies and procedures designed to, among other things, address risk management, monitor compliance with position limits, prevent conflicts of interest, and promote diligent supervision, as well as

---

[355] See 7 U.S.C. 6s(e). See also Proposed Capital Requirements, 76 FR at 27817 ("The Commission's capital proposal for [swap dealers] and MSPs includes a minimum dollar level of $20 million. A non-bank [swap dealer] or MSP that is part of a U.S. bank holding company would be required to maintain a minimum of $20 million of Tier 1 capital as measured under the capital rules of the Federal Reserve Board. [A swap dealer] or MSP that also is registered as an FCM would be required to maintain a minimum of $20 million of adjusted net capital as defined under [proposed] section 1.17. In addition, [a swap dealer] or MSP that is not part of a U.S. bank holding company or registered as an FCM would be required to maintain a minimum of $20 million of tangible net equity, plus the amount of the [swap dealer's] or MSP's market risk exposure and OTC counterparty credit risk exposure.").

[356] See 7 U.S.C. 6s(k).

maintain business continuity and disaster recovery programs.[357] The Commission adopted implementing regulations 23.600, 23.601, 23.602, 23.603, 23.605, and 23.606).[358] The Commission also adopted regulation 23.609, which requires certain risk management procedures for swap dealers or MSPs that are clearing members of a DCO.[359] Collectively, these requirements help to establish a robust and comprehensive internal risk management program for swap dealers and MSPs, which is critical to effective systemic risk management for the overall swaps market.

iv. Swap data recordkeeping (except certain aspects of swap data recordkeeping relating to complaints and sales materials)

CEA section 4s(f)(1)(B) requires swap dealers and MSPs to keep books and records for all activities related to their business.[360] Sections 4s(g)(1) and (4) require swap dealers and MSPs to maintain trading records for each swap and all related records, as well as a complete audit trail for comprehensive trade reconstructions.[361] Pursuant to these provisions, the Commission adopted regulations 23.201and 23.203, which require swap dealers and MSPs to

---

[357] 7 U.S.C. 6s(j).

[358] Swap Dealer and Major Swap Participant Recordkeeping, Reporting, and Duties Rules; Futures Commission Merchant and Introducing Broker Conflicts of Interest Rules; and Chief Compliance Officer Rules for Swap Dealers, Major Swap Participants, and Futures Commission Merchants, 77 FR 20128 (Apr. 3, 2012) ("Final Swap Dealer and MSP Recordkeeping Rule") (relating to risk management program, monitoring of position limits, business continuity and disaster recovery, conflicts of interest policies and procedures, and general information availability, respectively).

[359] Customer Clearing Documentation, Timing of Acceptance for Clearing, and Clearing Member Risk Management, 77 FR 21278 (Apr. 9, 2012) ("Final Customer Documentation Rules"). Also, swap dealers must comply with Commission regulation 23.608, which prohibits swap dealers providing clearing services to customers from entering into agreements that would: (i) disclose the identity of a customer's original executing counterparty; (ii) limit the number of counterparties a customer may trade with; (iii) impose counterparty-based position limits; (iv) impair a customer's access to execution of a trade on terms that have a reasonable relationship to the best terms available; or (v) prevent compliance with specified time frames for acceptance of trades into clearing.

[360] 7 U.S.C. 6s(f)(1)(B).

[361] 7 U.S.C. 6s(g)(1).

keep records including complete transaction and position information for all swap activities, including documentation on which trade information is originally recorded. Pursuant to Commission regulation 23.203, records of swaps must be maintained for the duration of the swap plus 5 years, and voice recordings for 1 year, and records must be "readily accessible" for the first 2 years of the 5 year retention period. Swap dealers and MSPs also must comply with Parts 43, 45 and 46 of the Commission's regulations, which, respectively, address the data recordkeeping and reporting requirements for all swaps subject to the Commission's jurisdiction, including swaps entered into before the date of enactment of the Dodd-Frank Act ("pre-enactment swaps") and swaps entered into on or after the date of enactment of the Dodd-Frank Act but prior to the compliance date of the swap data reporting rules ("transition swaps").[362]

**b. Second Category of Entity-Level Requirements**

i. SDR Reporting

CEA section 2(a)(13)(G) requires all swaps, whether cleared or uncleared, to be reported to a registered SDR.[363] CEA section 21 requires SDRs to collect and maintain data related to swaps as prescribed by the Commission, and to make such data electronically available to particular regulators under specified conditions related to confidentiality.[364] Part 45 of the Commission's regulations (and Appendix 1 thereto) sets forth the specific swap data that must be reported to a registered SDR, along with attendant recordkeeping requirements; and part 46 addresses recordkeeping and reporting requirements for pre-enactment and transition swaps

---

[362] See 17 CFR 46.1 et seq.; Swap Data Recordkeeping and Reporting Requirements: Pre-Enactment and Transition Swaps, 76 FR 22833 (Apr. 25, 2011) ("Proposed Data Rules").

[363] 7 U.S.C. 2(a)(13)(G).

[364] 7 U.S.C. 24a.

("historical swaps"). The fundamental goal of part 45 of the Commission's regulations is to ensure that complete data concerning all swaps subject to the Commission's jurisdiction is maintained in SDRs where it will be available to the Commission and other financial regulators for fulfillment of their various regulatory mandates, including systemic risk mitigation, market monitoring and market abuse prevention. Part 46 supports similar goals with respect to pre-enactment and transition swaps and ensures that data needed by regulators concerning "historical" swaps is available to regulators through SDRs. Among other things, data reported to SDRs will enhance the Commission's understanding of concentrations of risks within the market, as well as promote a more effective monitoring of risk profiles of market participants in the swaps market. The Commission also believes that there are benefits that will accrue to swap dealers and MSPs as a result of the timely reporting of comprehensive swap transaction data and consistent data standards for recordkeeping, among other things. Such benefits include more robust risk monitoring and management capabilities for swap dealers and MSPs, which in turn will improve the monitoring of their current swaps market positions.

ii. Swap data recordkeeping relating to complaints and marketing and sales materials

CEA section 4s(f)(1) requires swap dealers and MSPs to "make such reports as are required by the Commission by rule or regulation regarding the transactions and positions and financial condition of the registered swap dealer or MSP."[365] Additionally, CEA section 4s(h) requires swap dealers and MSPs to "conform with such business conduct standards … as may be

[365] 7 U.S.C. 6s(f)(1).

prescribed by the Commission by rule or regulation."[366] Pursuant to these provisions, the Commission promulgated final rules that set forth certain reporting and recordkeeping for swap dealers and MSPs.[367] Commission Regulation 23.201 states that "[e]ach swap dealer and major swap participant shall keep full, complete, and systematic records of all activities related to its business as a swap dealer or major swap participant." Such records must include, among other things, "[a] record of each complaint received by the swap dealer or major swap participant concerning any partner, member, officer, employee, or agent,"[368] as well as "[a]ll marketing and sales presentations, advertisements, literature, and communications."[369]

iii. Physical commodity large swaps trader reporting (Large Trader Reporting)

CEA section 4t authorizes the Commission to establish a large trader reporting system for significant price discovery swaps (of which the economically equivalent swaps subject to part 20 of the Commission's regulations are a subset).[370] Pursuant thereto, the Commission adopted its Large Trader Reporting rules (part 20 of the Commission's regulations), which require routine reports from swap dealers, among other entities, that hold significant positions in swaps that are linked, directly or indirectly, to a prescribed list of U.S.-listed physical commodity futures contracts.[371] Additionally, Large Trader Reporting requires that swap dealers, among other entities, comply with certain recordkeeping obligations.

---

[366] 7 U.S.C. 6s(h)(1); see 7 U.S.C. 6s(h)(3).

[367] Final Swap Dealer and MSP Recordkeeping Rule, 77 FR 20128.

[368] 17 CFR 23.201(b)(3)(i).

[369] 17 CFR 23.201(b)(4).

[370] 7 U.S.C. 6t.

[371] Large Trader Reporting for Physical Commodity Swaps, 76 FR 43851 ( July 22, 2011). The rules require routine position reporting by clearing organizations, as well as clearing members and swap dealers with reportable positions

### 2. **Description of the Transaction-Level Requirements**

The Transaction-Level Requirements include: (i) required clearing and swap processing; (ii) margining (and segregation) for uncleared swaps; (iii) mandatory trade execution; (iv) swap trading relationship documentation; (v) portfolio reconciliation and compression; (vi) real-time public reporting; (vii) trade confirmation; (viii) daily trading records; and (ix) external business conduct standards.

The Transaction-Level Requirements – with the exception of external business conduct standards – relate to both risk mitigation and market transparency. Certain of these requirements, such as clearing and margining, serve to lower a firm's risk of failure. In that respect, these Transaction-Level Requirements could be classified as Entity-Level Requirements. Other Transaction-Level Requirements – such as trade confirmation, swap trading relationship documentation, and portfolio reconciliation and compression – also serve important risk mitigation functions, but are less closely connected to risk mitigation of the firm as a whole and thus are more appropriately applied on a transaction-by-transaction basis. Likewise, the requirements related to trade execution, trade confirmation, daily trading records, and real-time public reporting have a closer nexus to the transparency goals of the Dodd-Frank Act, as opposed to addressing the risk of a firm's failure.

As a result, whether a particular requirement of Title VII should apply on a transaction-by-transaction basis in the context of cross-border activity for purposes of section 2(i) of the

---

in the covered physical commodity swaps. The rules also establish recordkeeping requirements for clearing organizations, clearing members and swap dealers, as well as traders with positions in the covered physical commodity swaps that exceed a prescribed threshold. In general, the rules apply to swaps that are linked, directly or indirectly, to either the price of any of the 46 U.S. listed physical commodity futures contracts the Commission enumerates (Covered Futures Contracts) or the price of the physical commodity at the delivery location of any of the Covered Futures Contracts.

CEA requires the Commission to exercise some degree of judgment. Nevertheless, in the interest of comity principles, the Commission believes that the Transaction-Level Requirements may be applied on a transaction-by-transaction basis. The Transaction-Level Requirements are split into two categories. All of the Transaction-Level Requirements except external business conduct standards are in Category A. The external business conduct standards are in Category B.

Each of the Transaction-Level Requirements is discussed below.

**a. Category A: Risk Mitigation and Transparency**

i. Required clearing and swap processing

Section 2(h)(1) of the CEA requires a swap to be submitted for clearing to a DCO if the Commission has determined that the swap is required to be cleared, unless one of the parties to the swap is eligible for an exception from the clearing requirement and elects not to clear the swap.[372] Clearing via a DCO mitigates the counterparty credit risk between swap dealers or MSPs and their counterparties.

Commission regulations implementing the first designations of swaps for required clearing were published in the Federal Register on December 13, 2012.[373] Under Commission regulation 50.2, all persons executing a swap that is included in a class of swaps identified under Commission regulation 50.4 must submit such swap to an eligible DCO for clearing as soon as technologically practicable after execution, but in any event by the end of the day of execution.

---

[372] 7 U.S.C. 2(h)(1), (7).

[373] Clearing Requirement Determination Under Section 2(h) of the CEA, 77 FR 74284 (Dec. 13, 2012) ("Clearing Requirement Determination").

Regulation 50.4 establishes required clearing for certain classes of swaps. Currently, those classes include, for credit default swaps: specified series of untranched North American CDX indices and European iTraxx indices; and for interest rate swaps: fixed-to-floating swaps, basis swaps, forward rate agreements referencing U.S. Dollar, Euro, Sterling, and Yen, and overnight index swaps referencing U.S. Dollar, Euro, and Sterling. Each of the six classes is further defined in Commission regulation 50.4. Swaps that have the specifications identified in the regulation are required to be cleared and must be cleared pursuant to the rules of any eligible DCO[374] unless an exception or exemption specified in the CEA or the Commission's regulations applies.

Generally, if a swap is subject to CEA section 2(h)(1)(A) and part 50 of the Commission's regulations, it must be cleared through an eligible DCO, unless: (i) one of the counterparties is eligible for and elects the end-user exception under Commission regulation 50.50;[375] or (ii) both counterparties are eligible for and elect an inter-affiliate exemption under Commission regulation 50.52.[376] To elect either the End-User Exception or the Inter-Affiliate Exemption, the electing party or parties and the swap must meet certain requirements set forth in the regulations.

Closely connected with the clearing requirement are the following swap processing requirements: (i) Commission regulation 23.506, which requires swap dealers and MSPs to

---

[374] A DCO's eligibility to clear swaps that are required to be cleared pursuant to section 2(h)(1)(A) of the CEA and part 50 of the Commission's regulations is governed by regulation 39.5(a), relating to DCO eligibility.

[375] See End-User Exception to the Clearing Requirement for Swaps, 77 FR 42560 (July 19, 2012) ("End-User Exception").

[376] The Commission has adopted an exemption from required clearing for swaps between certain affiliated entities. Exemption for Swaps Between Certain Affiliated Entities, 78 FR 21750 (Apr. 11, 2013) ("Inter-Affiliate Exemption").

submit swaps promptly for clearing; and (ii) Commission regulations 23.610 and 39.12, which establish certain standards for swap processing by DCOs and/or swap dealers and MSPs that are clearing members of a DCO.[377] Together, required clearing and swap processing requirements promote safety and soundness of swap dealers and MSPs, and mitigate the credit risk posed by bilateral swaps between swap dealers or MSPs and their counterparties.[378]

ii. Margin and segregation requirements for uncleared swaps

Section 4s(e) of the CEA requires the Commission to set margin requirements for swap dealers and MSPs that trade in swaps that are not cleared.[379] The margin requirements ensure that outstanding current and potential future risk exposures between swap dealers and their counterparties are collateralized, thereby reducing the possibility that swap dealers or MSPs take on excessive risks without having adequate financial backing to fulfill their obligations under the uncleared swap. In addition, with respect to swaps that are not submitted for clearing, section 4s(l) requires that a swap dealer or MSP notify the counterparty of its right to request that funds provided as margin be segregated, and upon such request, to segregate the funds with a third-party custodian for the benefit of the counterparty. In this way, the segregation requirement enhances the protections offered through margining uncleared swaps and thereby provides

---

[377] 17 CFR 23.506 and 23.610. See also Final Customer Documentation Rules, 77 FR 21278.

[378] See section H regarding the application of required clearing rules to market participants that are not registered as swap dealers or MSPs, including the circumstances under which the parties to such swaps would be eligible for substituted compliance.

[379] See 7 U.S.C. 6s(e). See also Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 76 FR 23732, 23733-40 (Apr. 28, 2011) ("Proposed Margin Requirements"). Section 4s(e) explicitly requires the adoption of rules establishing margin requirements for swap dealers and MSPs, and applies a bifurcated approach that requires each swap dealer and MSP for which there is a prudential regulator to meet the margin requirements established by the applicable prudential regulator, and each swap dealer and MSP for which there is no prudential regulator to comply with the Commission's margin regulations. In contrast, the segregation requirements in section 4s(1) do not use a bifurcated approach – that is, all swap dealers and MSPs are subject to the Commission's regulations regarding notice and third party custodians for margin collected for uncleared swaps.

additional financial protection to counterparties. The Commission is working with foreign and domestic regulators to develop and finalize appropriate regulations for margin and segregation requirements.

iii. Trade execution

Integrally linked to the clearing requirement is the trade execution requirement, which is intended to bring the trading of swaps that are required to be cleared and are made available to trade onto regulated exchanges or execution facilities. Specifically, section 2(h)(8) of the CEA provides that unless a clearing exception applies and is elected, a swap that is subject to a clearing requirement must be executed on a DCM or SEF, unless no such DCM or SEF makes the swap available to trade.[380] Commission regulations implementing the process for a DCM or SEF to make a swap available to trade were published in the Federal Register on June 4, 2013.[381] Under Commission regulations 37.10 and 38.12, respectively, a SEF or DCM may submit a determination for Commission review that a mandatorily cleared swap is available to trade based on enumerated factors. By requiring the trades of mandatorily cleared swaps that are made available to trade to be executed on an exchange or an execution facility – each with its attendant pre- and post-trade transparency and safeguards to ensure market integrity – the trade execution requirement furthers the statutory goals of financial stability, market efficiency, and enhanced transparency.

---

[380] See 7 U.S.C. 2(h)(8).

[381] See Process for a Designated Contract Market or Swap Execution Facility To Make a Swap Available to Trade, Swap Transaction Compliance and Implementation Schedule, and Trade Execution Requirement Under the Commodity Exchange Act,78 FR 33606 (Jun. 4, 2013).

iv. Swap trading relationship documentation

CEA section 4s(i) requires each swap dealer and MSP to conform to Commission standards for the timely and accurate confirmation, processing, netting, documentation and valuation of swaps. Pursuant thereto, Commission regulation 23.504(a) requires swap dealers and MSPs to "establish, maintain and enforce written policies and procedures" to ensure that the swap dealer or MSP executes written swap trading relationship documentation.[382] Under Commission regulation 23.504(b), the swap trading relationship documentation must include, among other things: all terms governing the trading relationship between the swap dealer or MSP and its counterparty; credit support arrangements; investment and re-hypothecation terms for assets used as margin for uncleared swaps; and custodial arrangements.[383] Further, the swap trading relationship documentation requirement applies to all swaps with registered swap dealers and MSPs. In addition, Commission regulation 23.505 requires swap dealers and MSPs to document certain information in connection with swaps for which exceptions from required clearing are elected.[384] Swap documentation standards facilitate sound risk management and may promote standardization of documents and transactions, which are key conditions for central clearing, and lead to other operational efficiencies, including improved valuation.

---

[382] See also Confirmation, Portfolio Reconciliation, Portfolio Compression, and Swap Trading Relationship Documentation Requirements for Swap Dealers and Major Swap Participants; 77 FR 55904 (Sept. 11, 2012) ("Final Confirmation Rules").

[383] The requirement under section 4s(i) relating to trade confirmations is a Transaction-Level Requirement. Accordingly, Commission regulation 23.504(b)(2) requires a swap dealer's and MSP's swap trading relationship documentation to include all confirmations of swaps, will apply on a transaction-by-transaction basis.

[384] See also Final Confirmation Rules, 77 FR at 55964.

v. Portfolio reconciliation and compression

CEA section 4s(i) directs the Commission to prescribe regulations for the timely and accurate processing and netting of all swaps entered into by swap dealers and MSPs. Pursuant to CEA section 4s(i), the Commission adopted regulations (23.502 and 23.503), which require swap dealers and MSPs to perform portfolio reconciliation and compression, respectively, for all swaps.[385] Portfolio reconciliation is a post-execution risk management tool to ensure accurate confirmation of a swap's terms and to identify and resolve any discrepancies between counterparties regarding the valuation of the swap. Portfolio compression is a post-trade processing and netting mechanism that is intended to ensure timely, accurate processing and netting of swaps.[386] Regulation 23.503 requires all swap dealers and MSPs to establish policies and procedures for terminating fully offsetting uncleared swaps, when appropriate, and periodically participating in bilateral and/or multilateral portfolio compression exercises for uncleared swaps with other swap dealers or MSPs or conducted by a third party.[387] The rule also requires policies and procedures for engaging in such exercises for uncleared swaps with non-swap dealers and non-MSPs upon request. Further, participation in multilateral portfolio compression exercises is mandatory for dealer-to-dealer trades.

---

[385] See id.

[386] For example, the reduced transaction count may decrease operational risk as there are fewer trades to maintain, process, and settle.

[387] See Confirmation, Portfolio Reconciliation, and Portfolio Compression Requirements for Swap Dealers and Major Swap Participants, 75 FR 81519 (Dec. 28, 2010) ("Confirmation NPRM").

vi. Real-time public reporting

Section 2(a)(13) of the CEA directs the Commission to promulgate rules providing for the public availability of swap transaction and pricing data on a real-time basis.[388] In accordance with this mandate, the Commission promulgated part 43, which provides that all "publicly reportable swap transactions" must be reported and publicly disseminated, and which establishes the method, manner, timing and particular transaction and pricing data that must be reported by parties to a swap transaction.[389] Additionally, the Commission adopted regulation 23.205, which directs swap dealers and MSPs to undertake such reporting and to have the electronic systems and procedures necessary to transmit electronically all information and data required to be reported in accordance with part 43.[390] The real-time dissemination of swap transaction and pricing data supports the fairness and efficiency of markets and increases transparency, which in turn improves price discovery and decreases risk (e.g., liquidity risk).[391]

vii. Trade confirmation

Section 4s(i) of the CEA[392] requires that each swap dealer and MSP must comply with the Commission's regulations prescribing timely and accurate confirmation of swaps. The Commission has adopted regulation 23.501, which requires, among other things, a timely and accurate confirmation of swap transactions (which includes execution, termination, assignment,

---

[388] See 7 U.S.C. 2(a)(13). See also Real-Time Public Reporting of Swap Transaction Data, 77 FR 1182, 1183 (Jan. 9, 2012) ("Final Real-Time Reporting Rule").

[389] Part 43 defines a "publicly reportable swap transaction" as (i) any swap that is an arm's-length transaction between two parties that results in a corresponding change in the market risk position between the two parties; or (ii) any termination, assignment, novation, exchange, transfer, amendment, conveyance, or extinguishing of rights or obligations of a swap that changes the pricing of a swap. See Final Real-Time Reporting Rule, 77 FR 1182.

[390] Final Swap Dealer and MSP Recordkeeping Rule, 77 FR at 20205.

[391] See Final Real-Time Reporting Rule, 77 FR at 1183.

[392] 7 U.S.C. 6s(i).

novation, exchange, transfer, amendment, conveyance, or extinguishing of rights or obligations of a swap) among swap dealers and MSPs by the end of the first business day following the day of execution.[393] Timely and accurate confirmation of swaps – together with portfolio reconciliation and compression – are important post-trade processing mechanisms for reducing risks and improving operational efficiency.[394]

viii. Daily trading records

Pursuant to CEA section 4s(g), the Commission adopted regulation 23.202, which requires swap dealers and MSPs to maintain daily trading records, including records of trade information related to pre-execution, execution, and post-execution data that is needed to conduct a comprehensive and accurate trade reconstruction for each swap. The final rule also requires that records be kept of cash or forward transactions used to hedge, mitigate the risk of, or offset any swap held by the swap dealer or MSP.[395] Accurate and timely recordkeeping regarding all phases of a swap transaction can serve to greatly enhance a firm's internal supervision, as well as the Commission's ability to detect and address market or regulatory abuses or evasion.

**b. Category B: External Business Conduct Standards**

Pursuant to CEA section 4s(h), the Commission has adopted external business conduct rules, which establish business conduct standards governing the conduct of swap dealers and

---

[393] See also Final Confirmation Rules, 77 FR 55904.

[394] In addition, the Commission notes that regulation 23.504(b)(2) requires that the swap trading relationship documentation of swap dealers and MSPs must include all confirmations of swap transactions.

[395] See Final Swap Dealer and MSP Recordkeeping Rule, 77 FR 20128.

MSPs in dealing with their counterparties in entering into swaps.[396] Broadly speaking, these rules are designed to enhance counterparty protection by significantly expanding the obligations of swap dealers and MSPs towards their counterparties. Under these rules, swap dealers and MSPs will be required, among other things, to conduct due diligence on their counterparties to verify eligibility to trade, provide disclosure of material information about the swap to their counterparties, provide a daily mid-market mark for uncleared swaps and, when recommending a swap to a counterparty, make a determination as to the suitability of the swap for the counterparty based on reasonable diligence concerning the counterparty.

### E. Categorization of Entity-Level and Transaction-Level Requirements

As noted above, even before the Commission published the Proposed Guidance, a number of commenters recommended that the Commission, in interpreting the cross-border applicability of the Dodd-Frank Act swaps provisions, should distinguish between requirements that apply at an entity level (i.e., to the firm as a whole) as compared to those that apply at a transactional level (i.e., to the individual swap transaction or trading relationship).[397] The Commission agrees with such commenters, and generally expects that it may apply its policies differently depending on the category (Entity-Level or Transaction-Level) or sub-category (First or Second Category of Entity-Level Requirements or Category A or B of the Transaction-Level Requirements) into which such requirement falls, subject to its further consideration of all of the relevant facts and circumstances.

---

[396] See 7 U.S.C. 6s(h). See also External Business Conduct Rules, 77 FR at 9822-29.

[397] See note 351, supra.

After giving further consideration to the categorization in the Proposed Guidance, including comments received in this area, this Guidance makes a few minor modifications to the proposed categorization of Entity-Level and Transaction-Level Requirements, as described below.

### 1. Categorization under the Proposed Guidance

The Proposed Guidance separated the Entity-Level Requirements into two subcategories. The first included capital adequacy, chief compliance officer, risk management, and swap data recordkeeping, all of which relate to risks to a firm as a whole. The second proposed subcategory included SDR Reporting and Large Trader Reporting, which relate directly to the Commission's market oversight.

The Proposed Guidance separated the Transaction-Level Requirements into two subcategories, "Category A" and "Category B." The "Category A" Transaction-Level Requirements relate to risk mitigation and transparency: (1) clearing and swap processing; (2) margining and segregation for uncleared swaps; (3) trade execution; (4) swap trading relationship documentation; (5) portfolio reconciliation and compression; (6) real-time public reporting; (7) trade confirmation; and (8) daily trading records.

The "Category B" Transaction-Level Requirements – the external business conduct standards – are those requirements that may not be necessary to apply to swaps between non-U.S. persons taking place outside the United States. With respect to these swaps, the Commission believes that foreign regulators may have a relatively stronger supervisory interest in regulating sales practices concerns than the Commission.

### 2. **Comments**

Commenters generally supported the division of Dodd-Frank's swaps provisions (and Commission regulations thereunder) into Entity-Level and Transaction-Level Requirements.[398] Certain of these commenters, however, made specific recommendations for reclassification of some of these Requirements.

#### a. **Reporting and trade-execution requirements**

With regard to reporting and trade-execution requirements, a number of commenters argued that all forms of swaps reporting, including SDR Reporting and Large Trader Reporting, should be treated as Transaction-Level Requirements and thereby could be eligible for substituted compliance for certain transactions with non-U.S. counterparties.[399] In their view, SDR Reporting – like real-time public reporting – is implemented on a swap-by-swap basis and more closely linked to market transparency than risk mitigation. Credit Suisse noted that the Commission's bifurcated approach to SDR Reporting and real-time public reporting creates unnecessary complications. It argued that both sets of reporting requirements should apply to a non-U.S. swap dealer only when dealing with U.S. persons (excluding foreign branches of U.S. swap dealers).[400]

ISDA believed that real-time public reporting and trade execution should be treated like the external business conduct rules. It argued that these rules relate to pre-trade price discovery

---

[398] See, e.g., SocGen (Aug. 8, 2012) at 6; IIB (Aug. 27, 2012) at 2; Clearing House (Aug. 27, 2012) at 22.

[399] See, e.g., SIFMA (Aug. 27, 2012) at A4, A34, A35; Credit Suisse (Aug. 27, 2012) at 10; Association for Financial Markets in Europe (AFME) (Aug. 24, 2012) at 8-9.

[400] Credit Suisse (Aug. 27, 2012) at 10.

and market structure and client protections.[401] Similarly, J.P. Morgan commented that the real-time public reporting and trade execution requirements should not apply to transactions between non-U.S. swap dealers or non-U.S. MSPs and non-U.S. counterparties, arguing that these requirements do not reduce market risk but rather promote price competition.[402] IIB stated that the Commission should treat mandatory trade execution, real-time public reporting and daily trading records as "Category B" Transaction-Level Requirements, since these requirements are intended to give customers enhanced access to the best pricing and affect not only individual counterparties but the overall market.[403]

On the other hand, Senator Levin stated that reporting and trade execution requirements should be applied broadly to all swaps of non-U.S. swap dealers and non-U.S. MSPs that are affiliates of U.S. financial institutions, so as to provide transparency regarding their swap activities and to protect the U.S. financial system.[404] He stated that standard trade execution

---

[401] ISDA (Aug. 27, 2012) at 11. Similarly, Australian Bankers stated that the real-time public reporting and trade execution requirements should be treated in the same manner as the external business conduct standards and have no application to transactions involving a non-U.S. swap dealer and its non-U.S. counterparties. Australian Bankers (Aug. 27, 2012) at 5. See also SIFMA (Aug. 27, 2012) at A37 (stating that real-time public reporting should be treated in the same way as external business conduct standards and, in particular, should not apply to non-U.S. swap entities or non-U.S. branches for transactions with non-U.S. persons).

[402] See also The Clearing House (Aug. 27, 2012) at 22 (stating that no pre- or post-trade transparency rules or conflict of interest rules should apply to transactions with non-U.S. counterparties. These rules should be treated similarly to the external business conduct rules – excluded from the Transaction-Level and Entity-Level categories, and not applied at all to transactions between a non-U.S. entity (including a non-U.S. branch of a U.S. entity) and its non-U.S. counterparty, regardless of whether that counterparty is guaranteed by, or a conduit for, a U.S. person).

[403] IIB (Aug. 27, 2012) at 17, 32-33. IIB further stated that application of these pre- and post-trade requirements to swaps between non-U.S. persons outside the United States would raise "serious, unprecedented" concerns relating to the sovereignty of foreign markets. IIB (Aug. 27, 2012) at 34.

[404] Letter from Sen. Levin at 11-12.

helps to ensure that complex swaps are properly booked, and reporting discourages "below-the-radar" transactions involving complex swaps.[405]

**b. Swap trading relationship documentation, portfolio reconciliation and compression, daily trading records and external business conduct standards**

Sumitomo stated that certain Transaction-Level Requirements, including swap trading relationship documentation, portfolio reconciliation and compression, daily trading records, and external business conduct standards, should instead be classified as Entity-Level Requirements. It contended that these are not logically linked to particular transactions and would be required to be conducted on a daily basis per counterparty.[406] IATP stated that portfolio compression and reconciliation requirements are critical to a firm's central risk mitigation functions and therefore should be classified as Entity-Level Requirements. This commenter also argued that margin, segregation and other requirements for swaps that are so designated by non-U.S. affiliates of U.S. persons as to be unclearable should be regulated under the Entity-Level Requirements.[407]

Similarly, Senator Levin stated that clearing, margin and portfolio reconciliation and compression requirements and external business conduct standards should be applied to all swaps of non-U.S. swap dealers and non-U.S. MSPs that are affiliates of U.S. financial institutions.[408] In the Senator's view, margin requirements are critical safeguards against rapidly increasing losses, portfolio reconciliation and compression procedures help to maintain an

---

[405] Id.

[406] Sumitomo (Aug. 24, 2012) at 3.

[407] IATP (Aug. 27, 2012) at 7.

[408] Letter from Sen. Levin at 11-12.

accurate understanding of the size and nature of a firm's swaps positions, and external business conduct standards encourage integrity in the swaps markets.[409] Societe Generale also stated that rules relating to confirmation processing and portfolio reconciliation and compression should be categorized as Entity-Level Requirements, explaining that these all relate to the functioning of a swap dealer's "back office" operations and are tied to its trading systems. As a result, implementing confirmation rules, for example, for swaps with U.S. persons only is "extremely difficult from a technological standpoint."[410]

IIB recommended that the daily trading records requirements (Commission regulation 23.202) be categorized as a Category B Transaction-Level Requirement. It reasoned that this rule is most relevant when a non-U.S. swap dealer or non-U.S. MSP is trading with a U.S. person to whom it owes U.S. sales practice obligations and for whom the Commission's interest in addressing market abuses is highest. It also noted that the obligation to make and retain records of pre-execution oral conversations, a principal element of the rule, is most likely to give rise to conflicts with foreign privacy laws.[411]

**c. Internal conflicts of interest requirement**

IIB noted that the internal conflicts of interest requirement (Commission regulation 23.605) is categorized as an Entity-Level Requirement in the Proposed Guidance. It stated that

---

[409] Id.

[410] SocGen (Aug. 8, 2012) at 6 (stating that banks with a centralized booking model will face technological difficulties in applying confirmation processing and portfolio reconciliation and compression rules only with respect to U.S. persons, and that a requirement to apply these rules to all customers (even non-U.S. persons) is inconsistent with international comity). See also Australian Bankers (Aug. 27, 2012) at 5 (stating that portfolio reconciliation and compression requirements should be categorized as Entity-Level Requirements, as they are critical to risk mitigation and back-office functions).

[411] IIB (Aug. 27, 2012) at 32-33.

internal research conflicts of interest procedures are intended to promote the integrity of research reports to customers, and that internal clearing conflicts of interest procedures are intended to promote client access to better pricing on execution and clearing. As a result, IIB views the Commission's interest in applying these requirements to non-U.S. clients as minimal and recommends that the internal conflicts of interest requirement be categorized as a new "Category B" Entity-Level Requirement.[412]

**d. Position limits and anti-manipulation rules**

SIFMA stated that position limits and anti-manipulation rules, which were not addressed in the Proposed Guidance, should be categorized as Transaction-Level Requirements and, therefore, be eligible for relief in some circumstances. They argued that these rules have a close nexus to market transparency, as opposed to risk mitigation of a firm's failure.[413]

3. **Commission Guidance**

In general, the Commission would apply the Dodd-Frank provisions differently depending on the category (Entity-Level or Transaction-Level) or sub-category (First or Second Category of Entity-Level Requirements or Category A or B of the Transaction-Level Requirements) into which such requirement falls. Therefore, the Commission has carefully reviewed comments on the classification of the Entity-Level Requirements and Transaction-Level Requirements, as well as comments regarding whether and how Entity-Level and Transaction-Level Requirements should apply to swaps between various types of counterparties,

---

[412] IIB (Aug. 27, 2012) at 32. This would render internal conflicts of interest requirements applicable only in connection with personnel of its research department or clearing unit preparing research reports for use with, or providing clearing services to, respectively, U.S. persons.

[413] SIFMA (Aug. 27, 2012) at A35-36.

and under what circumstances the Commission's policy should contemplate that various swaps should generally be eligible for substituted compliance, or provide that certain of the Commission's requirements would generally not apply.

After careful consideration, the Commission would generally treat swaps requirements as Entity-Level Requirements and Transaction-Level Requirements largely in accordance with the Proposed Guidance, with certain minor modifications described below.

**a. Entity-Level Requirements**

Consistent with CEA section 2(i), the Commission would treat the following requirements as Entity-Level Requirements, as proposed: capital adequacy, chief compliance officer, risk management, swap data recordkeeping, SDR Reporting, and Large Trader Reporting.

At the core of a robust internal risk controls system is the firm's capital – and particularly, how the firm identifies and manages its risk exposure arising from its portfolio of activities.[414] Equally foundational to the financial integrity of a firm is an effective internal risk management process, which must be comprehensive in scope and reliant on timely and accurate data regarding its swap activities. To be effective, such a system must have a strong and independent compliance function. These internal controls-related requirements – namely, the requirements related to chief compliance officer, risk management, swap data recordkeeping – are designed to serve that end. Given their functions, the Commission's policy is that these

[414] By way of illustration, consistent with the purpose of the capital requirement, which is intended to reduce the likelihood and cost of a swap dealer's default by requiring a financial cushion, a swap dealer's or MSP's capital requirements would be set on the basis of its overall portfolio of assets and liabilities.

requirements should be applied on a firm-wide basis to effectively address risks to the swap dealer or MSP as a whole, and should be classified as Entity-Level Requirements.

SDR Reporting and Large Trader Reporting relate more closely to market transparency and to the Commission's market surveillance program. Among other things, data reported to SDRs will enhance the Commission's understanding of concentrations of risks within the market, as well as promote a more effective monitoring of risk profiles of market participants in the swaps market. Large Trader Reporting, along with an analogous reporting system for futures contracts, is essential to the Commission's ability to conduct effective surveillance of markets in U.S. physical commodity futures and economically equivalent swaps. Given the functions of these reporting requirements, the Commission's view is that each requirement generally should be applied across swaps, irrespective of the counterparty or the location of the swap, in order to ensure that the Commission has a comprehensive and accurate picture of market activities. Otherwise, the intended value of these requirements would be significantly compromised, if not undermined. Therefore, the Commission's policy is to generally treat SDR Reporting and Large Trader Reporting as Entity-Level Requirements.

The Commission did not address in the Proposed Guidance whether position limits and anti-manipulation provisions should fall in the Entity-Level or Transaction-Level Requirements category. It is the Commission's view that these provisions relate more to market integrity, as opposed to the financial integrity of a firm, and it is essential that they apply regardless of the counterparty's status (U.S. person or not) in order to fully achieve the underlying purpose of these respective provisions. Accordingly, these requirements are outside the scope of this Guidance. However, the monitoring of position limits under Commission regulation 23.601 is included in the Entity-Level Requirements under this Guidance.

After considering the input of market participants and others through the comment process, and giving further consideration to how the language in CEA section 2(i) should be interpreted for purposes of applying the Entity-Level Requirements and permitting substituted compliance, the Commission's policy is to treat the Entity-Level Requirements in subcategories largely as proposed.

As explained above, Entity-Level Requirements ensure that registered swap dealers and MSPs implement and maintain a comprehensive and robust system of internal controls to ensure the financial integrity of the firm, and in turn, the protection of the financial system. In this respect, the Commission has strong supervisory interests in applying the same rigorous standards, or comparable and comprehensive standards, to non-U.S. swap dealers and non-U.S. MSPs whose swap activities or positions are substantial enough to require registration under the CEA. Requiring such swap dealers and MSPs to rigorously monitor and address the risks they incur as part of their day-to-day businesses would lower the registrants' risk of default – and ultimately protect the public and the financial system.

Therefore, the Commission contemplates that non-U.S. swap dealers and non-U.S. MSPs will comply with all of the First Category of Entity-Level Requirements. In addition, consistent with principles of international comity, substituted compliance may be available for these Entity-Level Requirements in certain circumstances, as explained further below. In contrast, with regard to Entity-Level Requirements in the Second Category, substituted compliance should generally be available only where the counterparty is a non-U.S. person.[415]

---

[415] In addition, as noted in section G below, reflecting its interpretation of CEA section 2(i), the Commission generally contemplates that U.S. swap dealers and MSPs would comply in full with the Entity-Level Requirements (regardless of whether the Entity-Level Requirements are classified as being in the First Category or Second

i. The First Category – Capital Adequacy, Chief Compliance Officer, Risk Management, and Swap Data Recordkeeping (except for certain recordkeeping requirements)

The Commission's policy generally is to treat the requirements related to capital adequacy, chief compliance officer, risk management, and swap data recordkeeping (except swap data recordkeeping relating to complaints and marketing and sales materials under Commission regulations 23.201(b)(3) and 23.201(b)(4), respectively) in the First Category. These requirements address and manage risks that arise from a firm's operation as a swap dealer or MSP. Collectively, they constitute a firm's first line of defense against financial, operational, and compliance risks that could lead to a firm's default.

The First Category is identical to the first subcategory proposed by the Commission in the Proposed Guidance, except that the Commission's policy is to treat swap data recordkeeping under part 43 and part 46 of the Commission's regulations and swap data recordkeeping related to complaints and marketing and sales materials under Commission regulations 23.201(b)(3) and 23.201(b)(4) as part of the "Second Category" of Entity-Level Requirements. As noted above, for Entity-Level Requirements in the First Category, substituted compliance generally would be available for a non-U.S. swap dealer or non-U.S. MSP (including one that is an affiliate of a U.S. person) regardless of whether the counterparty is a U.S. person or a non-U.S. person.[416] In contrast, for Entity-Level Requirements in the Second Category, substituted compliance

---

Category), without substituted compliance available. This interpretation also applies to swaps with U.S. swap dealers or U.S. MSPs that are affiliates of non-U.S. persons.

[416] As explained in section G below, the Commission's policy is that where a swap dealer or MSP is a U.S. person, all of the entity-level requirements would generally apply in full (without substituted compliance available), regardless of the type of counterparty.

generally would be available for a non-U.S. swap dealer or MSP only where the counterparty is a non-U.S. person.

ii. The Second Category – SDR Reporting, Certain Swap Data Recordkeeping Requirements and Large Trader Reporting

The Commission's policy retains SDR Reporting in the Second Category, as proposed. SDR Reporting furthers the goals of the Dodd-Frank Act to reduce systemic risk, increase transparency and promote market integrity. Specifically, data reported to SDRs under the SDR Reporting rules provide the Commission with information necessary to better understand and monitor concentrations of risk, as well as risk profiles of individual market participants for cleared and uncleared swaps.

The Commission believes that retaining SDR Reporting in the Second Category would be appropriate. Consistent with section 2(i), the Commission's policy is that U.S. swap dealers or MSPs (including those that are affiliates of a non-U.S. person) generally should comply in full with all of the Entity-Level Requirements, including SDR Reporting. Further, non-U.S. swap dealers and non-U.S. MSPs (including those that are affiliates of a U.S. person), generally should comply with SDR Reporting, and substituted compliance should be available (to the extent applicable) only where the swap counterparty is a non-U.S. person, provided that the Commission has direct access (including electronic access) to the relevant swap data that is stored at the foreign trade repository.[417]

The Commission contemplates treating swap data recordkeeping related to complaints and marketing and sales materials under Commission regulations 23.201(b)(3) and 23.201(b)(4)

---

[417] See section G, infra, for additional information on the application of the Entity-Level Requirements.

as part of the "Second Category" because, in the Commission's view, non-U.S. swap dealers and non-U.S. MSPs (including those that are affiliates of a U.S. person) generally should comply with SDR Reporting. Further, substituted compliance should be available for non-U.S. swap dealers or MSPs, to the extent applicable, only where the swap counterparty is a non-U.S. person.

Large Trader Reporting furthers the goals of the Dodd-Frank Act to reduce systemic risk, increase transparency and promote market integrity. Large Trader Reporting, in conjunction with the Commission's large trader reporting system for futures contracts, is essential to the Commission's ability to conduct effective surveillance of markets in U.S. physical commodity futures and economically equivalent swaps. Given the regulatory function of Large Trader Reporting, the Commission's policy is to apply these requirements to non-U.S. persons whose trading falls within its scope to the same extent as U.S. persons. Accordingly, as discussed further in section G below, the Commission would not recognize substituted compliance in place of compliance with Large Trader Reporting.

**b. Transaction-Level Requirements**

As previously noted, whether a particular Dodd-Frank Act requirement should apply on a transaction-by-transaction basis in the context of cross-border activity for purposes of section 2(i) of the CEA requires the exercise of some degree of judgment. Nevertheless, bearing in mind principles of international comity, the Commission anticipates that, in general, the Transaction-Level Requirements may be applied on a transaction-by-transaction basis.

The Commission's policy contemplates treating as Transaction-Level Requirements all of the requirements that the Commission proposed to include. Thus, the Transaction-Level Requirements are: (1) required clearing and swap processing; (2) margining and segregation for

uncleared swaps; (3) trade execution; (4) swap trading relationship documentation; (5) portfolio reconciliation and compression; (6) real-time public reporting; (7) trade confirmation; (8) daily trading records; and (9) external business conduct standards.

The Commission contemplates treating the Transaction-Level Requirements in two subcategories, designated as Category A and Category B, largely as proposed. Generally, these categories reflect how the Commission generally contemplates applying various Transaction-Level Requirements to various types of counterparties, and in guiding the consideration of when substituted compliance will be available under this Guidance.[418]

i. The Category A Transaction-Level Requirements

The "Category A" Transaction-Level Requirements relate to risk mitigation and transparency, and included the first eight Transaction-Level requirements referenced above.

The Commission does not believe it would be appropriate to treat, as suggested by commenters, swap trading relationship documentation, portfolio reconciliation and compression, daily trading records and external business conduct standards as Entity-Level Requirements. The Commission recognizes that firms may find a certain degree of operational efficiency in applying these requirements on a firm-wide basis. On the other hand, the Commission expects that treatment of these as Transaction-Level Requirements should allow for greater flexibility in terms of whether and how Dodd-Frank requirements apply. For example, under the Proposed Guidance, the Commission would not interpret section 2(i) generally to apply the Dodd-Frank's clearing requirement to a swap between a non-U.S. swap dealer and a non-U.S. counterparty. In

[418] Substituted compliance is discussed in section F, infra. The application of the Category A Transaction-Level Requirements and eligibility for substituted compliance is discussed in section IV.G.4. The application of the Category B Transaction-Level Requirements is discussed in section IV.G.5. The application of certain CEA provisions and certain Entity and Transaction-Level Requirements to non-registrants is discussed in section IV.H.

the Commission's judgment, allowing swap trading relationship documentation, portfolio reconciliation and compression and external business conduct standards to be applied on a transaction basis would not undermine the underlying regulatory objectives and, yet, will give due recognition to the home jurisdiction's supervisory interest. Consistent with this rationale, the Commission would treat margin, segregation, and related requirements as Transaction-Level Requirements.

The Commission also is retaining the trade execution requirement, as proposed, in Category A. The trade execution requirement is intended to bring the trading of mandatorily cleared swaps that are made available to trade onto regulated exchanges or execution facilities. By requiring the trades of mandatorily cleared swaps that are made available to trade to be executed on an exchange or an execution facility – each with its attendant pre- and post-trade transparency and safeguards to ensure market integrity – the trade execution requirement furthers the statutory goals of promoting financial stability, market efficiency and enhanced transparency.

The Commission's policy will treat real-time public reporting as a Transaction-Level Requirement. However, for the reasons discussed below, the Commission clarifies that it does not intend that its policy would preclude a market participant from applying real-time public reporting with respect to swap transactions that are not necessarily subject to this Transaction-Level Requirement if doing so would be more efficient for the market participant.

Part 43 of the Commission's regulations and part 45 of the Commission's regulations, respectively, prescribe the data fields that are to be included in real-time public reporting and SDR Reporting reports with respect to a reportable swap transaction.[419]

The Commission understands from commenters that in certain circumstances, reporting part 43 and part 45 data for the same swap transaction in separate reports ("two stream reporting") could accommodate market participants that have a transactional structure and/or systems that are designed or suited to send separate submissions.[420] However, the Commission also recognizes that in other circumstances, permitting market participants to include part 43 and part 45 data for the same swap transaction in a single report ("single stream reporting") could optimize efficiency.[421]

The Commission anticipated that reporting parties might elect to use one data reporting stream for both SDR Reporting and real-time public reporting under part 45 and part 43 respectively, to reduce costs and optimize efficiency, and many market participants have chosen

---

[419] See generally Final Real-Time Reporting Rule, 77 FR at 1250-1266; Swap Data Recordkeeping and Reporting Requirements, 77 FR 2136, 2210-24 (Jan. 13, 2012) ("Final Data Rules"). Part 43 applies to reports of swap transaction and pricing data to a registered SDR, in order that the SDR can publicly disseminate such data pursuant to part 43 and Appendix A to part 43 as soon as technologically practicable after execution of the publicly reportable swap. Final Real-Time Reporting Rule, 77 FR at 1249. Under part 45, counterparties report creation data for the swap – including all primary economic terms ("PET") data and confirmation data – as well as continuation data also as soon as technologically practicable. See Final Data Rules, 77 FR at 2149-51, 2199-202.

[420] See Final Real-Time Reporting Rule, 77 FR at 1237 (Jan. 9, 2012) (noting that "… coordination is expected to reduce costs by allowing reporting parties, SEFs and DCMs to send one set of data to an SDR for the purpose of satisfying the requirements of both rules."); id. at 1210 (noting that " … although reporting parties may use the same data stream for reporting regulatory data and real-time data, Commission regulation 43.4(d)(2) clarifies the intent of the Proposing Release: The reporting requirements for SEFs, DCMs and reporting parties for real-time public reporting purposes are separate from the requirement to report to an SDR for regulatory reporting purposes.").

[421] Final Data Rules, 77 FR at 2150, 2182. If SDR Reporting and real-time public reporting do not both apply to a swap transaction, market participants that have connected to registered SDRs and employed single stream reporting infrastructure and systems may be required to change such systems to bifurcate the part 43 and part 45 data sets, which are generated and transmitted in a single report. The Commission understands that such bifurcation could occur due to the manner with which Transaction-Level and Entity-Level requirements apply to the particular swap transaction.

to build and integrate single stream reporting systems.[422] The Commission is aware that, as commenters have stated, categorizing SDR Reporting under part 45 as an Entity-Level requirement and real-time public reporting under part 43 as a Transaction-Level requirement could, in certain circumstances, negate the benefits of single stream reporting, and could present challenges to market participants who have built single stream reporting infrastructure.

In view of these concerns, the Commission would, in general, treat real-time public reporting as a Transaction-Level Requirement. However, the Commission does not intend that its policy would preclude a market participant from applying real-time public reporting with respect to swap transactions that are not necessarily subject to this Transaction-Level Requirement if, for example, this would allow the market participant to realize efficiency gains from single stream reporting or otherwise as discussed above.

ii. The Category B Transaction-Level Requirements (External Business Conduct Standards)

As proposed, the Commission's policy will treat external business conduct standards as a "Category B" Transaction-Level Requirement for purposes of the general application of this Transaction-Level Requirement to various categories of swap counterparties.[423] External business conduct standards are oriented toward customer-protection. Among other obligations, the external business conduct rules generally require registrants to conduct due diligence on their counterparties to verify eligibility to trade (including eligible contract participant status), refrain from engaging in abusive market practices, provide disclosure of material information about the

---

[422] Real-Time Public Reporting of Swap Transaction Data, 77 FR at 1217. See also Final Data Rules, 77 FR at 2182.

[423] The application of the Category B Transaction-Level Requirements to swap dealers and MSPs is discussed in section IV.G.5.

swap to their counterparties, provide a daily mid-market mark for uncleared swaps and, when recommending a swap to a counterparty, make a determination as to the suitability of the swap for the counterparty based on reasonable diligence concerning the counterparty. In the Commission's view, such rules have an attenuated link to, and are distinguishable from, market-oriented protections such as the trade execution mandate. Additionally, the Commission believes that the foreign jurisdictions in which non-U.S. persons are located are likely to have a significant interest in the type of business conduct standards that would be applicable to transactions with such non-U.S. persons within their jurisdiction. Because the Commission believes that foreign regulators may have a relatively stronger supervisory interest in regulating sales practices concerns related to swaps between non-U.S. persons taking place outside the United States than the Commission, the Commission believes that generally it is appropriate that the business conducts standards of the home jurisdiction, rather than those established by the Commission, apply to such transactions between non-U.S. persons.

After reviewing the comments on internal conflicts of interest procedures, the Commission has given consideration to whether to treat internal conflicts of interest rules relating to clearing under Commission regulation 23.605 under Category B of the Transaction-Level Requirements. The Commission considered the view of commenters that stated that this particular requirement is generally more akin to the external business conduct standards and, as such, can reasonably be expected to be narrowly targeted to apply only with respect to U.S. clients, without undermining the regulatory benefits associated with the rule. However, because the Commission believes that internal conflicts of interest related to clearing should be applied on a firm-wide basis, the Commission's policy is that this requirement generally should be treated as an Entity-Level Requirement as proposed.

The Commission also has considered whether internal conflicts of interest procedures relating to research should be treated as Entity-Level Requirements as proposed. These informational and supervisory firewalls are designed to ensure that research reports are free from undue influence by the firm's trading personnel. As a practical matter, it is generally difficult, if not impossible, to establish and maintain such safeguards on a transaction or client basis. Because the Commission believes that these firewalls, in order to achieve their regulatory purpose, should be applied on a firm-wide basis, the Commission's policy is that internal conflicts of interest procedures relating to research generally should be treated as Entity-Level Requirements.

### F. Substituted Compliance

#### 1. Proposed Guidance

In the Proposed Guidance, the Commission stated that a cross-border policy that allows for flexibility in the application of the CEA while ensuring the high level of regulation contemplated by the Dodd-Frank Act and avoiding potential conflicts between U.S. regulations and foreign law is consistent with principles of international comity. To that end, the Commission set forth a general framework for substituted compliance. Under this "substituted compliance" regime, the Commission may determine that certain laws and regulations of a foreign jurisdiction are comparable to and as comprehensive as a corresponding category of U.S. laws and regulations. If the Commission makes such a determination, then an entity or transaction in that foreign jurisdiction that is subject to the category of U.S. laws and regulations for which comparability is determined will be deemed to be in compliance therewith if that entity or transaction complies with the corresponding foreign laws and regulations.

### 2. **Comments**

Several commenters urged the Commission to use a principles-based approach and to review the legal regime as a whole, rather than evaluate comparability on an issue-by-issue basis.[424] A commenter supported the Commission's view that comparable does not mean identical, and urged the Commission to place an emphasis on shared principles and mutual recognition.[425]

Some commenters stated that foreign jurisdiction laws and regulations are unlikely to be identical to those in the United States and that they thus support the Commission's proposed "outcomes based approach" to evaluating whether foreign regulatory requirements meet Dodd-Frank normative objectives.[426] One of these commenters stated that in some cases foreign regulators would be faced with several challenges, noting that in "light touch" or principle-based regulatory jurisdictions, commodity derivatives data collection and surveillance is weak or even non-existent, as is concomitant enforcement.[427]

Commenters stressed the need to avoid imposing duplicative or conflicting regulatory requirements which could result in unnecessary costs.[428] Commenters urged the Commission to

---

[424] See, e.g., SIFMA, (Aug. 27, 2012) at 3, A46; State Street (Aug. 27, 2012) at 3; Global Financial Markets Association ("GFMA") (Aug. 27, 2012) at 2; Association for Financial Markets in Europe ("AFME") (Aug. 27, 2012) at 2; J.P. Morgan (Aug. 13, 2012) at 5; Australian Bankers (Aug. 27, 2012) at 2; Japanese Bankers Association (Aug. 27, 2012) at 3; Comissao de Valores Mobiliarios ("CVM") (Aug. 27, 2012) at 2.

[425] See, e.g., FSR (Aug. 27, 2012) at 6-7.

[426] See IATP (Aug. 27, 2012) at 11-12; IIAC (Aug. 27, 2012) at 2, 9-11.

[427] See IATP (Aug. 27, 2012) at 11-12.

[428] See, e.g., ICI (Aug. 23, 2012) at 7-11; Capital Markets (Aug. 24, 2012) at 5-6.

engage in a dialogue with other regulators[429] and to build on work done at the international level.[430]

Some commenters expressed the view that substituted compliance should not require Commission approval if the applicable foreign regulator promulgates applicable regulations in accordance with G20 commitments, or that a presumption that foreign rules are comparable should apply if the rules are consistent with G20 principles.[431] Some commenters urged the Commission to take what they described as an "equivalence approach" similar to EMIR in the European Union,[432] by making substituted compliance determinations based on recognition of "equivalent" jurisdictions and not of individual firms.[433] The European Commission stated that EU firms dealing with U.S. counterparties would always be subject to the Dodd-Frank Act, while U.S. firms dealing with EU counterparties could not be subject to EU rules if the EU decides to grant equivalence to the United States. The European Commission stated that it is difficult to understand why comparable foreign legislation in the EU should not be sufficient.[434]

Commenters, including foreign regulators, requested that the Commission more clearly outline the circumstances under which a particular foreign jurisdiction would be acceptable for

---

[429] See Deutsche Bank, Aug. 27, 2012 at 5-6; Lloyds (Aug. 24, 2012) at 2.

[430] See Australian Securities and Investments Commission; Hong Kong Monetary Authority; Monetary Authority of Singapore; Reserve Bank of Australia; Securities and Futures Commission, Hong Kong (Aug. 27, 2012) at 3-4.

[431] See CEWG (Aug. 27, 2012) at 7; CVM (Aug. 27, 2012) at 2; ICI (Aug. 23, 2012) at 9; IIB (Aug. 27, 2012) at 38-39; Hong Kong Banks (Aug. 27, 2012) at 2, 10, 14, 15; Korea Federation of Banks ("Korea Banks") (Aug. 27, 2012) at 2-3; The Clearing House (Aug. 27, 2012) at 3-4, 31-35.

[432] See Australian Securities and Investments Commission; Hong Kong Monetary Authority; Monetary Authority of Singapore; Reserve Bank of Australia; Securities and Futures Commission, Hong Kong (Aug. 27, 2012) at 2-3.

[433] See Deutsche Bank (Aug. 27, 2012) at 6.

[434] See European Commission (Aug. 24, 2012) at 4.

substituted compliance purposes.[435] Commenters stressed the need for comparability determinations to be transparent.[436] One commenter stated that comparability determinations should allow for notice and comment.[437] Another commenter stated that there should be a procedure for appeals, that memoranda of understanding ("MOUs") should form the framework for comparability determinations, and that the Commission should develop a process for periodic review of comparability determinations.[438]

Some commenters found the Commission's proposed approach to substituted compliance too narrow or limiting. The European Securities and Markets Authority ("ESMA") stated that when equivalence or substituted compliance is granted for an entire jurisdiction, registration should not be a prerequisite before substituted compliance can apply. ESMA also stated that the Commission's approach is quite limited because it is applied not uniformly but "chapter by chapter," which ESMA represents contradicts what they described as EMIR's concepts of equivalence and mutual recognition.[439] Japan FSA and Bank of Japan expressed concern that the scope of application of substituted compliance is too narrow and requested that it be extended to avoid overlap or conflict with foreign regulations.[440] Other commenters stated that the approach being taken toward substituted compliance was narrow and not in accordance with comity.[441] However, another commenter stated that substituted compliance procedures are an inferior

---

[435] See, e.g., Financial Services Authority (United Kingdom) (Aug. 24, 2012) at 3.

[436] See IIB (Aug. 27, 2012) at 40; American Bankers Association, (Aug. 27, 2012) at 2; IATP (Aug. 27, 2012) at 11.

[437] See American Bankers Association (Aug. 27, 2012) at 2.

[438] See IATP (Aug. 27, 2012) at 11-13.

[439] See ESMA (Aug. 27, 2012) at 3-4.

[440] See Japan FSA and Bank of Japan (Aug. 13, 2012) at 2-3.

[441] See SIFMA (Aug. 27, 2012) at 3, A46; Futures Industry Association (FIA), (Aug. 27, 2012) at 5-7.

option to direct compliance with Commission regulations. This commenter stated that the Commission does not violate principles of international comity by extending the cross-border application to cover how "U.S. persons" operate in foreign jurisdictions, particularly when those jurisdictions lack the laws and/or regulatory capacity to prevent damage to the U.S. economy resulting from counterparty defaults originating in foreign affiliate swaps.[442]

Another commenter stated that substituted compliance should be expanded to a broader category of swap transactions, specifically, to the trade execution requirement.[443]

Some commenters urged the Commission to clarify which law is "substituted" for U.S. law and allow swap entities to determine which jurisdictions' laws apply where it could be more than one.[444]

Some commenters expressed concern regarding the timing of reform in other jurisdictions, urging the Commission to delay substituted compliance implementation or provide a grace period for these jurisdictions.[445]

Some commenters urged the Commission not to allow substituted compliance or to use it only sparingly, pointing out the risks of substituted compliance by the Commission. For example, one commenter contended that substituted compliance fails to ensure rigorous regulation of derivatives markets and so should not be allowed for foreign subsidiaries of U.S. parents as these subsidiaries pose a severe risk to the U.S. economy.[446] This commenter also

---

[442] See IATP (Aug. 27, 2012) at 2-3.

[443] See Tradeweb Markets LLC (Aug. 27, 2012) at 4.

[444] See SIFMA (Aug. 27, 2012) at A48; Deutsche Bank (Aug. 27, 2012) at 6.

[445] See, e.g., CFA Institute (Aug. 27, 2012) at 3; Financial Services Authority (United Kingdom) (Aug. 24, 2012) at 3; Barclays (Aug. 27, 2012) at 2; ICAP Group (Aug. 27, 2012) at 2; IIB (Aug. 27, 2012) at 39.

[446] See Greenberger (Aug. 27, 2012) at 20-24.

stated that substituted compliance should only be used in "rare circumstances" and only after such rules in foreign jurisdictions have come into existence,[447] stating that the Commission "cannot, through its use of comity, consider other countries' interests to the total derogation of Congress's intent to protect U.S. taxpayers."[448] Citizen and taxpayer groups contended that substituted compliance should not be permitted when the swap transaction is with a U.S. counterparty,[449] including subsidiaries of a U.S. person.[450]

Commenters also urged that, to the extent substituted compliance is permitted, a rigorous approach be applied, including examining the history of enforcement in a foreign jurisdiction, the ability to revoke substituted compliance where necessary, the ability of the public to comment on substituted compliance applications, periodic review of the application of substituted compliance and a requirement that the applicant immediately inform the Commission of any material changes in its jurisdiction.[451]

With regard to SDR Reporting, some commenters disagreed with the Commission that a foreign trade repository must allow Commission access to information to be considered comparable, arguing that comparability should be based solely on the foreign jurisdiction's regulatory regime,[452] or that access is unnecessary where swaps are between non-U.S. counterparties.[453] In contrast, another commenter stated that open access to foreign swap data

---

[447] See Greenberger (Aug. 27, 2012) at 3, 19, 22-23.

[448] See Greenberger (Aug. 27, 2012) at 19.

[449] See Public Citizen (Aug. 27, 2012) at 13, 16, 19.

[450] See Better Markets (Aug. 27, 2012) at 10.

[451] See, e.g., Better Markets (Aug. 27, 2012) at 10-11; Public Citizen (Aug. 27, 2012) at 13, 16, 19.

[452] See Deutsche Bank (Aug. 27, 2012) at 6.

[453] See Japanese Bankers Association (Aug. 27, 2012) at 10.

repositories is necessary to ensure that foreign surveillance of transaction-level swaps data flow requirements is comparable and comprehensive.[454]

International regulators have continued to express commitment to the Pittsburgh G20 reforms of OTC derivatives regulation, including a commitment to harmonize cross-border regulations and allow for substituted compliance or equivalence arrangements when appropriate. However, no international consensus has emerged regarding the implementation of such reforms or the circumstances under which substituted compliance should be permitted. In an April 18, 2013 letter to Treasury Secretary Lew, nine international financial regulators expressed concern about fragmentation in the OTC derivatives market as a result of lack of regulatory coordination, noting that "[a]n approach in which jurisdictions require that their own domestic regulatory rules be applied to their firms' derivatives transactions taking place in broadly equivalent regulatory regimes abroad is not sustainable."[455] The letter expressed concern that such an approach would lead the global derivatives market to "recede into localized and less efficient structures, impairing the ability of business across the globe to manage risk." The letter also suggested, among other things, that cross-border rules be adopted that would not result in duplicative or conflicting requirements through substituted compliance or equivalence arrangements, and that a

---

[454] See IATP (Aug. 27, 2012) at 6-7.

[455] See letter to Treasury Secretary Lew regarding cross-border OTC derivatives regulation from Deputy Prime Minister Taro Aso, Minister of State for Finance Services, Government of Japan; Commissioner Michel Barnier, Commissioner for Internal Markets and Services, European Commission; Minister Pravin Gordhan, Minister of Finance, Government of South Africa; Minister Guido Mantega, Ministry of Finance, Government of Brazil; Minister Pierre Moscovici, Ministry of Finance, Government of France; Chancellor George Osborne, Chancellor of the Exchequer, Government of the United Kingdom; Minister Wolfgang Schäuble, Ministry of Finance, Government of Germany; Minister Anton Siluanov, Minister of Finance, Government of Russia; and Minister Eveline Widmer-Schlumpf, Finance Minister, Government of Switzerland ("Nine International Regulators") (Apr. 18, 2013). See also letter to Treasury Secretary Lew from Sens. Kristen E. Gillibrand, Thomas R. Carper, Kay R. Hagan, Heidi Heitkamp, Michael F. Bennet, and Charles E. Shumer (June 26, 2013) (advocating domestic and international harmonization of derivatives regulation).

reasonable transition period and measures be provided to foreign entities to ensure a smooth transition.[456]

A group of 25 organizations from numerous nations responded by asserting that the letter to Treasury Secretary Lew "appears to place a higher priority on preventing 'fragmentation' in global financial markets than on effective management of global financial risks."[457] Emphasizing that the global financial crisis of 2008-2009 caused "mass unemployment, home foreclosures, and cutbacks in key public services," these organizations argued that "[s]ince G-20 nations have not yet met their 2009 Pittsburgh commitment to put in place effective derivatives regulation by the close of 2012, the first priority should be to complete this crucial element of financial oversight."[458] Although these organizations recognized the challenge of effectively regulating the global financial markets, they asserted that "the path to addressing these challenges does not lie in further delays that prevent any nation from acting until every jurisdiction globally has agreed on a similar approach."[459] Instead, these organizations urged the international community "to coordinate around a shared high level of financial oversight, and in the meantime to support the efforts of individual nations to ensure that the scope of their

---

[456] Id.

[457] See letter to Nine International Regulators from ActionAid International; AFL-CIO (American Federation of Labor And Congress of Industrial Organizations); Americans for Financial Reform; Berne Declaration; Center of Concern; The Centre for Research on Multinational Corporations (SOMO); Centre national de coopération au développement, CNCD-11.11.11; CGIL - Italian General Confederation of Labour; Consumer Federation of America; Global Progressive Forum; IBON International; The International Institute for Monetary Transformation; Institute for Agriculture and Trade Policy (IATP); Institute for Policy Studies, Global Economy Project; Jubilee Debt Campaign, UK; Kairos Europe (Brussels); Missionary Oblates - USP (Washington DC); Oxfam; Red Latinoamericana sobre Deuda, Desarrollo y Derechos – LATINDADD; Stamp Out Poverty; Tax Justice Network; UBUNTU Forum; War on Want; WEED (World Economy, Ecology, and Development); and World Development Movement (Jul. 1, 2013).

[458] Id.

[459] Id.

financial regulation properly captures all transactions, wherever conducted, that affect the safety and stability of each national financial system."[460]

### 3. Overview of the Substituted Compliance Regime

Once registered, a non-U.S. swap dealer or non-U.S. MSP would become subject to all of the substantive requirements under Title VII of the Dodd-Frank Act that apply to registered swap dealers or MSPs. In other words, the requirements under Title VII of the Dodd-Frank Act related to swap dealers and MSPs apply to all registered swap dealers and MSPs, irrespective of where they are based.

Consistent with CEA section 2(i) and comity principles, the Commission's policy generally is that eligible entities may comply with a substituted compliance regime under certain circumstances, subject, however, to the Commission's retention of its examination authority[461] and its enforcement authority. To the extent that the substituted compliance regime applies, the Commission generally would permit a non-U.S. swap dealer or MSP, U.S. bank that is a swap

---

[460] Id.

[461] Under Commission regulations 23.203 and 23.606, all records required by the CEA and the Commission's regulations to be maintained by a registered swap dealer or MSP shall be maintained in accordance with Commission regulation 1.31 and shall be open for inspection by representatives of the Commission, the United States Department of Justice, or any applicable prudential regulator.

In the January Order, the Commission noted that an applicant for registration as a swap dealer or MSP must file a Form 7-R with the National Futures Association and that Form 7-R was being modified at that time to address existing blocking, privacy or secrecy laws of foreign jurisdictions that applied to the books and records of swap dealers and MSPs acting in those jurisdictions. See 78 FR at 871-72 n. 107. The modifications to Form 7-R were a temporary measure intended to allow swap dealers and MSPs to apply for registration in a timely manner in recognition of the existence of the blocking, privacy, and secrecy laws. The Commission clarifies that the change to Form 7-R impacts the registration application only and does not modify the Commission's authority under the CEA and its regulations to access records held by registered swap dealers and MSPs. Commission access to a registrant's books and records is a fundamental regulatory tool necessary to properly monitor and examine each registrant's compliance with the CEA and the regulations adopted pursuant thereto. The Commission has maintained an ongoing dialogue on a bilateral and multilateral basis with foreign regulators and with registrants to address books and records access issues and may consider appropriate measures where requested to do so.

dealer or MSP with respect to its foreign branches,[462] or non-U.S. non-registrant that is a guaranteed or conduit affiliate, as applicable, to substitute compliance with the requirements of the relevant home jurisdiction's law and regulations (or in the case of foreign branches of a bank, the foreign location of the branch) in lieu of compliance with the attendant Entity-Level Requirements and/or Transaction-Level Requirements under the CEA and Commission regulations, provided that the Commission finds that such home jurisdiction's requirements (or in the case of foreign branches of a bank, the foreign location of the branch) are comparable with and as comprehensive as the corollary area(s) of regulatory obligations encompassed by the Entity- and Transaction-Level Requirements. Significantly, the Commission will rely upon an outcomes-based approach to determine whether these requirements achieve the same regulatory objectives of the Dodd-Frank Act. An outcomes-based approach in this context means that the Commission is likely to review the requirements of a foreign jurisdiction for rules that are comparable to and as comprehensive as the requirements of the Dodd-Frank Act, but it will not require that the foreign jurisdiction have identical requirements to those established under the Dodd-Frank Act. This approach builds on the Commission's longstanding policy of recognizing comparable regulatory regimes based on international coordination and comity principles with respect to cross-border activities involving futures (and options on futures).[463] The Commission

---

[462] The types of offices which the Commission would consider to be a "foreign branch" of a U.S. bank, and the circumstances in which a swap is with such foreign branch, are discussed further in section IV.C.3, supra.

[463] For example, under part 30 of the Commission's regulations, if the Commission determines that compliance with the foreign regulatory regime would offer comparable protection to U.S. customers transacting in foreign futures and options and there is an appropriate information-sharing arrangement between the home supervisor and the Commission, the Commission has permitted foreign brokers to comply with their home regulations (in lieu of the applicable Commission regulations), subject to appropriate conditions. See, e.g., Foreign Futures and Options Transactions, 67 FR 30785 (May 8, 2002); Foreign Futures and Options Transactions, 71 FR 6759 (Feb. 9, 2009).

anticipates that its approach also will require close consultation, cooperation, and coordination among the Commission and relevant foreign regulators regarding ongoing compliance efforts. To date, the Commission notes that it has engaged in many multilateral and bilateral consultations and efforts to coordinate on the substance of OTC derivatives reform efforts.

In part, because many foreign jurisdictions have been implementing OTC derivatives reforms in an incremental manner, the Commission's comparability determinations may be made on a requirement-by-requirement basis, rather than on the basis of the foreign regime as a whole. For example, many jurisdictions have moved more quickly to implement reporting to trade repositories, and so the Commission may focus first on comparability with those requirements. In addition, in making its comparability determinations, the Commission may include conditions that take into account timing and other issues related to coordinating the implementation of reform efforts across jurisdictions.

A non-U.S. swap dealer or non-U.S. MSP, a U.S. bank that is a swap dealer or MSP with respect to its foreign branches, or non-U.S. non-registrant that is a guaranteed or conduit affiliate, to the extent applicable under this Guidance, may comply with regulations in its home jurisdiction (or in the case of foreign branches of a bank, the foreign location of the branch) to the extent that the Commission determines that these requirements are comparable to, and as

---

Upon promulgating part 30, the Commission stated that it "intends to monitor closely the application of this regulatory scheme for the offer and sale of foreign futures and foreign options in the U.S. and to make adjustments in these rules, as necessary, based, in part, on it experience in administering the exemptive procedure [i.e., 30.10 relief] as well as other requests for interpretations of the provisions herein." Foreign Futures and Foreign Options Transactions, 52 FR 28980, 28993 (Aug. 5, 1987). For example, the Commission has expanded part 30 to allow 30.10-exempt foreign brokers to act as introducing brokers for the purpose of executing linked U.S. transactions on behalf of U.S. customers under certain circumstances. The Commission also promulgated regulation 30.12 to allow unlicensed "local" brokers located outside the United States to execute trades through the customer omnibus account of an FCM or 30.10 exempt foreign broker, again under certain circumstances. The Commission expects that the substituted compliance process contemplated by this Guidance may similarly evolve.

comprehensive as, the corollary areas of the CEA and Commission regulations.[464] As noted above, however, the home jurisdiction's requirements do not have to be identical to the Dodd-Frank Act requirements. Moreover, the Commission notes, however, that entities relying on substituted compliance may be required to comply with certain of the Dodd-Frank Act requirements where comparable and comprehensive regulation in their home jurisdiction (or in the case of foreign branches of a bank, the foreign locations of the branches) are determined to be lacking.[465]

In evaluating whether a particular category of foreign regulatory requirement(s) is comparable and comprehensive to the applicable requirement(s) under the CEA and Commission regulations, the Commission will take into consideration all relevant factors, including but not limited to, the comprehensiveness of those requirement(s), the scope and objectives of the relevant regulatory requirement(s), the comprehensiveness of the foreign regulator's supervisory compliance program, as well as the home jurisdiction's authority to support and enforce its oversight of the registrant. In this context, comparable does not necessarily mean identical. Rather, the Commission would evaluate whether the home jurisdiction's regulatory requirement is comparable to and as comprehensive as the corresponding U.S. regulatory requirement(s).

---

[464] As stated in note 88, for purposes of this Guidance, the terms "home jurisdiction" or "home country" are used interchangeably and refer to the jurisdiction in which the person or entity is established, including the European Union. Further, the Commission clarifies that where a non-U.S. swap dealer (or non-U.S. MSP), or a non-U.S. non-registrant that is a guaranteed or conduit affiliate, transacts outside the home jurisdiction, substituted compliance is available and they may comply with the comparable and comprehensive requirements of the home jurisdiction, provided that they comply with such requirements in that other jurisdiction.

[465] The Commission recognizes that substantial progress has been made in other jurisdictions towards implementing OTC derivatives reform. For example, EMIR requires financial counterparties, including hedge funds, to clear OTC derivatives contracts subject to the clearing obligation through a central counterparty registered or recognized in accordance with EMIR. EMIR also requires such entities to comply with EMIR's risk mitigation techniques for uncleared OTC derivatives contracts; risk mitigation techniques include, confirmation, portfolio reconciliation, compression, valuation and dispute resolution. Lastly, EMIR requires financial counterparties to report all derivatives contracts to a trade repository registered or recognized in accordance with EMIR.

In response to comments requesting greater clarity with respect to the substituted compliance determinations, the Commission notes that a comparability analysis would begin with a consideration of the regulatory objectives of a foreign jurisdiction's regulation of swaps and swaps market participants. In this regard, the Commission will first look to foreign regulator's swap-specific regulations. The Commission recognizes, however, that jurisdictions may not have swap-specific regulations in some areas, and instead may have regulatory or supervisory regimes that achieve comparable and comprehensive regulatory objectives as the Dodd-Frank Act requirements, but on a more general, entity-wide, or prudential, basis.[466] In addition, portions of a foreign regulatory regime may have similar regulatory objectives, but the means by which these objectives are achieved with respect to swaps market activities may not be clearly defined, or may not expressly include specific regulatory elements that the Commission concludes are critical to achieving the regulatory objectives or outcomes required under the CEA and the Commission's regulations. In these circumstances, the Commission anticipates that, as part of its broader efforts to consult and coordinate with foreign jurisdictions, it will work with the regulators and registrants in these jurisdictions to consider alternative approaches that may result in a determination that substituted compliance applies.[467]

The approaches used will vary depending on the circumstances relevant to each jurisdiction. One example would include coordinating with the foreign regulators in developing appropriate regulatory changes or new regulations, particularly where changes or new

---

[466] The Commission notes that, of the 35 provisionally registered non-U.S. swap dealers as of July 12, 2013, all but one of them are banking entities that are subject to prudential supervision by banking supervisors in their home jurisdictions or affiliates of such banks. By comparison, 19 of the provisionally registered U.S. swap dealers and MSPs are not regulated by a prudential supervisor or the SEC.

[467] The Commission notes that such alternatives are available for both Entity- and Transaction-Level Requirements, but are more likely appropriate for Entity-Level Requirements.

regulations already are being considered or proposed by the foreign regulators or legislative bodies. As another example, the Commission may, after consultation with the appropriate regulators and market participants, include in its substituted compliance determination a description of the means by which certain swaps market participants can achieve substituted compliance within the construct of the foreign regulatory regime. The identification of the means by which substituted compliance is achieved would be designed to address the regulatory objectives and outcomes of the relevant Dodd-Frank Act requirements in a manner that does not conflict with a foreign regulatory regime and reduces the likelihood of inconsistent regulatory obligations. For example, the Commission may specify that swap dealers and MSPs in the jurisdiction undertake certain recordkeeping and documentation for swap activities that otherwise is only addressed by the foreign regulatory regime with respect to financial activities generally. In addition, the substituted compliance determination may include provisions for summary compliance and risk reporting to the Commission to allow the Commission to monitor whether the regulatory outcomes are being achieved. By using these approaches, in the interest of comity, the Commission would seek to achieve its regulatory objectives with respect to the Commission's registrants that are operating in foreign jurisdictions in a manner that works in harmony with the regulatory interests of those jurisdictions.[468]

#### 4. Process for Comparability Determinations

Any comparability analysis will be based on a comparison of specific foreign requirements against specific related CEA provisions and Commission regulations in 13

[468] The Commission anticipates that non-U.S. SD and MSPs may require additional time after a Substituted Compliance Determination in order to phase in compliance with the relevant requirements of the jurisdiction in which the non-US SD or MSP is established. The Commission and its staff intend to address the need for any further transitional relief at the time that the subject Substituted Compliance Determination is made.

categories of regulatory obligations and will consider the factors described above. After receiving a submission from an applicant, the resulting comparability determination would be made by the Commission with regard to each of the 13 categories of regulatory obligations, as appropriate. More specifically, the Commission could determine that a particular set of foreign laws and regulations provides a sufficient basis for an affirmative finding of comparability with respect to a relevant area of regulatory obligations. Where no comparability determination can be made,[469] the non-U.S. swap dealer or non-U.S. MSP, U.S. bank that is a swap dealer or MSP with respect to its foreign branches, or non-registrant, to the extent applicable under this Guidance, may be required to comply with the applicable Entity- or Transactional-Level requirements under the CEA and Commission regulations.

Anyone who is eligible for substituted compliance may apply, either individually or collectively, as may foreign regulators. Persons who may request a comparability determination include: (i) foreign regulators, (ii) an individual non-U.S. entity, or group of non-U.S. entities; (iii) a U.S. bank that is a swap dealer or MSP with respect to its foreign branches; [470] or (iv) a trade association, or other group, on behalf of similarly-situated entities. Persons requesting a

---

[469] A finding of comparability may not be possible for a number of reasons, including the fact that the foreign jurisdiction has not yet implemented or finalized particular requirements.

[470] As previously noted, where the counterparty to a swap with a foreign branch is a non-U.S. person (whether or not such non-U.S. person is guaranteed or otherwise supported by, or is an affiliate conduit of, a U.S. person), the Commission continues to be of the view that compliance with comparable and comprehensive requirements in the foreign jurisdiction should be permitted in light of the supervisory interest of the foreign jurisdiction in the swaps transacted in that jurisdiction, together with the fact that foreign branches of U.S. swap dealers or U.S. MSPs are subject generally to direct or indirect oversight by U.S. regulators because they are part of a U.S. person. As discussed further in section IV.F.3, supra, the Commission's recognition of substituted compliance would be based on an evaluation of whether the requirements of the home jurisdiction are comparable and comprehensive to the applicable requirement(s) under the CEA and Commission regulations based on a consideration of all relevant factors, including among other things: (i) the comprehensiveness of the foreign regulator's supervisory compliance program and (ii) the authority of such foreign regulator to support and enforce its oversight of the registrant's branch or agency with regard to such activities to which substituted compliance applies.

comparability determination may want to coordinate their application with other market participants and their home regulators to simplify and streamline the process. Once a comparability determination is made for a jurisdiction, it will apply for all entities or transactions in that jurisdiction to the extent provided in the determination, as approved by the Commission.

Generally, the Commission would expect that the applicant, at a minimum, state with specificity the factual and legal basis for requesting that the Commission find that a particular set of foreign laws and regulations is comparable to, and as comprehensive as, particular Dodd-Frank Act requirements as described above; include with specificity all applicable legislation, rules, and policies; and provide an assessment whether the objectives of the two regulatory regimes are comparable and comprehensive.[471] If the applicant is a registered swap dealer or MSP, it also would generally be helpful to understand the capacity in which the applicant is licensed with the applicant's regulator(s) in its home country and whether the applicant is in good standing.

The Commission expects that the comparability analysis process would, in most cases, involve consultation with the regulators in each jurisdiction for which a substituted compliance application has been submitted so that the Commission may better analyze the compliance regime of a jurisdiction. Consultations are particularly important in the near future because many jurisdictions are in the process of finalizing and implementing their derivatives reforms incrementally and the Commission's comparability determinations may need to take into account the timing of regulatory reforms that have been proposed or finalized, but not yet implemented.

---

[471] The Commission may, as it deems appropriate and necessary, conduct an on-site examination of the applicant, as well as consult with the applicant's home regulator regarding the status of the applicant. For certain matters, the Commission may request an opinion of counsel.

Further, the Commission expects that, in connection with a determination that substituted compliance is appropriate, it would enter into an appropriate MOU or similar arrangement between the Commission and the relevant foreign regulator(s). Existing information-sharing and/or enforcement arrangements would be indicative of a foreign supervisor's ability to share information and otherwise work with the Commission. However, going forward, the Commission and relevant foreign supervisor(s) would need to establish supervisory MOUs or other arrangements that provide for information sharing and cooperation in the context of supervising swap dealers and MSPs. The Commission contemplates that such a supervisory MOU would establish the type of coordination activities that would continue on an ongoing basis between the Commission and the foreign supervisor(s), including topics such as procedures for confirming continuing oversight activities, access to information,[472] on-site visits, and notification procedures in certain situations.[473]

The Commission expects that an applicant would notify the Commission of any material changes to information submitted in support of a comparability determination (including, but not limited to, changes in the relevant supervisory or regulatory regime) as the Commission's comparability determination may no longer be valid.

Within four years of issuing any Substituted Compliance Determination, the Commission will reevaluate its initial determination to ascertain whether any changes should be made to its

---

[472] As previously noted, the Commission observes that under section 4s(j)(3) and (4) of the CEA and Commission regulation 23.606, a registered swap dealer or MSP must make all records required to be maintained in accordance with Commission regulation 1.31 available to the Commission promptly upon request to representatives of the Commission. The Commission reserves this right to access records held by registered swap dealers and MSPs, including those that are non-U.S. persons who may comply with the Dodd-Frank recordkeeping requirement through substituted compliance. See also 7 U.S.C. 6s(f); 17 CFR 23.203.

[473] In this regard, the Commission has started working with foreign regulators to prepare for such arrangements.

finding and shall reissue the relevant Commission action, conditionally or unconditionally, as it deems appropriate.

SDR Reporting and real-time public reporting would generally be eligible for substituted compliance, as outlined above, but only if the Commission has direct access to all of the reported swap data elements that are stored in a foreign trade repository. The Commission intends that direct access would generally include, at a minimum, real time, direct electronic access to the data and the absence of any legal impediments to the Commission's access to the data. Due to the technical nature of this inquiry, a comparability evaluation for SDR Reporting and real-time public reporting would generally entail a detailed comparison and technical analysis. The Commission notes that while direct access to swap data is a threshold matter to be addressed in a comparability evaluation, a more particularized analysis would generally be necessary to determine whether the data stored in a foreign trade repository provides for effective Commission use, in furtherance of the regulatory purposes of the Dodd-Frank Act.

Comparability determinations for SDR Reporting and real-time public reporting would generally take into account whether the Commission may effectively access and use data stored in foreign trade repositories, both in isolation and when compared to and aggregated with swap data from other foreign trade repositories, as well as registered SDRs. At a minimum, effective use would generally require that the data elements stored in foreign trade repositories are sufficient to permit comparison and aggregation, and that all transactions with comparable required data elements, otherwise required to be reported to a registered SDR, are available in the foreign trade repository.

### 5. **Conflicts Arising under Privacy and Blocking Laws**

Potential and actual conflicts between the Commission's regulations and the privacy and blocking laws of some non-U.S. jurisdictions may, in certain circumstances, limit or prohibit the disclosure of data that is required to be reported under the Dodd-Frank Act and implementing regulations.[474] For example, the Commission's part 45 and part 46 swap data reporting rules establish swap data recordkeeping and SDR reporting requirements applicable to reporting counterparties. Among other requirements, these rules prescribe certain reporting data fields for all swaps subject to the Commission's jurisdiction, including the identity of each counterparty to a swap. The privacy laws of some non-U.S. jurisdictions may, however, restrict or prohibit the disclosure by a reporting party or registrant of a non-reporting party's identity. In some jurisdictions, this privacy restriction may be overcome if the counterparty consents to the disclosure. In others, the restriction may take the form of a blocking statute which acts as an absolute prohibition to the disclosure of information, creating a direct conflict with the requirements of the Dodd-Frank Act.

The Commission recognizes that, notwithstanding the importance of swap data to its mandate under the Dodd-Frank Act, its regulations may be in conflict with the blocking, privacy, and/or secrecy laws of other jurisdictions. The Commission is mindful of the challenges presented by such circumstances and continues to work on a bilateral and multilateral basis with foreign regulators to address these issues. Where appropriate, the Commission may consider

---

[474] Section 727 of the Dodd Frank Act added to the CEA new section 2(a)(13)(G), which requires all swaps, whether cleared or uncleared, to be reported to registered SDRs. Section 21 of the CEA, added by section 728 of the Dodd Frank Act, directs the Commission to prescribe standards that specify the data elements for each swap that shall be collected and maintained by each registered SDR. Part 45 of the Commission's regulations establishes swap data recordkeeping and SDR reporting requirements; part 46 establishes similar requirements for pre-enactment and transition swaps (collectively, "historical swaps").

reasonable alternatives that allow the Commission to fulfill its mandate while respecting the regulatory interests of other jurisdictions. In that regard, where a real conflict of laws exists, the Commission strongly encourages regulators and registrants to consult directly with its staff.

### 6. Clearing

#### a. Clearing Venues

With respect to acceptable clearing venues, the Commission notes that section 2(h)(1) of the CEA provides that swaps subject to the clearing requirement must be submitted for clearing to a registered DCO or a DCO that is exempt from registration under the CEA.[475]

The Commission has previously recognized the role of foreign-based clearing organizations, including in the context of FBOTs. Specifically, in the final rules pertaining to Registration of Foreign Boards of Trade, the Commission required that an FBOT, in order to be registered, clear through a clearing organization that either is registered with the Commission as a DCO or observes the Principles for Financial Market Infrastructures ("PFMIs").[476] Other relevant requirements in the FBOT final rules include, among other things, that the clearing organization be in good regulatory standing in its home country.

In addition, in the final rules adopting the Inter-Affiliate Exemption, the Commission permitted eligible affiliated counterparties that are located in certain jurisdictions to satisfy a condition to electing the exemption (requiring counterparties to clear their swaps with third-parties) by clearing the swap through a registered DCO or a clearing organization that is subject

---

[475] As noted above, EMIR requires financial counterparties, including hedge funds, to clear OTC derivatives contracts subject to the clearing obligation through a CCP registered or recognized in accordance with EMIR.

[476] Registration of Foreign Boards of Trade, 76 FR 80674, 80681-82 (Dec. 23, 2011) (the PFMIs are the successor standards to the Recommendations for Central Counterparties ("RCCPs"), which were issued jointly by the Committee on Payment and Settlement Systems ("CPSS") and the Technical Committee of IOSCO).

to supervision by appropriate government authorities in the clearing organization's home country and that has been assessed to be in compliance with the PFMIs.[477]

More recently, in the final rulemaking adopting Core Principles and Other Requirements for Swap Execution Facilities, the Commission noted that under section 5b(h) of the CEA it has discretionary authority to exempt DCOs, conditionally or unconditionally, from the applicable DCO registration requirements.[478] Thus, the Commission has discretion to exempt from registration DCOs that, at a minimum, are subject to comparable and comprehensive supervision by another regulator. The Commission further noted that it had not yet exercised its discretionary authority to exempt DCOs from registration. The Commission explained that, notwithstanding that there were no exempt DCOs at that time, certain swaps executed on a SEF could be cleared at an exempt DCO, if and when the Commission determined to exercise its authority to exempt DCOs from applicable registration requirements, at which time the Commission would likely address, among other things, the conditions and limitations applicable to clearing swaps for customers subject to section 4d(f) of the CEA.[479]

The conditions that may have to be met for a clearing organization to be eligible to qualify as an exempt DCO could include, among other things: (i) the Commission having entered into an appropriate memorandum of understanding or similar arrangement with the

---

[477] Inter-Affiliate Exemption, 78 FR at 21784 (adopting 17 CFR 50.52(b)(4)(i)(E)).

[478] Specifically, section 5b(h) of the CEA provides that "[t]he Commission may exempt, conditionally or unconditionally, a derivatives clearing organization from registration under this section for the clearing of swaps if the Commission determines that the [DCO] is subject to comparable, comprehensive supervision and regulation by the Securities and Exchange Commission or the appropriate government authorities in the home country of the organization." 7 U.S.C. 7a-1(h). See also Core Principles and Other Requirements for Swap Execution Facilities, 78 FR 33476, 33591 (Jun. 4, 2013) (adopting 17 CFR 37.701) ("Part 37 SEF Regulations").

[479] Id. at 33534.

relevant foreign supervisor in the clearing organization's home country and (ii) the clearing organization having been assessed to be in compliance with the PFMIs.[480] The use of the PFMIs, an international standard that is substantially similar to the requirements for registered DCOs under part 39 of the Commission's regulations, would be consistent with the Commission's determination in the context of FBOTs.[481]

The Commission notes that its exemptive authority under CEA section 5b(h) is entirely discretionary. Accordingly, the Commission is not compelled to exempt any clearing organization from the DCO registration requirements, even upon a finding that a facility is "subject to comparable, comprehensive supervision and regulation" by another regulator.

**b. Foreign End-Users**

One of the conditions of the Inter-Affiliate Exemption, known as the "treatment of outward-facing swaps" condition, generally requires the clearing of swaps between affiliated counterparties and their unaffiliated counterparties.[482] Pursuant to Commission regulation 50.52(b)(4)(i)(C), eligible affiliate counterparties[483] can satisfy the treatment of outward-facing swaps condition by complying with the requirements of an exception or exemption under section 2(h)(7) of the CEA or part 50 of the Commission's regulations. Pursuant to section 2(h)(7) of the

---

[480] The PFMIs were developed with significant input and public comment from market participants, and benefited from broad participation of market regulators and prudential supervisors from multiple nations. The PFMIs were approved by both IOSCO's Technical Committee and the CPSS and published in April 2012.

[481] The Commission recognizes that certain DCOs registered with the Commission also may be authorized, licensed, or recognized by a foreign authority. The Commission continues to work on a bilateral basis with such non-US authorities with respect to issues of central counterparty supervision. The Commission also participates in multilateral discussions with its foreign counterparts through a number of international groups.

[482] See Clearing Exemption for Swaps Between Certain Affiliated Entities, 78 FR 21749; Commission regulation 50.52(b)(4)(i).

[483] As such term is defined in Commission regulation 50.52(a).

CEA, also known as the end-user exception, a counterparty to a swap that is subject to the clearing requirement[484] may elect not to clear the swap provided that such counterparty meets the conditions of section 2(h)(7)(A)(i)-(iii) of the CEA and the attendant regulations.[485]

For the purposes of the Inter-Affiliate Exemption, consistent with section 2(i), the Commission will permit a non-US person eligible affiliate counterparty to satisfy Commission regulation 50.52(b)(4)(i)(C) for swaps entered into with an unaffiliated non-US person that is not otherwise subject to the CEA ("Foreign End-User"), under certain circumstances. The Foreign End-User may elect the end-user exception as if the provisions of sections 2(h)(7)(A)(i) and (ii) of the CEA apply to the Foreign End-User and the Foreign End-User elects not to clear the swap.[486]

Accordingly, a Foreign End-User may elect not to clear a swap if (1) the Foreign End-User and non-US person eligible affiliate counterparty are not located in a foreign jurisdiction in which the Commission has determined that a comparable and comprehensive clearing requirement exists and that the exceptions and/or exemptions thereto are comparable and comprehensive;[487] (2) the Foreign End-User is not a financial entity as provided in section 2(h)(7)(A)(i) of the CEA; and (3) the Foreign End-User enters into the swap to hedge or mitigate

---

[484] See Clearing Requirement Determination, 77 FR 74284.

[485] See End-User Exception to the Clearing Requirement for Swaps, 77 FR 42560.

[486] If the Foreign End-User is an issuer of securities under, or required to file reports pursuant to, the Securities Exchange Act of 1934 ("SEC Filer"), then the Foreign End-User must obtain the approval to enter into uncleared swaps from an appropriate committee of the SEC Filer's board of directors (or governing body). See section 2(j) of the CEA. The Commission considers a counterparty controlled by an SEC Filer to be an SEC Filer itself for the purposes of the end-user exception. See 77 FR at 42570.

[487] In these situations, the counterparties should comply with laws of the foreign jurisdiction. See Commission regulations 50.52(b)(4)(i)(B) and (D).

commercial risk as provided in section 2(h)(7)(A)(ii) of the CEA.[488] In the interests of international comity, the Commission will not require the Foreign End-User to satisfy the provisions of section 2(h)(7)(A)(iii) of the CEA which require the end-user to notify the Commission how it generally meets its financial obligations associated with entering into non-cleared swaps.[489]

### G. Application of the Entity-Level and Transaction-Level Requirements to Swap Dealers and MSPs

This section sets forth the Commission's policy on application of the Entity-Level and Transaction-Level Requirements to swap dealers and MSPs, including when swaps generally would be eligible for substituted compliance.

#### 1. Comments

As noted in section E above, commenters generally supported the division of Dodd-Frank's swaps provisions (and Commission regulations thereunder) into Entity-Level and Transaction-Level Requirements for purposes of this Guidance. Certain of these commenters, however, made specific recommendations for reclassification of some of these requirements.[490]

In addition, some commenters addressed perceived disparities in the application of Transaction-Level Requirements to U.S. swap dealers, stating that transactions between U.S. swap dealers and non-U.S. counterparties should be eligible for substituted compliance for

---

[488] Foreign End-Users may look to Commission regulation 50.50(c) in order to determine whether a swap hedges or mitigates commercial risk.

[489] This guidance is only applicable to Commission regulation 50.52(b)(4)(i)(C); all other persons electing the End-User Exception must comply with the requirements of section 2(h)(7) of the CEA and Commission regulation 50.50.

[490] See section E, supra.

Transaction-Level Requirements so as to avoid putting U.S. swap dealers at a competitive disadvantage.[491]

Other commenters supported the Commission's proposed application of the Transaction-Level Requirements to the transactions of U.S. persons with non-U.S. persons.[492] One commenter stated that the Transaction-Level Requirements should apply to transactions by registered swap dealers and MSPs with U.S. persons.[493]

Several commenters objected to the applicability of certain Transaction-Level Requirements to transactions between two non-U.S. parties.[494] One commenter stated that Transaction-Level Requirements should never apply to swaps between counterparties that are both non-U.S. persons.[495]

With respect to external business conduct standards, one commenter stated that these standards should not apply to swaps between U.S. swap entities and non-U.S. persons because the Commission's supervisory interest in these transactions are less implicated when the

---

[491] See SIFMA (Aug. 27, 2012) at A36. See also State Street (Aug. 27, 2012) at 2; IIB (Aug. 27, 2012) at 27-28; The Clearing House (Aug. 27, 2012) at 4, 27.

[492] See Public Citizen (Aug. 27, 2012) at 13 (arguing that substituted compliance should not be permitted when the swap involves a U.S. counterparty and that Transaction-Level Requirements should be required for counterparties that are non-U.S. persons). See also IATP (Aug. 27, 2012) at 7-8 (recommending that Transaction-Level Requirements apply to transactions between non-U.S. swap dealers or MSPs and a U.S. person who is not a swap dealer or MSP).

[493] See IIAC (Aug. 27, 2012) at 8.

[494] See, e.g., Clearing House (Aug. 27, 2012) at 22-24 (arguing that pre- and post-trade transparency rules should not apply to interactions with non-U.S. customers); SIFMA (Aug. 27, 2012) at A37 (stating that real-time public reporting requirements would be inappropriate for swaps involving only non-U.S. counterparties).

[495] See Australian Bankers (Aug. 27, 2012) at 5, A8.

counterparty is a non-U.S. person.[496] Other commenters also stated that the external business conduct standards should not apply to transactions between two non-U.S. persons.[497]

2. **Commission Guidance**

The Commission has carefully considered the comments on Entity-Level and Transaction-Level Requirements. With regard to U.S. swap dealers and U.S. MSPs, the Commission's policy is that they generally would be expected to comply in full with all of the Entity-Level Requirements and Transaction-Level Requirements, without substituted compliance available. The Commission's policy would apply regardless of whether the counterparty to the swap is a U.S. person or non-U.S. person. This is consistent with the Commission's traditional approach to registered FCMs, wherein a person, once registered as an FCM, is subject to the full panoply of regulations applicable to such registrants, without distinctions based on whether the counterparties are U.S. or non-U.S. counterparties.

Further, the Commission believes that its cross-border policy and interpretation with respect to U.S. swap dealers and MSPs must be informed by the purposes of the Dodd-Frank Act. As discussed earlier, the Dodd-Frank Act was enacted to reduce systemic risk, increase transparency, and promote market integrity within the financial system by, among other things, providing for the comprehensive regulation of swap dealers and MSPs. In doing so, Congress understood the highly integrated nature of the global swaps business, with regard to both

---

[496] See SIFMA (Aug. 27, 2012) at A38.

[497] See Australian Bankers (Aug. 27, 2012) at 4, A10. See also IIAC (Aug. 27, 2012) at 8 (agreeing that external business conduct standards should not apply to swaps between non-U.S. swap dealers and MSPs and non-U.S. counterparties (whether or not guaranteed by a U.S. person)).

individual firms and the market at large, and that risk to U.S. firms and in turn, U.S. financial markets may arise anywhere in the world.

In view of the policy goals underlying the Dodd-Frank Act swaps reforms, the Commission's view is that U.S. swap dealers and MSPs should be fully subject to the robust oversight contemplated by the Dodd-Frank Act, without regard to whether their counterparty is a U.S. or non-U.S person. These firms are conducting their swap dealing business within the territory of the United States. That some of their business may be directed to foreign clients does not diminish the Commission's obligation to ensure that swaps between U.S. swap dealers and MSPs and their counterparties are subject to Dodd-Frank's financial safeguards and transparency requirements, to the fullest extent. Therefore, in the Commission's view, substituted compliance is incompatible with the Commission's ability to effectively discharge its statutory responsibilities.

For substantially the same reasons, the Commission believes that full U.S. regulation of U.S. swap dealers and MSPs, even when they transact swaps with non-U.S. counterparties, is a reasonable exercise of U.S. jurisdiction under the principles of foreign relations law. Among the factors supporting this exercise of U.S. jurisdiction are the links between the U.S. swap dealers and MSPs and their swap activities to U.S. commerce, and the generally accepted importance of regulating the activities of these entities both to the United States and the international financial system.[498] In addition, having an agency of the U.S. government serve as the primary regulator of U.S. entities is generally consistent with normal expectations and with traditions of the

---

[498] See Restatement §§ 403(2)(a)-(c), 403(2)(e).

international system.[499] To the extent that other countries have an interest in regulating transactions with their nationals, the Commission notes that the U.S. regulatory scheme for swap dealers and MSPs does not preclude other countries from imposing their regulations if they consider it necessary for transactions affecting their interests.[500] As discussed below, the Commission will work with other regulators to avoid, and resolve where necessary, direct conflicts, as well as to reduce unnecessary burdens. The Commission observes that very few conflicts between the foreign regimes and Dodd-Frank Act requirements have been identified as part of many multilateral and bilateral consultations between staff of the CFTC and their foreign counterparts. For these purposes, conflict means that actions required for compliance under one jurisdiction's law are prohibited under the other jurisdiction's law, or compliance with the regulations of both jurisdictions is otherwise impossible.

With regard to non-U.S. swap dealers or MSPs (including those that are affiliates of a U.S. person), the Commission's policy is that these firms should be subject to all of the Entity-Level Requirements, but under certain circumstances substituted compliance should be available (except with regard to Large Trader Reporting). The Commission's policy with regard to the application of Transaction-Level Requirements to non-U.S. swap dealers or MSPs, and the availability of substituted compliance, depends in part on the type of counterparty to the swap transaction.

The foreign branch of a U.S. bank that is a swap dealer or MSP is expected to comply in full with the Entity-Level Requirements, without substituted compliance available, because it is

---

[499] See Restatement §§ 403(2)(d), 403(2)(f).

[500] See Restatement § 403(2)(g).

not a separate legal entity.[501] In some circumstances the Commission's policy is that a foreign branch of a U.S. swap dealer or MSP would be expected to comply in full with Category A Transaction-Level Requirements where its counterparty is a U.S. person. However, as further explained below, substituted compliance would generally be available to a foreign branch of a U.S. bank with regard to Category A Transaction-Level Requirements where the counterparty to a swap transaction is a non-U.S. person or a foreign branch of a U.S. bank that is a swap dealer or MSP. In addition, the Commission's policy with regard to the application of the Category B Transaction-Level Requirements is explained below.

Below, the Commission describes its policies regarding how Entity-Level and Transaction-Level Requirements should apply to both U.S. and non-U.S. swap dealers and MSPs, and to foreign branches of a U.S. banks that are swap dealers and MSPs, as well as the circumstances under which substituted compliance would be available.

### 3. Application of the Entity-Level Requirements to Swap Dealers and MSPs

In this section, the Commission discusses its policy regarding the application of the Entity-Level Requirements to swap dealers and MSPs in cross-border transactions under its interpretation of 2(i), as well as the circumstances under which such swaps would be eligible for substituted compliance.

Section a discusses the Commission's view on the application of Entity-Level Requirements to swaps with U.S. swap dealers and U.S. MSPs, including subsidiaries and

---

[501] The types of offices the Commission would consider to be a "foreign branch" of a U.S. bank, and the circumstances in which a swap is with such foreign branch, are discussed further in section C, supra.

affiliates of non-U.S. persons, and foreign branches of U.S. swap dealers or U.S. MSPs, under CEA section 2(i).

Section b discusses the Commission's view on the application of Entity-Level Requirements to swaps with non-U.S. swaps dealers and MSPs, including subsidiaries and affiliates of U.S. persons.

The Commission's policy on application of the Entity-Level Requirements to swap dealers and MSPs, as well as substituted compliance, is discussed below and summarized in Appendix C to this Guidance, which should be read in conjunction with the rest of the Guidance.

**a. To U.S. Swap Dealers and MSPs**

As explained above, U.S. swap dealers and U.S. MSPs generally would be expected to comply in full with all of the Entity-Level Requirements, without substituted compliance available. The Commission's policy generally would apply regardless of whether the counterparty to the swap is a U.S. person or non-U.S. person.

Because under this Guidance the term "U.S. person" includes corporations, partnerships, limited liability companies, and other legal entities (as discussed above), the foregoing interpretation also applies to affiliates of non-U.S. persons that are U.S. swap dealers or U.S. MSPs. It also applies to U.S. banks that are swap dealers or MSPs when the swap is with their foreign branch. In this case, because a foreign branch of a U.S. bank is an integral part of the U.S. principal entity and has no separate legal existence, and the U.S. principal bank is the entity that registers as a swap dealer or MSP, under the Commission's interpretation of CEA section 2(i), the U.S. bank (principal entity) would be the party ultimately responsible for compliance with the Entity-Level Requirements for the entire legal entity.

### b. To Non-U.S. Swap Dealers and MSPs

Consistent with CEA section 2(i), the Commission would expect non-U.S. swap dealers and non-U.S. MSPs to comply with all of the Entity-Level Requirements. This policy also applies to foreign affiliates of a U.S. person that are independently required to register as swap dealers or MSPs and to comply with applicable Dodd-Frank Act requirements.

However, in considering whether substituted compliance is available to a non-U.S. swap dealer or MSP with respect to particular Entity-Level Requirements, the Commission would consider it relevant whether the Entity-Level Requirement is classified in the First Category or Second Category (and with respect to the Second Category, whether the counterparty is a U.S. person).

The Commission recognizes that non-U.S swap dealers or MSPs are likely to have their principal swap business in their home jurisdiction, and in consideration of international comity principles, is interpreting CEA section 2(i) such that such non-U.S swap dealers or MSPs generally would be eligible for substituted compliance with regard to Entity-Level Requirements in the First Category (i.e., capital adequacy, chief compliance officer, risk management, and swap data recordkeeping, except certain aspects of swap data recordkeeping relating to complaints and marketing and sales materials[502]).[503]

---

[502] See 17 CFR 23.201(b)(3), (4).

[503] As noted in the Proposed Guidance, the Commission anticipates that non-U.S. swap dealers and non-U.S. MSPs will likely have their principal swap business in their home jurisdiction. In these circumstances, the Commission notes that the home regulator would have a primary relationship to the swap dealer or MSP, which, coupled with the firm-wide focus of the Entity-Level Requirements, supports generally making the non-U.S. registrant eligible for substituted compliance. Therefore, consistent with the Proposed Guidance, the Commission believes that it is appropriate to make non-U.S. swap dealers and MSPs eligible for substituted compliance with respect to Entity-Level Requirements in the First Category where the non-U.S. swap dealers or non-U.S. MSPs are subject to comparable regulation in their home jurisdiction.

With respect to Entity-Level Requirements in the First Category, as noted by commenters on the Proposed Guidance, an affiliate of a U.S. SD that is guaranteed by such U.S. SD (or guaranteed by a U.S.-based parent or other affiliate of such SD) may under certain circumstances be required to register as a SD based on its swap dealing activity solely with non-U.S. persons, including those non-U.S. persons that are neither guaranteed affiliates or affiliate conduits of U.S. persons. Commenters have represented that some corporate groups may be required to register many of these guaranteed affiliates as SDs, even though such affiliates provide swap dealing services only to non-U.S. markets, and that many of such guaranteed affiliates exist only because the law of the local jurisdiction requires that a subsidiary be incorporated in the jurisdiction in order to enter into swaps with counterparties located in such jurisdiction. The Commission recognizes that certain structural conditions required to comply with the regulatory obligations of SDs may be burdensome for a corporate group with many of these guaranteed affiliates due to the requirement that such obligations be complied with at the individual entity level (e.g., Commission regulations §§ 3.3 (Chief compliance officer), 23.600 (Risk Management Program for swap dealers and major swap participants), 23.601 (Monitoring of position limits), 23.602 (Diligent supervision), 23.603 (Business continuity and disaster recovery), and 23.606 (General information: availability for disclosure and inspection)).

Specifically, the Commission notes that Commission regulations §§ 3.3 (Chief compliance officer), 23.600 (Risk Management Program for swap dealers and major swap participants), 23.601 (Monitoring of position limits), 23.602 (Diligent supervision), 23.603 (Business continuity and disaster recovery), and 23.606 (General information: availability for disclosure and inspection) mandate that each SD in a corporate group under common control individually establish policies, procedures, governance structures, reporting lines, operational

units, and systems specified in the rules. Thus, the Commission would consider relief, subject to appropriate conditions and restrictions to be determined, that would permit guaranteed affiliates in a corporate group under common control that do not enter into swaps with U.S. persons to comply with such regulations by establishing consolidated policies, procedures, governance structures, reporting lines, operational units, and systems, thereby increasing operational efficiencies and lessening the economic burden on these groups with respect to their guaranteed affiliates that do not directly face U.S. persons when engaging in swaps activities.[504] The Commission notes, however, that any such relief would require a consolidated program to manage the risks of the included guaranteed affiliates on an individual, rather than a net, basis.

The Commission encourages interested parties to contact the Director of the Division of Swap Dealer and Intermediary Oversight to discuss the necessary conditions and restrictions of appropriate relief.

The Commission clarifies that, in the interest of international comity and for the purpose of permitting efficiencies in compliance programs, it would remain open to considering (or directing its staff to consider) relief, subject to appropriate conditions and restrictions to be determined, that would permit guaranteed affiliates in a corporate group under common control (that do not enter into swaps with U.S. persons or U.S. guaranteed affiliates or affiliate conduits of U.S. persons) to comply with certain of such regulations on a consolidated or group basis. The Commission notes, however, that any such relief would require a consolidated program to manage the risks of the included guaranteed affiliates on an individual, rather than a net, basis. With respect to one of the Entity-Level Requirements in the Second Category, SDR Reporting

---

[504] "Swaps activities" are defined in Commission regulation 23.600(a)(7).

(i.e., SDR Reporting and swap data recordkeeping related to complaints and marketing and sales materials),[505] the Commission interprets CEA section 2(i) such that swap dealers or MSPs that are not U.S. persons generally would be eligible for substituted compliance only with respect to swaps where the counterparty is a non-U.S. person that is not a guaranteed or conduit affiliate.

With respect to the other Entity-Level Requirement in the Second Category (i.e., swap data recordkeeping related to complaints and marketing and sales materials),[506] the Commission interprets CEA section 2(i) such that swap dealers or MSPs that are not U.S. persons generally would be eligible for substituted compliance only with respect to swaps where the counterparty is a non-U.S. person. However, as explained below, with respect to Large Trader Reporting, the Commission's policy would not recognize substituted compliance in place of compliance with Large Trader Reporting.

Specifically, with respect to SDR Reporting, the Commission interprets CEA section 2(i) such that substituted compliance may be available to non-U.S. swap dealers and non-U.S. MSPs (whether or not such swap dealers or MSPs are affiliates of or are guaranteed by U.S. persons) for swaps with non-U.S. counterparties, provided that the Commission has direct access (including electronic access) to the relevant swap data that is stored at the foreign trade repository. The Commission believes that this ensures that the Commission will have access to information that is critical to its oversight of these entities even where substituted compliance with regard to SDR Reporting would be applicable under this Guidance.[507] However, the

---

[505] See 17 CFR 23.201(b)(3), (4).

[506] See id.

[507] As the Commission noted in the Proposed Guidance, data reported to SDRs is critical to ensure that the Commission has a comprehensive and accurate picture of swap dealers and MSPs that are its registrants, including

Commission interprets section 2(i) as applied to these requirements such that substituted compliance generally would not be available for non-U.S. swap dealers and non-U.S. MSPs (whether or not such swap dealers or MSPs are guaranteed by U.S. persons) with respect to swaps with U.S. counterparties. The Commission believes that in general, application of these requirements, without eligibility for substituted compliance, is appropriate given its strong supervisory interest in a swap between a registered swap dealer or MSP and a U.S. counterparty.

However, with regard to the SDR reporting requirements, for the future, the Commission has agreed to continue to work collaboratively and to consider any unforeseen implementation effects that might arise in the application of our respective rules. The Commission will continue discussions with other international partners with a view to establishing a more generalized system that would allow, on the basis of these countries' implementation of the G-20 commitments, an extension of the treatment the EU and the CFTC will grant to each other.

With regard to certain aspects of swap data recordkeeping that relate to complaints and marketing and sales materials, the Commission interprets CEA section 2(i) such that non-U.S. swap dealers or non-U.S. MSPs generally would be eligible for substituted compliance with respect to swaps with non-U.S. counterparties.[508]

---

the gross and net counterparty exposures of swaps of all swap dealers and MSPs, to the greatest extent possible. Therefore, the Commission's view is that non-U.S. swap dealers and non-U.S. MSPs generally should be expected to report all of their swaps to a registered SDR. At the same time, the Commission recognized the interests of foreign jurisdictions with respect to swaps between a non-U.S. swap dealer or non-U.S. MSP with a non-U.S. counterparty. Therefore, the Commission would interpret section 2(i) so that swaps between non-U.S. swap dealers or MSPs with non-U.S. counterparties generally are eligible for substituted compliance with regard to SDR Reporting, but only if the Commission has direct access to all of the reported swap data elements that are stored at a foreign trade repository.

[508] In the Proposed Guidance, the Commission included all of the swap data recordkeeping requirements of regulations 23.201 and 23.203 in the proposed first subcategory of Entity-Level Requirements. 77 FR at 41225. In this Guidance, swap data recordkeeping related to complaints and marketing and sales materials under regulations 23.201(b)(3) and 23.201(b)(4), respectively, are being moved from the First Category to the Second Category

To the extent that swap data reported to a foreign trade repository would include data regarding the physical commodity swaps covered by Large Trader Reporting, the Commission – even if provided with direct access to such data – would still likely be required to convert it to "futures equivalent" positional data in order to render it comparable to the data obtained through Large Trader Reporting, which contemplates conversion by the entity required to report data to the Commission.[509] Given that Large Trader Reporting is intended to enable the Commission, in a prompt and efficient manner, to identify significant traders in the covered physical commodity swaps and to collect data on their trading activity in order to reconstruct market events, the time and resources expended by the Commission in conversion could significantly impede its market surveillance efforts.

The Commission notes further that its interpretation of CEA section 2(i) to permit substituted compliance with comparable and comprehensive regimes in certain circumstances recognizes the interests of foreign jurisdictions with respect to swaps between non-U.S. persons. Large Trader Reporting, however, reflects a very specific interest of the Commission in conducting effective surveillance of markets in swaps that have been determined to be economically equivalent to certain U.S.-listed physical commodity futures contracts. In light of this specific Commission interest – which is reflected in the particularized scope and

---

because the Commission does not believe that substituted compliance generally should be available for requirements relating to complaints and marketing and sales materials where the counterparty is a U.S. person. This policy pertains equally to swaps with foreign affiliates of a U.S. person that are required to independently register as swap dealers and to comply with applicable Entity-Level Requirements.

[509] Large Trader Reporting provides the Commission with data regarding large positions in swaps that are linked, directly or indirectly, to a discrete list of U.S.-listed physical commodity futures contracts, in order to enable the Commission to implement and conduct effective surveillance of these economically equivalent swaps and futures. To facilitate surveillance efforts and the monitoring of trading across the swaps and futures markets, swaps positions must be converted to equivalent positions of the related U.S. futures contract ("futures equivalents") for reporting purposes; reportable thresholds are also defined in terms of "futures equivalents."

methodology of Large Trader Reporting – and in light of the anticipated impediments to obtaining directly comparable positional data through any foreign swap data reporting regime, the Commission's policy would not recognize substituted compliance in place of compliance with Large Trader Reporting.

#### 4. Application of the "Category A" Transaction-Level Requirements to Swap Dealers and MSPs

This section discusses the Commission's guidance on the application of the Category A Transaction Level Requirements to the parties to a swap where one of the parties is a registered swap dealer or MSP,[510] including when substituted compliance may be available to various types of counterparties.

As noted above, the Category A Transaction Level Requirements include: (1) required clearing and swap processing; (2) margining and segregation requirements for uncleared swaps; (3) trade execution; (4); swap trading relationship documentation; (5) portfolio reconciliation and compression; (6) real-time public reporting; (7) trade confirmation; and (8) daily trading records.[511]

The Commission's policy on application of the Category A Transaction-Level Requirements is summarized in Appendix D to this Guidance, which should be read in conjunction with the rest of the Guidance.

---

[510] Some of the Transaction-Level and Entity-Level Requirements also are applicable to market participants that are not swap dealers or MSPs, which are referred to herein as non-registrants. See section H, infra, for a discussion of the Commission's interpretation of how these requirements would apply to non-registrants under CEA section 2(i).

[511] The categorization of Transaction-Level Requirements into Categories A and B is discussed in section E, supra. See Appendix B for a descriptive list of the Category A and Category B requirements and Appendix D for a table summarizing the application of the Category A Transaction-Level Requirements to Swap Dealers and MSPs.

### a. Swaps with U.S. Swap Dealers and MSPs

As explained above, where one of the counterparties to a swap is a U.S. swap dealer or U.S. MSP, under the Commission's interpretation of CEA section 2(i), the Commission would generally expect the parties to the swap to comply with Category A Transaction-Level Requirements with respect to the transaction, without regard to whether the other counterparty to the swap is a U.S. person or a non-U.S. person.

Because the Commission interprets section 2(i) so that the term "U.S. person" would include any legal entity organized or incorporated under the laws of the United States or having its principal place of business in the United States, this interpretation also would apply where one of the parties to the swap is a U.S. swap dealer or U.S. MSP that is an affiliate of a non-U.S. person.[512] In addition, because the Commission considers a foreign branch of a U.S. person to be a part of the U.S. person, the foregoing interpretation also applies to swaps with foreign branches of a U.S. bank that is a swap dealer or MSP (although in some circumstances substituted compliance may be available as explained below).

Further, as explained above, with regard to substituted compliance, where one of the counterparties to a swap is a U.S. swap dealer or U.S. MSP (including those that are affiliates of a non-U.S. person), other than a foreign branch of a U.S. bank that is a swap dealer or MSP, the Commission's policy is that substituted compliance generally would not be available for the Category A Transaction-Level Requirements, without regard to whether the other counterparty is a U.S. person or a non-U.S. person. The Commission has a strong supervisory interest in

---

[512] See the Proposed Guidance, 77 FR at 41218.

ensuring that the Category A Transaction-Level Requirements apply to swaps with a U.S. swap dealer or MSP.[513]

Similarly, under the Commission's interpretation of 2(i), where a swap is between a foreign branch of a U.S. bank that is a swap dealer or MSP, on the one hand, and a U.S. Person on the other, the Commission's policy is that substituted compliance generally would not be available with respect to the Category A Transaction-Level Requirements. In this case, the Commission also has a strong supervisory interest in ensuring that the Category A Transaction-Level Requirements fully apply to the transaction because it views the swap transaction as being between two U.S. persons. The Commission believes that this approach is appropriate in light of the Commission's strong supervisory interests in entities that are part or an extension of a U.S. swap dealer or U.S. MSP.

However, where a swap is between two foreign branches of U.S. banks that are both swap dealers or MSPs, the Commission believes that the interests of foreign regulators in applying their transaction-level requirements to a swap taking place in their jurisdiction, together with the fact that foreign branches of U.S. swap dealers or U.S. MSPs are subject generally to direct or indirect oversight by U.S. regulators, weigh in favor of allowing substituted compliance with comparable and comprehensive foreign regulatory requirements (to the extent applicable).

---

[513] Consistent with the foregoing rationale, the Commission takes the view that a U.S. branch of a non-U.S. swap dealer or MSP would be subject to Transaction-Level requirements, without substituted compliance available. As discussed above, a branch does not have a separate legal identity apart from its principal entity. Therefore, the Commission considers a U.S. branch of a non-U.S. swap dealer or non-U.S. MSP to be a non-U.S. person (just as the Commission considers a foreign branch of a U.S. person to be a U.S. person). Nevertheless, the Commission also recognizes its strong supervisory interest in regulating the dealing activities that occur with the United States, irrespective of the counterparty (just as the Commission allows for substituted compliance for foreign branches in certain instances to take into account the strong supervisory interest of local regulators).

In addition, where a swap is between the foreign branch of a U.S. bank that is a swap dealer or MSP, on the one hand, and a non-U.S. person on the other (regardless of whether the non-U.S. person is a guaranteed or conduit affiliate), as a policy matter, the Commission believes that substituted compliance should be available (if otherwise applicable). In this case, even though the Commission considers the foreign branch of a U.S. person to be a U.S. person, the Commission believes that the interests of foreign regulators in applying their transaction-level requirements to a swap taking place in their jurisdiction, together with the fact that foreign branches of U.S. swap dealers or U.S. MSPs are subject generally to direct or indirect oversight by U.S. regulators because they are part of a U.S. person, may weigh in favor of allowing substituted compliance with comparable and comprehensive foreign regulatory requirements (to the extent applicable) where the counterparty to the foreign branch is a non-U.S. person.

In a modification to the Proposed Guidance, where a swap between the foreign branch of a U.S. swap dealer or U.S. MSP and a non-U.S. person (that is not a guaranteed or conduit affiliate) takes place in a foreign jurisdiction other than Australia, Canada, the European Union, Hong Kong, Japan, or Switzerland,[514] the Commission's policy is to interpret CEA section 2(i) so that counterparties may comply with the transaction-level requirements applicable to entities domiciled or doing business in the foreign jurisdiction where the foreign branch is located, rather than the Transaction-Level Requirements that would otherwise be applicable, if two elements are present. First, the aggregate notional value (expressed in U.S. dollars and measured on a quarterly basis) of the swaps of all U.S. swap dealer's foreign branches in foreign jurisdictions

[514] Market participants or regulators in all of these jurisdictions have submitted requests for Substituted Compliance Determinations.

other than Australia, Canada, the European Union, Hong Kong, Japan, or Switzerland does not exceed five percent of the aggregate notional value (expressed in U.S. dollars and measured on a quarterly basis) of all of the swaps of the U.S. swap dealer. Second, the U.S. person maintains records with supporting information to verify that the first element is present, as well as to identify, define, and address any significant risk that may arise from the non-application of the Transaction-Level Requirements. The Commission believes this policy is appropriate because U.S. swap dealers' dealing activities through branches or agencies in jurisdictions other than the six jurisdictions referenced above, though not significant in many cases, may be nevertheless an integral element of their global business. The Commission notes that this exception is not available in the six jurisdictions referenced above because the Commission has received, or expects to receive in the near term, a request for substituted compliance determinations for transactions in these jurisdictions.

Although the foreign branch of a U.S. registrant would not register separately as a swap dealer or MSP, the Commission interprets 2(i) in a manner that would permit the U.S. registrant to task its foreign branch to fulfill its regulatory obligations with respect to the Category A Transaction-Level Requirements. The Commission would generally consider compliance by the foreign branch to constitute compliance with these Transaction-Level Requirements. However, under the Commission's interpretation of 2(i), the U.S. person (principal entity) would remain responsible for compliance with the Category A Transaction-Level Requirements.

**b. Swaps with Non-U.S. Swap Dealers and Non-U.S. MSPs**

Under the Commission's interpretation of CEA section 2(i), where a swap is between a non-U.S. swap dealer or non-U.S. MSP (including an affiliate of a U.S. person), on the one hand, and a U.S. person (other than a foreign branch of a U.S. swap dealer or MSP), on the other, the

Commission would generally expect the parties to comply with Category A Transaction-Level Requirements with respect to the transaction.[515]

The Commission notes, however, that where a swap is executed anonymously between any non-U.S. person, whether a swap dealer or an MSP, and a U.S. person (other than a foreign branch of a U.S. swap dealer or MSP) on a registered DCM or SEF and cleared, the non-U.S. person will generally be considered to have satisfied each of the eight Category A Transaction-Level Requirements that apply to such a swap transaction as a consequence of being so executed on a DCM or SEF. Thus, neither the non-U.S. person (nor its U.S. person counterparty) will need to take any further steps to comply with the Category A Transaction-Level Requirements in connection with such a transaction.[516]

In making this determination, the Commission observes that where a cleared swap transaction is executed anonymously on a registered DCM or SEF, certain independent requirements that apply to DCM and SEF transactions generally, pursuant to the CEA or the Commission's regulations, will ensure that four of the eight Category A Transaction-Level Requirements will be met for such transactions – required clearing and swap processing,[517] trade

---

[515] Under the Commission's futures regulatory regime, any person located outside the U.S. that seeks to serve as an intermediary to U.S. persons trading on a U.S. designated contract market or in foreign futures and option contracts is required to register in the appropriate category and comply with related regulations, absent the availability of an exemption from registration (e.g., relief pursuant to Commission regulation 30.10 in the foreign futures and option context)." See, e.g., Commission regulation 30.4.

[516] However, non-U.S. SDs and MSPs must satisfy the daily trading record requirement found in Commission regulation 23.202(a)(1).

[517] Pursuant to Commission regulations 37.702 and 38.601, each SEF and DCM must coordinate with each DCO to which it submits transactions for clearing in the development of rules and procedures to facilitate prompt and efficient transaction processing to meet the requirements of Commission regulation 39.12(b)(7). Commission regulation 39.12(b)(7)(ii) requires a DCO to accept or reject swaps executed on a SEF or DCM for clearing "as quickly after execution as would be technologically practicable if fully automated systems were used." See also 17 CFR 23.506(a); 39.12(b)(7)(iii); Final Customer Documentation Rules, 77 FR at 21306-10. As stated in the Final

execution,[518] real-time public reporting,[519] and trade confirmation.[520]

For a combination of reasons, the Commission also believes that the four remaining Transaction-Level Requirements do not, or should not, apply to cleared, anonymous DCM or SEF transactions. So, for instance, the fact that the DCM or SEF swap transaction will be cleared, obviates the need for margining or segregation requirements applicable to uncleared swaps. Two other Category A Transaction-Level Requirements – swap trading relationship documentation and portfolio reconciliation and compression – would not apply because the Commission regulations that establish those requirements make clear that they do not apply to cleared DCM or SEF transaction.[521] The last requirement – the daily trading records

---

Customer Documentation Rules, these rules, taken as a whole, "require SEFs, DCMs, swap dealers, MSPs, and DCOs to coordinate in order to facilitate real time acceptance or rejection of trades for clearing." Id. at 21296.

[518] CEA section 2(h)(8)(A) provides that transactions in swaps subject to the trade execution mandate must be executed on a registered DCM or SEF, or a SEF that has been exempted from registration. The Commission clarifies that the trading mandate under CEA section 2(h)(8)(A) is satisfied by trading on a registered DCM or SEF or a SEF that has been exempted from registration.

[519] Parties that execute a swap transaction on a DCM or SEF meet their real-time public reporting obligations by operation of a set of Commission regulations that essentially delegate the obligations to the DCM or SEF on which the transaction was executed, and the SDR to which the DCM or SEF reports the transaction. Specifically, Commission regulation 43.3(a)(2) provides that a party to a publicly reportable swap transaction satisfies its real-time reporting obligations by executing a publicly reportable swap transaction on or pursuant to the rules of a registered SEF or DCM. In turn, Commission regulation 43.3(b)(1) requires a SEF or DCM to transmit swap transaction and pricing data to a registered SDR, as soon as technically practicable after the publicly reportable swap transaction has been executed on or pursuant to the rules of such trading platform or facility. Finally, Commission regulation 43.3(b)(2) requires a registered SDR to ensure that swap transaction and pricing data is publicly disseminated, as soon as technologically practicable after such data is received from a registered SEF or DCM.

[520] See Commission regulation 23.501(a)(4)(i) ("Any swap transaction executed on a swap execution facility or designated contract market shall be deemed to satisfy the requirements of this section, provided that the rules of the swap execution facility or designated contract market establish that confirmation of all terms of the transactions shall take place at the same time as execution"); 37.6(b); Part 37 SEF Regulations, 78 FR at 33585 ("A swap execution facility shall provide each counterparty to a transaction that is entered on or pursuant to the rules of the swap execution facility with a written record of all of the terms of the transaction which shall legally supersede any previous agreement and serve as confirmation of the transaction. The confirmation of all terms shall take place at the same time as execution …").

[521] See 17 CFR 23.504(a)(1) ("The requirements of this section [swap trading relationship documentation] shall not apply to … swaps executed on a board of trade designated as a contract market under section 5 of the Act or to swaps executed anonymously on a swap execution facility under section 5h of the Act, provided that such swaps are

requirement[522] – would only be applicable to the non-U.S. swap dealer and only with regard to pre-trade execution swaps. However, because the non-U.S. swap dealer will have no information about its counterparty where the swap is executed anonymously, the Commission is of the view that, as a matter of international comity, CEA section 2(i) should not be interpreted to apply all of the daily trading records requirements to such a swap.[523]

In addition, the Commission is interpreting CEA section 2(i) such that, where a swap between a non-U.S. person, regardless of its swap dealer or MSP status, and a U.S. person is executed anonymously on an FBOT registered with the Commission pursuant to part 48 and cleared the non-U.S. person will generally be considered to have satisfied the Category A Transaction-Level Requirements that pertain to such a swap transaction. Some of the requirements will be satisfied by requirements levied by regulation on the FBOT and some will be satisfied because a registered FBOT is analogous to a DCM and is subject to comprehensive supervision and regulation in its home country that is comparable to that exercised over a DCM by the Commission. Thus, neither the non-U.S. person (nor its U.S. person counterparty) will need to take any further steps to satisfy the applicable Category A Transaction-Level Requirements in connection with such a transaction.[524]

---

cleared by a derivatives clearing organization … "); 23.502(d) ("Nothing in this section [portfolio reconciliation] shall apply to a swap that is cleared by a derivatives clearing organization"); 23.503(c) ("Nothing in this section [portfolio compression] shall apply to a swap that is cleared by a derivatives clearing organization.").

[522] See 17 CRR 23.202.

[523] The Commission is of the view that CEA section 2(i) should not be interpreted to apply the daily trading records requirements, with the exception of those found in Commission regulation 23.202(a)(1).

[524] However, a non-U.S. swap dealer or non-U.S. MSP must satisfy the daily trading record requirement found in Commission regulation 23.202(a)(1).

In making this determination, the Commission observes that where a cleared swap transaction is executed anonymously on a registered FBOT, the FBOT, similar to a DCM, based on certain independent requirements that apply to DCM transactions generally pursuant to the CEA or the Commission's regulations, will ensure that two of the eight Category A Transaction-Level Requirements will be satisfied for such transactions: required clearing and swap processing[525] and trade execution.[526] The Commission notes that while the real-time reporting requirement will be satisfied for cleared swaps executed anonymously on a DCM by operation of the Commission's real-time reporting regulations, absent further affirmative actions by an FBOT, the real-time public reporting requirements will not be satisfied through FBOT execution alone.[527]

For a combination of reasons, including the fact that the swap will be cleared, the Commission also is of the view that the remaining Transaction-Level Requirements do not apply to such transactions executed on a registered FBOT. For instance, the fact that the swap will be cleared, as required by regulation 48.7(c)(1)(ii), renders inapplicable the margining or segregation requirements for uncleared swaps. As the Commission observed above with respect

---

[525] As discussed above, pursuant to Commission regulation 48.7(c)(1)(ii), all contracts, including swaps, made available in the U.S. by a registered FBOT must be cleared. The clearing organization must be either a DCO or must observe international clearing standards: the RCCP or the successor standards, PFMI.

[526] See discussion of clearing at section IV.F.6, supra. The Commission clarifies that the trading mandate under CEA section 2(h)(8)(A) is satisfied by trading on a registered FBOT.

[527] Pursuant to Commission regulation 48.8(a)(9), the registered FBOT must ensure that all transaction data relating to each swap transaction, including price and volume, are reported as soon as technologically practicable after execution of the swap transaction to a SDR that is either registered with the Commission or has an information sharing arrangement with the Commission. While Commission regulation 43(b)(2) requires that an SDR ensure that swap transaction and pricing data is publicly disseminated as soon as technologically practicable after such data is received from a registered SEF, DCM or reporting party, it does not specifically require public dissemination of swap transaction and pricing data from the FBOT. Therefore, in order for the FBOT to ensure that the real-time public reporting requirement is satisfied, the FBOT must either report the data to the public itself or enter into an arrangement with the SDR to which the data are reported pursuant to which the SDR agrees to publicly disseminate the data as soon as technologically practicable.

to swaps executed anonymously on DCMs, certain of the other Category A Transaction-Level Requirements would not apply to the swap. Consistent with this determination, three of the other Category A Transaction-Level Requirements – swap trading relationship documentation, portfolio reconciliation and compression and trade confirmation – would not apply to the swap executed on a registered FBOT because the underlying Commission regulations themselves do not apply those requirements to cleared DCM or SEF transactions. The last requirement – the daily trading records requirement – would only be applicable to the non-U.S. swap dealer and only with regard to pre-trade execution swaps. However, because the non-U.S. swap dealer will have no information about its counterparty where the swap is executed anonymously on a registered FBOT, the Commission is of the view that, as a matter of international comity, CEA section 2(i) should be interpreted such that certain of the daily trading records requirements also would not apply to the swap.[528]

In addition, for the reasons discussed in the next two sections, where a swap is between a non-U.S. swap dealer or non-U.S. MSP, on the one hand, and a non-U.S. person that is a guaranteed or conduit affiliate, on the other, under the Commission's interpretation of 2(i), the Commission would generally expect the parties to comply with the Category A Transaction-Level Requirements.[529]

However, where a swap is between a non-U.S. swap dealer or non-U.S. MSP (including an affiliate of a U.S. person), on the one hand, and a non-U.S. person that is not a guaranteed or

---

[528] The Commission is of the view that CEA section 2(i) should not be interpreted to apply the daily trading records requirements, with the exception of those found in Commission regulation 23.202(a)(1).

[529] Where one of the parties to the swap is a conduit affiliate, the Commission would generally expect the parties to the swap only to comply with (to the extent that the Inter-Affiliate Exemption is elected), the conditions of the Inter-Affiliate Exemption, including the treatment of outward-facing swaps condition in Commission regulation 50.52(b)(4)(i). In addition, the part 43 real-time reporting requirements must be satisfied.

conduit affiliate, on the other, under the Commission's interpretation of 2(i), the Commission would not expect the parties to the swap to comply with the Category A Transaction-Level Requirements.[530] In this case, the Commission believes that generally there may be a relatively greater supervisory interest on the part of foreign regulators with respect to transactions between two counterparties that are non-U.S. persons so that application of the Category A Transaction-Level Requirements may not be warranted.[531]

With regard to substituted compliance, where a swap is between a non-U.S. swap dealer or non-U.S. MSP (including an affiliate of a U.S. person), on the one hand, and a U.S. person (other than a foreign branch of a U.S. bank swap dealer or U.S. MSP), on the other, the Commission's policy is that substituted compliance would generally not be available for the Category A Transaction-Level Requirements. The Commission believes that this approach is appropriate in this case because the Commission has a strong interest in ensuring that the swap fully complies with the Category A Transaction Level Requirements, without substituted compliance. A number of related reasons support this conclusion. As discussed above, a major purpose of Title VII is to control the potential harm to U.S. markets that can arise from risks that

---

[530] Thus, for example, a swap between a registered non-U.S. swap dealer and a German person would not be subject to Category A Transaction-Level Requirements.

[531] Where the counterparty to a non-U.S. swap dealer or non-U.S. MSP is an international financial institution such as the World Bank, the Commission also generally would not expect the parties to the swap to comply with the Category A Transaction-Level Requirements, even if the principal place of business of the international financial institution were located in the United States.

For this purpose, the Commission would consider the international financial institutions to be the institutions listed as such in the Final Entities Rules, 77 FR at 30692 n. 1180, which include the International Monetary Fund, International Bank for Reconstruction and Development, International Development Association, International Finance Corporation, Multilateral Investment Guarantee Agency, the Inter-American Development Bank, and the Inter-American Investment Corporation. Even though some or all of these international financial institutions may have their principal place of business in the United States, the Commission would generally not consider the application of the Category A Transaction-Level Requirements to be warranted, for the reasons of the traditions of the international system discussed in the Final Entities Rules.

are magnified or transferred between parties via swaps. As also discussed above, swaps between U.S. persons and non-U.S. persons inherently raise the possibility of such risk magnification and transfer. The Category A Transaction Level Requirements are designed to constrain such risk magnification and transfer. The United States thus has a strong interest in applying the Dodd-Frank Act requirements, rather than substitute requirements adopted by non-U.S. authorities, to swaps with U.S. persons. Exercise of U.S. jurisdiction with respect to the Category A Transaction Level Requirements over swaps between U.S. persons and non-U.S. persons is a reasonable exercise of jurisdiction because of the strong U.S. interest in minimizing the potential risks that may flow to the U.S. economy as a result of such swaps.[532]

Even though substituted compliance is not available with respect to swaps between a non-U.S. swap dealer or non-U.S. MSP, on the one hand, and a U.S. person (other than a foreign branch of a U.S. bank swap dealer or U.S. MSP), on the other, a market participant would be deemed in compliance with the relevant Dodd-Frank requirements where it complies with requirements in its home jurisdiction that are essentially identical to the Dodd-Frank requirements. Whether the home jurisdiction's requirements are essentially identical to the corollary Dodd-Frank requirements would be evaluated on a provision-by-provision basis. The Commission intends that a finding of essentially identical generally would be made through Commission action but in appropriate cases could be made through staff no-action.

---

[532] See Restatement §§ 403(2)(a) (effect on territory of regulating state), 403(2)(c) (importance of regulated activity to the regulating state); 403 cmt. b (weight to be given to reasonableness factors depends on circumstances).

Based on the foregoing principles, the Commission staff issued a no-action letter related to risk mitigation.[533] The Commission staff found that the Commission and the EU have essentially identical rules in important areas of risk mitigation for the largest counterparty swap market participants. Specifically, the Commission staff determined that under the European Market Infrastructure Regulation (EMIR), the EU has adopted risk mitigation rules that are essentially identical to certain provisions of the Commission's business conduct standards for swap dealers and major swap participants. In areas such as confirmation, portfolio reconciliation, portfolio compression, valuation, and dispute resolution, the Commission staff found that the respective regimes are essentially identical. The Commission staff determined that where a swap/OTC derivative is subject to concurrent jurisdiction under US and EU risk mitigation rules, compliance under EMIR will achieve compliance with the relevant Commission rules because they are essentially identical.[534]

However, where the swap is between a non-U.S. swap dealer or non-U.S. MSP (including an affiliate of a U.S. person) and a foreign branch of a U.S. bank that is a swap dealer or MSP, as a policy matter, the Commission believes that substituted compliance should be available for the Category A Transaction-Level Requirements, to the extent applicable. Under substituted compliance, a counterparty can choose to follow a foreign jurisdiction's rules even though those rules are not essentially identical, provided that the regime is comparable and comprehensive. The Commission believes that international comity principles support taking this more flexible

---

[533] See No-Action Relief for Registered Swap Dealers and Major Swap Participants from Certain Requirements under Subpart I of Part 23 of Commission Regulations in Connection with Uncleared Swaps Subject to Risk Mitigation Techniques under EMIR, CFTC Letter No. 13-45 (Jul. 11, 2013) ("Risk Mitigation Letter").

[534] The Risk Mitigation Letter provides an example of when requirements in a foreign jurisdiction would be essentially identical to Dodd-Frank requirements. See id.

approach where the transaction, although it involves a U.S. person, takes place in a foreign jurisdiction.

In addition, where a swap is between a non-U.S. swap dealer or non-U.S. MSP (including an affiliate of a U.S. person), on the one hand, and a non-U.S. person that is a guaranteed or conduit affiliate, on the other, substituted compliance may be available to satisfy the Category A Transaction Level Requirements, to the extent applicable, as discussed in the next two sections.

**c. Swaps with a Non-U.S. Person Guaranteed by a U.S. Person**

i. Proposed Guidance

In the Proposed Guidance, with respect to swaps between a non-U.S. swap dealer or non-U.S. MSP, on the one hand, and a non-U.S. counterparty on the other hand, the Commission proposed to interpret CEA section 2(i) such that a non-U.S. swap dealer or non-U.S. MSP would be expected to comply with the Category A Transaction-Level Requirements for swaps where the non-U.S. counterparty's performance is guaranteed, or otherwise supported by, a U.S. person.[535] In consideration of international comity principles, the Commission further proposed to interpret CEA section 2(i) so as to permit substituted compliance for these Transaction-Level Requirements.

The Commission explained that it proposed to interpret section 2(i) in this manner because, where a non-U.S. counterparty's swaps obligations are guaranteed by a U.S. person, the risk of non-performance by the counterparty rests with the U.S. person that is the guarantor of performance or payment. If the non-U.S. person defaults on its obligations under the swaps, then the U.S. person guarantor will be held responsible (or would bear the cost) to settle those

---

[535] See Proposed Guidance, 77 FR at 41288.

obligations. In circumstances in which a U.S. person ultimately bears the risk of non-performance of a counterparty to a swap with a non-U.S. swap dealer or non-U.S. MSP, the Commission noted its strong regulatory interest in performance by both parties to the swap, and hence proposed to apply these Transaction-Level Requirements.[536]

ii. Comments

Some commenters concurred in the Commission's emphasis on a guarantee by a U.S. person as an interpretive guidepost. IATP, for example, stated that "the U.S. person's guarantee is a crucial criterion for the Commission's determination of whether a non-U.S. person would be subject to compliance with Dodd-Frank or whether substituted compliance would be appropriate."[537] Similarly, AFR, in commenting on the Proposed Order, expressed concern about U.S. taxpayer exposure to "foreign affiliates of U.S. banks whose liabilities are guaranteed (implicitly or explicitly) by the parent company."[538]

Other commenters, by contrast, stated that: (1) the Transaction-Level Requirements should never apply to swaps between counterparties that are both non-U.S. persons;[539] (2) the Commission should exclude the swap dealing transactions of a non-U.S. person where the counterparties to the swaps are, themselves, non-U.S. persons, irrespective of whether such counterparties' obligations are guaranteed by the U.S. person;[540] and (3) section 2(i) does not provide a legal basis for jurisdiction over a swap between non-U.S. persons based on a guaranty

---

[536] See id.

[537] See IATP (Aug. 27, 2012) at 3-4.

[538] See AFR (Aug. 14, 2012) at 1-2.

[539] See Australian Bankers (Aug. 27, 2012) at A8.

[540] See Sumitomo (Aug. 24, 2012) at 3. Sumitomo added that, at a minimum, the Commission should exclude swaps obligations in excess of a capped guaranty. Id.

by a U.S. person because guarantees "do not alter the location of activity."[541] In a similar vein, IIB stated that the Commission's proposed treatment of guarantees based on its concern that the U.S. guarantor is exposed to risks incurred by one of its non-U.S. affiliates, "is unduly broad."[542]

IIB explained that guarantees are a very common way for U.S. multinational corporations (both financial and non-financial) to provide credit support for their non-U.S. subsidiaries. According to IIB, parent credit support enables these subsidiaries to hedge their risks cost-effectively in the markets in which they operate, thereby reducing the cost of risk management and therefore the costs of operations.[543] Citi noted that ordinary course parent support commitments, general payment guarantees and capital maintenance commitments are often necessary to enter foreign banking markets. It added that U.S. multinationals also guarantee obligations of local subsidiaries so that their subsidiaries can effectively hedge risks in local markets.[544]

IIB argued that these arrangements "are in stark contrast to circumstances where an unregulated foreign 'shell' affiliate is used for purposes of entering into significant swap dealing activity outside the scope of Dodd-Frank and systematically transferring the market and credit risks arising from the activity to a U.S. affiliate."[545] Accordingly, IIB maintained that application of Transaction-Level Requirements where a non-U.S. counterparty to a non-U.S.

---

[541] See CEWG (Aug. 27, 2012) at 6-7.

[542] See IIB (Aug. 27, 2012) at 14-15.

[543] Id. at 15-16.

[544] See Citi (Aug. 27, 2012) at 4-9.

[545] See IIB(Aug. 27, 2012) at 20.

swap dealer or non-U.S. MSP is guaranteed by a U.S. person is unnecessary because the Commission already has adopted an anti-evasion rule to address such schemes.[546]

Commenters stated that in many instances, the Commission's concerns about a guarantee by a U.S. person can be addressed as a safety and soundness matter by the Federal Reserve Board when it supervises both the guarantor and its subsidiaries; further, where the U.S. providing a guarantee is itself a swap dealer or MSP, it also will be subject to Title VII requirements.[547] In a related vein, the Commission was urged to adopt an exception from its proposed treatment of a non-U.S. counterparty with a guarantee from a U.S. person if either: (1) the counterparty is subject to U.S. capital requirements or comparable foreign (i.e., Basel-compliant) capital requirements; or (2) the guarantor is a U.S. bank holding company.[548]

IIB also stated that the Commission should tie the application of Title VII requirements to the cross-border activities of U.S.-guaranteed foreign subsidiaries to the significance of the risk to the United States arising from the underlying guaranteed activity – that is, where the existence of a guarantee gives rise to direct and significant risks to the United States.[549] Otherwise, IIB stated, "the level of risk to the United States is too contingent, remote or low to justify application of U.S. regulation in the face of strong and more direct non-U.S. regulatory

---

[546] Id. See also Sullivan & Cromwell (Aug. 13, 2012) at 7 ("the counterparty should be considered a non-U.S. person for purposes of the regulatory requirements, provided that the transactions are not being conducted by the non-U.S. persons as an evasion"); The Clearing House (Aug. 27, 2012) at 17 (stating that "[a]ny guaranteed entity of a US Person should only include 'shell' entities that have transferred substantially all of their market and credit risk to a U.S. Person (excluding non-financial entities) or any entities created to evade U.S. swaps rules."); Citi (Aug. 27, 2012) at 4-9 ("… Title VII should not apply to non-U.S. subsidiaries on the basis of guarantees … where such subsidiaries are bona fide companies.").

[547] See Sullivan & Cromwell (Aug. 13, 2012) at 15.

[548] See IIB (Aug. 27, 2012) at 17-18.

[549] Id. at 15-16, 18-19.

interests."[550] Under such an approach, IIB stated, the Commission should adopt an exception from its proposed treatment of a non-U.S. counterparty with a guarantee from a U.S. person if the non-U.S. counterparty is not a financial entity and is entering into the transaction for hedging or risk mitigation purposes.[551] More particularly, IIB posited, if the level of the non-U.S. counterparty's swap activity is insubstantial in relation to its net equity, or if the aggregate potential liability of the U.S. guarantor with respect to the non-U.S. counterparty's swap activity is insubstantial in relation to the net equity of the guarantor, then the risk to the United States will not be significant and Transaction-Level Requirements should not be applied.[552]

Many of the comments on this topic stated that the Commission's proposal in this regard would result in adverse competitive consequences.[553] Others, though, objected that Transaction-Level Requirements should not apply to entities guaranteed by U.S. persons because non-U.S. counterparties will likely be unwilling to agree to the legal documents necessary to comply with those requirements.[554] And others stated that the proposed interpretation will not achieve the objective of mitigating counterparties' exposure to the credit risks of swap dealers because the

---

[550] Id. at 4.

[551] Id. at 16-17.

[552] Id. at 15-16.

[553] See End Users Coalition (Aug. 27, 2012) at 3(Commission's proposal may disadvantage non-U.S. affiliates of U.S. end-users whose non-U.S. counterparties may require guarantees to do business); Citi (Aug. 27, 2012) at 4-9 (applying Transaction-Level Rules in these circumstances would place U.S. multinationals at a severe competitive disadvantage relative to foreign-based corporations, as their subsidiaries abroad would have to either forgo parent support or comply with different transaction-level rules than those of the local market); IIB (Aug. 27, 2012) at 18 (non-U.S. persons that register as swap dealers due to their trading with U.S. persons would be disadvantaged vis-à-vis non-U.S. firms that do not have a U.S. swap dealing business because only the former would be obligated to comply with the Transaction-Level Requirements for swaps with U.S.-guaranteed counterparties); Sullivan & Cromwell (Aug. 13, 2012) at 6 (Title VII should not apply to the non-U.S. operations and activities of an entity simply because it has a U.S. parent that provides a guarantee because this would impose duplicative regulation and unnecessary costs on non-U.S. operations that are already subject to local foreign rules and regulations).

[554] See Hong Kong Banks (Aug. 27, 2012) at 4-5.

U.S. guarantor's exposure in this scenario is to the credit risk of the guaranteed non-U.S. counterparty, not to the non-U.S. swap dealer that is transacting with that guaranteed non-U.S. counterparty.[555]

Citi commented that if Transaction-Level Requirements were to be applied to swaps of non-U.S. persons whose obligations were guaranteed by a U.S. person, then U.S.-based firms may be forced to remove parent support from their overseas subsidiaries in order to remain competitive. It argued that this would cause significant additional capital, resources, and personnel to be moved abroad so that these non-U.S. subsidiaries could manage swap risk on a stand-alone basis which, it averred, would fragment and harm the safety and soundness of U.S.-based firms, U.S. swaps markets, and the U.S. economy.[556] Accordingly, it urged the Commission to further study the issue of guarantees before finalizing its cross-border guidance.[557]

One commenter requested that the Commission clarify the scope of a "guarantee" that can trigger application of Transaction-Level Requirements in these circumstances.[558] Another objected to the scope of the term "guarantee" if it were defined to include not only a guarantee of payment or performance of swaps obligations, but also other formal arrangements to support the ability of a person to perform its obligations (such as liquidity puts and keepwell agreements).[559]

---

[555] See, e.g., ISDA (Aug. 10, 2012) at 10.

[556] See Citi (Aug. 27, 2012) at 4-9.

[557] Id. See also CEWG (Aug. 27, 2012) at 4-5 (recommending that the Commission "undertake a more thorough regulatory analysis with respect to guarantees of swaps obligations").

[558] See Hong Kong Banks at 4-5.

[559] See CEWG (Aug. 27, 2012) at 4-5.

iii. Commission Guidance

Under this Guidance, with respect to swaps between a non-U.S. swap dealer or non-U.S. MSP (including an affiliate of a U.S. person) on the one hand, and a non-U.S. counterparty on the other hand where the non-U.S. counterparty's performance is guaranteed (or otherwise supported by) a U.S. person, the Commission would generally expect the parties to the swap to comply with all of the Category A Transaction-Level Requirements. The Commission believes that this policy is warranted in light of the significant regulatory interest in managing and reducing the risks to U.S. firms, markets and commerce from such transactions. Further, this policy is based on the Commission's view that the failure to apply Category A Transaction-Level Requirements to such swaps could leave a significant gap in the regulation of risks presented by swap activities undertaken by U.S. firms. However, as proposed, the Commission's policy contemplates that substituted compliance (to the extent applicable) could satisfy the Category A Transaction-Level Requirements that otherwise might apply to such swaps, as further discussed below.

In response to commenters that requested clarification of the nature of the guarantee of a non-U.S. counterparty by a U.S. person that will trigger the application of Transaction-Level Requirements to swaps with non-U.S. swap dealers or non-U.S. MSPs, the Commission references the approach set forth in the final rule further defining the term "swap," among others.[560] That is, for this purpose, a guarantee of a swap is a collateral promise by a guarantor to answer for the debt or obligation of a counterparty obligor under a swap.[561] Thus, to the extent

---

[560] See Final Swap Definition, 77 FR at 48225-27. The interpretation herein applies only to a swap that is not a security-based swap or a mixed swap.

[561] Id. at 48226 n.186.

that the non-U.S. swap dealer or non-U.S. MSP would have recourse to the U.S. guarantor in connection with its swaps position, the Commission would generally expect such non-U.S. swap dealer or MSP to comply with the Category A Transaction-Level Requirements for such a guaranteed swap (although substituted compliance may satisfy compliance with such requirements to the extent it is applicable, as discussed above). This interpretation also is consistent with the interpretation related to the MSP definition that the Commission set forth in the Final Entities Rules.[562]

Conversely, where a non-U.S. swap dealer or non-U.S. MSP enters into a swap with a non-U.S. counterparty that does not have a guarantee as so described from a U.S. person and is not an affiliate conduit, the Commission's view is that the Transaction-Level Requirements should not apply. [563] Considerations relevant to application of the Transaction-Level Requirements also relate to persons guaranteeing swaps obligations. As noted in the proposal, the Transaction-Level Requirements with respect to required clearing and swap processing, margin (and segregation), and portfolio reconciliation and compression can serve to significantly mitigate risks to the swap dealer's counterparties, and by extension, the risk to the U.S. person guaranteeing the non-U.S. counterparty's obligations under the swap. Other Transaction-Level Requirements – trade confirmation, swap trading relationship documentation, and daily trading records – protect the counterparties to the swap, and thus also protect a U.S. person that

---

[562] See Final Entities Rules, 77 FR at 30689 ("[A]n entity's swap or security-based swaps positions in general would be attributed to a parent, other affiliate or guarantor for purposes of major participant analysis to the extent that counterparties to those positions would have recourse to that other entity in connection with the position. Positions would not be attributed in the absence of recourse.").

[563] The Commission agrees with commenters who stated that Transaction-Level Requirements should not apply if a non-U.S. swap dealer or non-U.S. MSP relies on a written representation by a non-U.S. counterparty that its obligations under the swap are not guaranteed with recourse by a U.S. person. Such an approach is consistent with Commission practice in other contexts such as the external business conduct rules.

guarantees a non-U.S. counterparty's obligations under the swap, by ensuring that swaps are properly documented and recorded.

In the Commission's view, because Congress directed that the trade execution requirement apply to swaps that are subject to the clearing requirement and made available to trade, it is appropriate for the trade execution requirement to apply to those cross-border swaps that are subject to the clearing mandate and are made available to trade. The Commission believes that both requirements – the clearing mandate and trade execution requirement – are of fundamental importance to the management and reduction of risks posed by swap activities of market participants. Requiring swaps to be traded on a regulated exchange or execution facility provides market participants with greater pre- and post-trade transparency. Real-time public reporting improves price discovery by requiring that swap and pricing data be made publicly available. Taken together, the trade execution and real-time public reporting Transaction-Level Requirements provide important information to market participants and regulators with resulting efficiency in the marketplace. This, in turn, facilitates risk management which benefits swap counterparties and also serves to reduce the likelihood that a U.S. guarantor will be called upon to satisfy a non-U.S. counterparty's swaps obligations.[564]

Further, in the Final Swap Definition, the Commission found that a guarantee of a swap is a term of that swap that affects the price or pricing attributes of that swap. The Commission therefore concluded that when a swap has the benefit of a guarantee, the guarantee is an integral

---

[564] Accordingly, the Commission disagrees with commenters who objected to the proposed interpretation on the ground that it would not advance the goal of mitigating the risk of credit exposure of the guarantor U.S. person to the non-U.S. swap dealer or non-U.S. MSP. The Transaction-Level Requirements also serve to protect against risk to the guarantor U.S. person by reducing the likelihood that its obligations under the guarantee will be called upon in the first instance.

part of that swap. The Commission explained that typically when a swap counterparty uses a guarantee as credit support for its swaps obligations, the guarantor's resources are added to the analysis of the swap because "the market will not trade with that counterparty at the same price, on the same terms, or at all without the guarantee."[565]

For all the foregoing reasons, the Commission disagrees with commenters that asserted that it should not, or lacks the legal authority to, interpret CEA section 2(i) as to apply to swaps where one counterparty is a non-U.S. swap dealer or a non-U.S. MSP and the other counterparty is a non-U.S. person whose obligations under the swap are guaranteed by a U.S. person. Where a U.S. person provides a guarantee of a non-U.S. counterparty's swaps obligations for which there is recourse to the U.S. person, where that guarantee is a term of the swap and affects the price or pricing attributes of that swap, and where the Transaction-Level Requirements serve to protect and mitigate risk to that U.S. person guarantor, the Commission believes that such swaps, either individually or in the aggregate, have a direct and significant connection with activities in, or effect on, U.S. commerce.

The application of Dodd-Frank Act requirements to swaps of non-U.S. persons whose swaps obligations are guaranteed by U.S. persons is also consistent with foreign relations law. As noted in the discussion above regarding the application of these requirements to swaps of U.S. persons with non-U.S. persons, a major purpose of Title VII is to control the potential harm to U.S. markets that can arise from risks that are magnified or transferred between parties via swaps. Similarly, a guarantee – which is an integral part of a swap – can lead to the transfer of risk from the guaranteed non-U.S. person to the U.S. guarantor. Because Category A

---

[565] See Final Swap Definition, 77 FR at 48225-26.

Transaction Level Requirements are designed to mitigate such risk transfer, the Commission believes there is a strong interest in applying the Dodd-Frank Act requirements to swaps of non-U.S. persons that are guaranteed by U.S. persons.[566] However, the Commission also understands the countervailing interest of home country regulators in such swaps, and therefore believes that substituted compliance should generally be available in this context.

The Commission also disagrees with commenters that suggested that its interpretation on this score should apply only to certain guaranteed swaps (e.g., not to swaps by non-financial entities entered into for hedging or risk mitigation purposes), or only to in certain circumstances (e.g., where the guaranteed non-U.S. counterparty's swap activity is a certain percentage of its net equity or the aggregate potential liability of the U.S. guarantor with respect to the non-U.S. counterparty's swaps obligations is a certain percentage of the guarantor's net equity), or only to a certain extent (e.g., to swaps obligations in excess of a capped guarantee). In the Final Swap Definition, the Commission acknowledged that a "full recourse" guarantee would have a greater effect on the price of a swap than a "limited" or "partial recourse" guarantee, yet nevertheless determined that the presence of any guarantee with recourse, no matter how robust, is price forming and an integral part of a guaranteed swap.[567]

The Commission similarly believes that the presence of any guarantee with recourse by a U.S. person of the swaps obligations of a non-U.S. counterparty to a swap with a non-U.S. swap dealer or non-U.S. MSP suffices to justify the application of Transaction-Level Requirements that swap. Therefore, as noted above, to the extent that a non-U.S. swap dealer or non-U.S. MSP

---

[566] See generally note 532 and related discussion, supra.

[567] Id. at 48226.

would have recourse to the U.S. guarantor in connection with its swaps position, the Commission would generally expect such non-U.S. swap dealer or MSP to comply with the Category A Transaction-Level Requirements for such a guaranteed swap (although substituted compliance may satisfy compliance with such requirements to the extent it is applicable). Although the Commission believes all relevant facts and circumstances should be analyzed, as a general matter the Commission is of the view that the purpose for which the non-U.S. counterparty is entering into the swap, or the net equity of the non-U.S. counterparty or the guarantor, or the extent of the guarantee, would generally not warrant a different conclusion.

Finally, the Commission disagrees with commenters that urged it to limit its interpretation in this regard to cases of evasion, or to exclude from the scope of its interpretation those swaps in which the non-U.S. counterparty is subject to appropriate capital requirements or the guarantor is a U.S. bank holding company. The events surrounding the collapse of AIGFP highlight how guarantees can cause major risks to flow to the guarantor. "AIGFP's obligations were guaranteed by its highly rated parent company … an arrangement that facilitated easy money via much lower interest rates from the public markets, but ultimately made it difficult to isolate AIGFP from its parent, with disastrous consequences."[568]

The Commission's view is that the protections and mitigation of risk exposures afforded by the Category A Transaction-Level Requirements would be rendered far less effective if in the case of swaps where one counterparty is a non-U.S. swap dealer or a non-U.S. MSP and the other counterparty is a non-U.S. person guaranteed by a U.S. person such requirements only apply when such swaps are part of a scheme to evade the Dodd-Frank Act. Further, while capital

---

[568] AIG Report, supra note 5, at 20.

requirements are an important element of the Title VII regime to reduce systemic risk,[569] the comprehensive regulatory structure established by the Dodd-Frank Act goes beyond such requirements. The CEA, as amended by the Dodd-Frank Act, also requires the imposition of the Transaction-Level Requirements[570] except to the extent that section 2(i) limits their application to cross-border transactions or activities. Therefore, the Commission believes that, rather than excluding the swaps at issue from the scope of the Title VII regulatory regime, with the corresponding increase in risk to U.S. persons and to the U.S. financial system, in most cases compliance with the Category A Transaction-Level Requirements is appropriate where non-U.S. swap dealers and non-U.S. MSPs that enter into swaps with non-U.S. counterparties guaranteed by a U.S. person. Further, the Commission does not believe that a different interpretation should be taken solely because applicable capital requirements are satisfied.[571]

---

[569] CEA section 4s(e)(1) provides that each registered swap dealer and MSP for which there is a prudential regulator shall meet such minimum capital requirements as the applicable prudential regulator shall prescribe, but that each registered swap dealer and MSP for which there is not a prudential regulator shall meet such minimum capital requirements as the Commission shall prescribe.

[570] See Appendix B for information regarding the Transaction-Level Requirements and the provisions of the CEA which they implement.

[571] In the Final Entities Rules, the Commission stated that it does "not believe that it is necessary to attribute a person's swap or security-based swaps positions to a parent or other guarantor if the person is already subject to capital regulation by the CFTC or SEC (i.e., swap dealers, security-based swap dealers, MSPs, major security-based swap participants, FCMs and broker-dealers) or if the person is a U.S. entity regulated as a bank in the United States. Positions of those regulated entities already will be subject to capital and other requirements, making it unnecessary to separately address, via major participant regulations, the risks associated with guarantees of those positions." See Final Entities Rules, 77 FR at 30689. The Commission continued, "As a result of this interpretation, holding companies will not be deemed to be major swap participants as a result of guarantees to certain U.S. entities that are already subject to capital regulation." Id. at 30689 n. 1134. Subsequently, in the Final Swap Definition, the Commission stated that "[a]s a result of interpreting the term 'swap' (that is not a security-based swap or mixed swap) to include a guarantee of such swap, to the extent that a counterparty to a swaps position would have recourse to the guarantor in connection with the position, and based on the reasoning set forth [in the Final Entities Rules] in connection with major swap participants, the CFTC will not deem holding companies to be swap dealers as a result of guarantees to certain U.S. entities that are already subject to capital regulation." See Final Swap Definition, 77 FR at 48266 n.188. The Commission's conclusion that capital compliance and prudential regulation, in certain circumstances, can obviate the need for registration as a swap dealer or MSP does not bear upon, and is not inconsistent with, the Commission's interpretation herein that notwithstanding capital compliance and prudential regulation, Transaction-Level Requirements may be applied where a non-U.S. swap dealer or non-U.S. MSP enters

In addition, the Commission believes that this Guidance, which contemplates a system of substituted compliance in accordance with principles of international harmonization, may allow non-U.S. swap dealers and non-U.S. MSPs to comply, in appropriate circumstances, with their home-country requirements when transacting with non-U.S. counterparties whose swaps obligations are guaranteed with recourse by U.S. persons. The Commission believes that the substituted compliance regime contemplated by the Guidance will facilitate equivalent regulatory treatment of equivalent swaps without undermining the swaps reforms enacted by Congress in Title VII.

**d. Swaps with a Non-U.S. Person that is an Affiliate Conduit**

i. Proposed Guidance

The Commission proposed to interpret CEA section 2(i) such that the Category A Transaction-Level Requirements would apply to a swap if at least one of the parties to the swap is an "affiliate conduit." Under the Proposed Guidance, an affiliate conduit exists when: (1) a non-U.S. person that is majority-owned, directly or indirectly, by a U.S. person; (2) the non-U.S. person regularly enters into swaps with one or more of its U.S. affiliates of its U.S. person owner; and (3) the financial results of such non-U.S. person are included in the consolidated financial statements of its U.S. person owner.[572] The Commission explained that it believed the proposed application of Transaction-Level Requirements was necessary because, "given the nature of the relationship between the conduit and the U.S. person, the U.S. person is directly

---

into a swap with a non-U.S. counterparty whose obligations under that swap are guaranteed, with recourse, by a U.S. person.

[572] See Proposed Guidance, 77 FR at 41229.

exposed to risks from and incurred by" the affiliate conduit.[573] The Commission further indicated that it was concerned that a U.S. swap dealer or U.S. MSP would utilize affiliate conduits to conduct swaps outside the Dodd-Frank regulatory regime.

ii. Comments

The commenters who addressed the Commission's proposed approach to affiliate conduits expressed concerns about what they felt was an overly broad scope of the term "affiliate conduit." Several of these commenters stated that the non-U.S. affiliate conduit concept should be omitted from the Guidance.[574] SIFMA stated that the term "regular" is too vague in that "it does not account for the purpose of the inter-affiliate swap, the relative amount of the conduit's risk transferred, the nature of the transferred risk, or whether some or all of the risk is transferred."[575] SIFMA also commented that activities of a non-U.S. affiliate conduit do not satisfy the requisite nexus to the United States under section 2(i) to justify different treatment from other non-U.S. counterparties. Further, SIFMA stated that where substituted compliance is unavailable, a non-U.S. swap dealer transacting with an affiliate conduit is subject to applicable Transaction-Level Requirements, which could cause non-U.S. swap dealers to cease doing business with non-U.S. affiliate conduits.[576] As an alternative, SIFMA recommended that the proposed affiliate conduit provision that the conduit "regularly enter into swaps" should be

---

[573] Id.

[574] SIFMA (Aug. 27, 2012) at A22-23; IIB at (Aug. 27, 2012) at 20-21; Hong Kong Banks (Aug. 27, 2012) at 13.

[575] SIFMA (Aug. 27, 2012) at A23. See also IIAC (stating that the Commission should clarify the meaning of "regularly enters into swaps with … affiliates" and circumstances under which the Commission would interpret the financials of a non-U.S. counterparty to be combined with the financial statements of the U.S. person for purposes of applying Transaction-Level Requirements to transactions by U.S. persons that might be using conduits to avoid such requirements) (Aug. 27, 2012) at 8.

[576] SIFMA (Aug. 27, 2012) at A22.

replaced with a provision that the conduit "regularly enter[] into swaps with one or more other U.S. affiliates of the U.S. person for the purpose of transferring to that U.S. person all risk of swap activity."

Other commenters raised similar objections concerning the scope of the affiliate conduit provision. Goldman stated that the proposed description of an affiliate conduit was so broad that "an entity could be rendered a conduit by executing even a single trade despite the fact that the entity otherwise would be eligible for substituted compliance, or would not fall within Title VII's jurisdiction at all."[577] Such a broad definition, in Goldman's view, will result in competitive disparities for foreign affiliates of U.S.-based swap dealers and may even cover non-financial entities attempting to hedge risk.[578] SIFMA added that the concept of indirect majority ownership is imprecise and its application to non-U.S. affiliate conduits is unclear.[579] Hong Kong Banks believed that the conduit proposal is unnecessary since its activities would be captured in the registration process.[580] Peabody stated that the application of Transaction-Level Requirements to affiliate conduits seemingly contradicts the Proposed Guidance's treatment of

---

[577] Goldman (Aug. 27, 2012) at 6. See also Japanese Bankers Association (Aug. 27, 2012) at 11 (stating that it is difficult to determine under the Proposed Guidance when a counterparty is a conduit for a U.S. person, and that the conduit provisions should not be implemented).

[578] Goldman (Aug. 27, 2012) at 6. See also Peabody (Aug. 27. 2012) at 3 (stating that applying the Dodd-Frank requirements to swaps entered into or booked by affiliates of commercial end-users outside the United States to hedge or mitigate commercial risks of activities outside the United States will create an overlapping (and potentially inconsistent) tangle of international laws that will increase costs and potential liabilities associated with such swaps, and materially undermine their utility and risk mitigation benefits; stating further that foreign entities wishing to avoid becoming subject to Dodd-Frank requirements will decline to enter into swaps with such affiliates, thereby decreasing market liquidity, increasing market risk competition, imposing higher commercial costs, and resulting in higher prices for customers and downstream consumers, and would put U.S. business at a competitive disadvantage in global markets).

[579] SIFMA (Aug. 27, 2012) at A24.

[580] Hong Kong Banks (Aug. 27, 2012) at 13.

foreign affiliates as non-U.S. persons.[581] If the affiliate conduit concept remains in the Guidance, SIFMA requested that the Commission clarify whether or not swap dealers may rely on a counterparty's representations as to its non-U.S.-affiliate's conduit status.[582]

IIB stated that the Commission should withdraw its proposal on affiliate conduits and instead, where there is clear circumvention, rely on its existing anti-evasion authority.[583] It added that the Commission's proposal for the "conduit" treatment of a foreign entity that "regularly" engages in back-to-back swaps with a U.S. affiliate is unjustifiably broad. IIB also stated that the proposed standard is inconsistent with statutory standards for the extraterritorial application of Title VII, and that there is no basis to conclude that inter-affiliate swaps create direct and significant risk to the United States simply because they occur "regularly."[584]

iii. Commission Guidance

In the Proposed Guidance, the Commission explained that it believed the proposed application of Transaction-Level Requirements was necessary because, "given the nature of the relationship between the conduit and the U.S. person, the U.S. person is directly exposed to risks from and incurred by" the affiliate conduit.[585] The Commission further indicated that it was concerned that a U.S. swap dealer or U.S. MSP would utilize affiliate conduits to conduct swaps outside the Dodd-Frank regulatory regime.

---

[581] Peabody (Aug. 28, 2012) at 2-3.

[582] SIFMA (Aug. 27, 2012) at A24. SIFMA stated that the determination of whether a counterparty to a swap is a non-U.S. affiliate conduit should be made at the inception of the swap based on the most recent updated representation from the counterparty, which should be renewed by the counterparty once per calendar year. Id. at A25.

[583] IIB (Aug. 27, 2012) at 20-21.

[584] Id. at 19.

[585] See Proposed Guidance, 77 FR at 41229.

For purposes of this policy statement, the Commission is clarifying that an affiliate conduit encompasses those entities that function as a conduit or vehicle for U.S. persons conducting swaps transactions with third-party counterparties. In response to comments received, the Commission is identifying some of the factors that the Commission believes are relevant to determining whether a non-U.S. person is an "affiliate conduit" of a U.S. person. As explained in greater detail below, modifications to the Proposed Guidance with regard to the term "affiliate conduit" are intended to respond to commenters' concerns about a lack of clarity on the scope of the term affiliate conduit and to better identify those non-U.S. affiliates whose swap activities, either individually or in the aggregate, have a direct and significant connection with activities in, or effect on, U.S. commerce as a result of their relationship with their U.S. affiliates. Specifically, the Commission is modifying the factors that might be relevant to the consideration of whether a non-U.S. affiliate of a U.S. person is an affiliate conduit by: (1) clarifying the meaning of "regularly enters into swaps," and in particular, the activities of a non-U.S. counterparty that renders it an affiliate conduit; and (2) adding the concept of "control."

As the Commission understands, it is common for large global companies to centralize their hedging or risk-management activities in one or more affiliates (informally referred to as a "treasury conduit" or "conduit"). Under this structure, the conduit may enter into swaps with its affiliates and then enter into offsetting swaps with third-parties. In other cases, the conduit may enter into swaps with third-parties as agent for its affiliates. In either case, the conduit functions as a vehicle by which various affiliates engage in swaps with third-parties (i.e., the market). This paradigm promotes operational efficiency and prudent risk management by enabling a company

to manage its risks on a consolidated basis at a group level.[586] Accordingly, based on comments, rather than considering whether a non-U.S. person "regularly enters into swaps" with one or more of its U.S. affiliates of its U.S. person owner, the Commission will generally consider whether the non-U.S. person, in the regular course of business, engages in swaps with non-U.S. third-parties for the purpose of hedging or mitigating risks faced by, or to take positions on behalf of, its U.S. affiliates, and enters into offsetting swaps or other arrangements with its U.S. affiliates in order to transfer the risks and benefits of such swaps with third-parties to its U.S. affiliates.

The Commission recognizes the significant benefits associated with a corporate group's use of a single entity to conduct the group's market-facing swap business. The Commission also believes, though, that in this situation the risks resulting from swaps of the entity that faces the market as a conduit on behalf of its affiliates in fact reside with those affiliates; that is, while the swaps are entered into by the conduit, through back-to-back swaps or other arrangements the

---

[586] One market participant described the functions of such a conduit and its relationship with respect to other affiliates within the corporate group in the following manner:

> Many business enterprises, including [Prudential Financial Inc., or "PFI"], elect to operate in a manner that assigns specific functions to related and commonly-controlled affiliates. With regard to swap transactions, it has long been our practice, as an enterprise-type company with separate legal entities that are commonly owned by PFI to use one affiliate, Prudential Global Funding LLC ("PGF"), to directly face the market as a "conduit" to hedge the net commercial and financial risk of the various operating affiliates within PFI. Under this practice, only PGF (i.e., the conduit) is required to trade with external market participants, while the internal affiliates within PFI trade directly with the PGF. The use of PGF as the single conduit for the various operating affiliates within PFI diminishes the demands on PFI's financial liquidity, operational assets and management resources, as affiliates within PFI avoid having to establish independent relationships and unique infrastructure to face the market. Moreover, use of PGF as a conduit within PFI permits the netting of our affiliates' trades (e.g., one affiliate is hedging floating rates while another is hedging fixed rates). This effectively reduces the overall risk of PFI and our affiliates, and allows us to manage fewer outstanding positions with external market participants.

The Prudential Insurance Company of America (Feb. 17, 2011) at 2.

conduit passes the risks and benefits of those swaps to its affiliates.[587] Where the conduit is located outside the United States, but is owned and controlled by a U.S. person, the Commission believes that to recognize the economic reality of the situation, the conduit's swaps should be attributed to the U.S. affiliate(s). The fact that the conduit is located outside the United States does not alter the economic reality that its swaps are undertaken for the benefit of, and at the economic risk of, the U.S. affiliate(s), and more broadly, for the corporate group that is owned and controlled by a U.S. person. Under these circumstances, the Commission believes that the swap activities of the non-U.S. conduit may meet the "direct and significant" jurisdictional nexus within the meaning of CEA section 2(i).[588]

Further, in order to facilitate a consistent application of the term affiliate conduit and to mitigate any undue burden or complexity for market participants in assessing affiliate conduit status, the Commission clarifies that its policy contemplates that a market participant may reasonably rely on counterparty representations as to its non-U.S. affiliate conduit status.[589]

Finally, the Commission notes in response to commenters that an affiliate conduit would not necessarily be guaranteed by its parent. As one market participant explained, "centralized hedging centers are generally evaluated as wholly-owned subsidiaries of the corporate group that do not require additional credit support, such as a parent guaranty or collateral."[590] Therefore, the Commission believes that it is reasonable and appropriate to interpret CEA section 2(i) in a

---

[587] See The Prudential Insurance Company of America (Feb. 17, 2011); Kraft Foods ("Kraft") (Feb. 11, 2011).

[588] In this respect, it is irrelevant whether the risk is wholly or partly transferred back to the U.S. affiliate(s); the jurisdictional nexus is met by reason of the trading relationship between the conduit and the affiliated U.S. persons.

[589] This is consistent with the Commission's approach to the determination of whether a counterparty is a "U.S. person." See section IV.A, supra.

[590] See Kraft (Feb. 11, 2011) at 3.

manner that recognizes an affiliate conduit as a separate category of counterparty whose swaps with non-U.S. persons may be subject to certain Transaction-Level Requirements. Specifically, where one of the parties to the swap is a conduit affiliate, the Commission would generally expect the parties to the swap only to comply with (to the extent that the Inter-Affiliate Exemption is elected), the conditions of the Inter-Affiliate Exemption, including the treatment of outward-facing swaps condition in Commission regulation 50.52(b)(4)(i). In addition, the part 43 real-time reporting requirements must be satisfied.

In summary, for the purposes of the Commission's interpretation of CEA section 2(i), the Commission believes that certain factors are relevant to considering whether a non-U.S. person is an "affiliate conduit." Such factors include whether:

(i) the non-U.S. person is a majority-owned affiliate[591] of a U.S. person;

(ii) the non-U.S. person is controlling, controlled by or under common control[592] with the U.S. person;

---

[591] Commission regulation 1.3(ggg)(6)(i) defines "majority-owned affiliates" as follows:

> [C]ounterparties to a swap are majority-owned affiliates if one counterparty directly or indirectly owns a majority interest in the other, or if a third party directly or indirectly owns a majority interest in both counterparties to the swap, where 'majority interest' is the right to vote or direct the vote of a majority of a class of voting securities of an entity, the power to sell or direct the sale of a majority of a class of voting securities of an entity, or the right to receive upon dissolution or the contribution of a majority of the capital of a partnership.

[592] Commission regulation 1.3(ggg)(4)(i) refers to an "entity controlling, controlled by or under common control with the person." Final Entities Rules elaborated on this provision, stating:

> For these purposes, we interpret control to mean the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract or otherwise. This is consistent with the definition of "control" and "affiliate" in connection with Exchange Act rules regarding registration statements. See Exchange Act rule 12b-2. …

77 FR at 30631 n. 437, and

> [I]f a parent entity controls two subsidiaries which both engage in activities that would cause the subsidiaries to be covered by the dealer definitions, then each subsidiary must aggregate the swaps or

(iii) the financial results of the non-U.S. person are included in the consolidated financial statements of the U.S. person; and

(iv) the non-U.S. person, in the regular course of business, engages in swaps with non-U.S. third-party(ies) for the purpose of hedging or mitigating risks faced by, or to take positions on behalf of, its U.S. affiliate(s), and enters into offsetting swaps or other arrangements with its U.S. affiliate(s) in order to transfer the risks and benefits of such swaps with third-party(ies) to its U.S. affiliates.

Other facts and circumstances also may be relevant. The Commission does not intend that the term "conduit affiliate" would include affiliates of swap dealers.

### 5. Application of the "Category B" Transaction-Level Requirements to Swap Dealers and MSPs

This section discusses the Commission's policy on the application of the Category B Transaction-Level Requirements to swaps in which at least one of the parties to the swap is a registered swap dealer or MSP. As noted earlier, the Category B Transaction Level Requirements pertain to external business conduct standards which the Commission adopted pursuant to CEA section 4s(b) as a Category B Transaction-Level Requirement.[593]

Consistent with the Proposed Guidance, the Commission will generally interpret CEA section 2(i) so that the Category B Transaction-Level Requirements (i.e., the external business

---

security-based swaps that result from both subsidiaries' dealing activities in determining if either subsidiary qualifies for the de minimis exception.

Id. at n. 438.

[593] The categorization of Transaction-Level Requirements into Categories A and B is discussed in section E, supra. See Appendix B for a descriptive list of the Category A and Category B requirements and Appendix D for a table summarizing the application of the Category A Transaction-Level Requirements to Swap Dealers and MSPs. The Appendices to this Guidance should be read in conjunction with this section and the rest of the Guidance.

conduct standards) either do or do not apply to the swap, based on the counterparties to the swap, as explained below. Under this interpretation, substituted compliance is generally not expected to be applicable with regard to the Category B Transaction-Level Requirements under this Guidance.[594]

In considering whether Category B Transaction-Level Requirements are applicable, the Commission would generally consider whether the swap is with a:

(i) U.S. swap dealer or U.S. MSP (including affiliates of non-U.S. persons);

(ii) foreign branch of a U.S. bank that is a swap dealer or MSP; or

(iii) non-U.S. swap dealer or non-U.S. MSP (including an affiliate of a U.S. person).

Specifically, as explained more below, where a swap is with a U.S. swap dealer or U.S. MSP, the parties to the swap generally should be subject to the Category B Transaction-Level Requirements in full, regardless of whether the other counterparty to the swap is a U.S. person or a non-U.S. person. However, in the case of a foreign branch of a U.S. bank that is a swap dealer or MSP, or a non-U.S. swap dealer or non-U.S. MSP, the parties to the swap should generally only be subject to the Category B Transaction-Level Requirements when the counterparty to the swap is a U.S. person (other than a foreign branch of a U.S. bank that is a swap dealer or MSP). Conversely, under the Commission's interpretation of 2(i), where a swap is between a non-U.S. swap dealer or non-U.S. MSP (including an affiliate of a U.S. person) and a non-U.S. counterparty (regardless of whether the non-U.S. counterparty is a guaranteed or conduit affiliate), the parties to the swap would not be expected to comply with the Category B

---

[594] See Appendix E to this Guidance for a summary of these requirements and the discussion in section D, supra.

Transaction-Level Requirements. The reasons for the Commission's policies are discussed below.

The application of the Category B Transaction-Level Requirements is summarized in Appendix E to this Guidance, which should be read in conjunction with the rest of this Guidance.

**a. Swaps with U.S. Swap Dealers and U.S. MSPs**

As explained above, where a swap is with a U.S. swap dealer or U.S. MSP (including an affiliate of a non-U.S. person), the Commission's policy is that the parties to the swap should be subject to the Category B Transaction-Level Requirements in full, regardless of whether the counterparty is a U.S. person or a non-U.S. person, without substituted compliance available.

**b. Swaps with Foreign Branches of a U.S. Bank that is a Swap Dealer or MSP**

In the case of a swap with a foreign branch of a U.S. bank that is a swap dealer or MSP, the Commission's policy is that the Category B Transaction-Level Requirements should apply only if the counterparty to the swap is a U.S. person (other than a foreign branch of a U.S. bank that is a swap dealer or MSP).[595]

The Commission believes that where a swap is between a foreign branch of a U.S. bank that is a swap dealer or MSP[596] and a U.S. person (other than a foreign branch of a U.S. bank that is a swap dealer or MSP), the swap has a direct and significant connection with activities in, or effect on, U.S. commerce. Because of the significant risks to U.S. persons and the financial

---

[595] For the reasons discussed in note 531, supra, where the counterparty to the swap is an international financial institution, the Commission also generally would not expect the parties to the swap to comply with the Category B Transaction-Level Requirements, even if the principal place of business of the international financial institution were located in the United States.

[596] See section C, supra, regarding the definition of a foreign branch and the determination of when a swap transaction is with a foreign branch for purposes of this Guidance.

system presented by such swap activities, under the Commission's interpretation of CEA section 2(i), generally the parties to the swap should comply with the Category B Transaction Level Requirements. Whenever a swap involves at least one counterparty that is a U.S. person, the Commission believes it has a strong supervisory interest in regulating and enforcing Transaction-Level Requirements, including external business conduct standards. In this case, the Commission believes the transaction should be viewed as being between two U.S. persons. For these reasons, the Commission's policy under section 2(i) is that substituted compliance would not be available.[597]

However, where the swap is between a foreign branch of a U.S. bank that is a swap dealer or MSP, on the one hand, and a non-U.S. person on the other (whether or not such non-U.S. person is a guaranteed or conduit affiliate), the Commission believes that the interests of the foreign jurisdiction in applying its own transaction-level requirements to the swap are sufficiently strong that the Category B Transaction-Level Requirements generally should not apply under section 2(i). In this case, even though the Commission considers a foreign branch of a U.S. bank that is a swap dealer or MSP to be a U.S. person, the Commission believes that because the counterparty is a non-U.S. person and the swap takes place outside the United States, foreign regulators may have a relatively stronger supervisory interest in regulating and enforcing sales practices related to the swap. Therefore, in light of international comity principles, the Commission believes that application of the Category B Transaction-Level Requirements may

[597] In this case, although the foreign branch would not register separately as a swap dealer, the Commission interprets 2(i) in a manner that would permit the U.S. person to task its foreign branch to fulfill its regulatory obligations with respect to the Category B Transaction-Level Requirements. The Commission would consider compliance by the foreign branch or agency to constitute compliance with these Transaction-Level Requirements. However, under the Commission's interpretation of 2(i), the U.S. person (principal entity) would remain responsible for compliance with the Category B Transaction-Level Requirements.

not be warranted in this case. Therefore, under the Commission's interpretation of section 2(i), the parties to the swap generally would not be expected to comply with the Category B Transaction-Level Requirements.

The Commission believes that, in the context of the Category B Transaction-Level Requirements, the same reasoning also should apply to a swap between two foreign branches of U.S. banks that are each swap dealers or MSPs. Just as the Commission would have a strong supervisory interest in regulating and enforcing sales practices associated with activities taking place within the United States, the foreign regulators would have a similar claim to overseeing sales practices occurring within their jurisdiction.

Accordingly, the Commission interprets CEA section 2(i) so that where a swap is between the foreign branch of a U.S. bank that is a swap dealer or MSP, on the one hand, and either a non-U.S. person or a foreign branch of a U.S. bank that is a swap dealer or MSP, on the other, the parties to the swap generally would not be expected to comply with the Category B Transaction-Level Requirements.

**c. Swaps with Non-U.S. Swap Dealers and Non-U.S. MSPs**

Under the Commission's interpretation of 2(i), where a swap is between a non-U.S. swap dealer or non-U.S. MSP (including an affiliate of a U.S. person), on the one hand, and a U.S. (or that is a guaranteed affiliate), on the other, the parties to the swap generally would be expected to comply with the Category B Transaction-Level Requirements.[598] In the Commission's view, in this case, the swap should be subject to the provisions of Title VII of the Dodd-Frank Act and

[598] As noted above, for the reasons discussed in note 531, where the counterparty to the swap is an international financial institution, the Commission also generally would not expect the parties to the swap to comply with the Category B Transaction-Level Requirements, even if the principal place of business of the international financial institution were located in the United States.

Commission implementing regulations, including the Category B Transaction-Level Requirements. Because of the significant risks to U.S. persons and the financial system presented by swap activities outside the United States where one of the counterparties to the swap is a U.S. person (whether inside or outside the United States), the Commission believes that a U.S. person's swap activities with a non-U.S. counterparty has the requisite direct and significant connection with activities in, or effect on, U.S. commerce under CEA section 2(i) to apply the Category B Transaction-Level Requirements to the transaction.

The Commission observes that, where a swap between a non-U.S. swap dealer and a U.S. person is executed anonymously on a registered DCM or SEF and cleared by a registered DCO,[599] the Category B Transaction-Level Requirements would not be applicable.[600]

Because a registered FBOT is analogous to a DCM, the Commission is of the view that the requirements likewise would not be applicable where such a swap is executed anonymously on a registered FBOT and cleared.

---

[599] As discussed in greater detail above, the Commission notes that there are no exempt DCOs at this time. If and when the Commission determines to exercise its authority to exempt DCOs from applicable registration requirements, the Commission would likely address, among other things, the conditions and limitations applicable to clearing swaps for customers subject to section 4d(f) of the CEA.

[600] See 17 CFR 23.402(b)-(c) (requiring swap dealers and MSPs to obtain and retain certain information only about each counterparty "whose identity is known to the swap dealer or MSP prior to the execution of the transaction"); 23.430(e) (not requiring swap dealers and MSPs to verify counterparty eligibility when a transaction is entered on a DCM or SEF and the swap dealer or MSP does not know the identity of the counterparty prior to execution); 23.431(c) (not requiring disclosure of material information about a swap if initiated on a DCM or SEF and the swap dealer or MSP does not know the identity of the counterparty prior to execution); 23.450(h) (not requiring swap dealers and MSPs to have a reasonable basis to believe that a Special Entity has a qualified, independent representative if the transaction with the Special Entity is initiated on a DCM or SEF and the swap dealer or MSP does not know the identity of the Special Entity prior to execution); 23.451(b)(2)(iii) (disapplying the prohibition on entering into swaps with a governmental Special Entity within two years after any contribution to an official of such governmental Special Entity if the swap is initiated on a DCM or SEF and the swap dealer or MSP does not know the identity of the Special Entity prior to execution).

Conversely, under the Commission's interpretation of 2(i), where a swap is between a non-U.S. swap dealer or non-U.S. MSP (including an affiliate of a U.S. person) and a non-U.S. counterparty (regardless of whether the non-U.S. counterparty is a guaranteed or conduit affiliate), the parties to the swap would not be expected to comply with the Category B Transaction-Level Requirements. The Commission believes that regulators may have a relatively stronger supervisory interest in regulating the Category B Transaction-Level Requirements related to swaps between non-U.S. persons taking place outside the United States than the Commission, and that therefore applying the Category B Transaction-Level Requirements to these transactions may not be warranted. The Commission notes that just as the Commission would have a strong supervisory interest in regulating and enforcing the Category B Transaction-Level Requirements associated with activities taking place in the United States, foreign regulators would have a similar claim to overseeing sales practices for swaps occurring within their jurisdiction.

For the reasons stated in section b above, under the Commission's interpretation of section 2(i), where a swap is between a non-U.S. swap dealer or non-U.S. MSP (including an affiliate of a U.S. person), on the one hand, and the foreign branch of a U.S. bank that is a swap dealer or MSP, on the other, the parties to the swap generally would not be expected to comply with the Category B Transaction-Level Requirements.

As noted previously, under the 2(i) interpretations, substituted compliance is generally not expected to be applicable to the Category B Transaction-Level Requirements under this Guidance.[601]

---

[601] See Appendix E to this Guidance for a summary of these requirements and the discussion in section E, supra.

### H. Application of the CEA's Swap Provisions and Commission Regulations to Market Participants that are not Registered as a Swap Dealer or MSP

This section sets forth the Commission's general policy on application of the CEA's swaps provisions and Commission regulations to swap counterparties that are not registered as swap dealers or MSPs ("non-registrants"), including the circumstances under which the counterparties would be eligible for substituted compliance.

Several of the CEA's swaps provisions and Commission regulations – namely, those relating to required clearing, trade execution, real-time public reporting, Large Trader Reporting, SDR Reporting, and swap data recordkeeping (collectively, the "Non-Registrant Requirements")[602] – also apply to persons or counterparties other than a swap dealer or MSP. In this section, the Commission sets forth the Commission's policy on application of these Non-Registrant Requirements to cross-border swaps in which neither counterparty is a swap dealer or MSP (i.e., all other market participants including "financial entities," as defined in CEA section 2(h)(7)(C)).[603]

Section 1 discusses the Commission's policy under CEA section 2(i) with regard to the application of the Non-Registrant Requirements to cross-border swaps between two non-registrants where one (or both) of the counterparties to the swap is a U.S. person.

---

[602] See section IV.D, supra. Part 45 of the Commission's regulations requires swap counterparties that are not swap dealers or MSPs to keep "full, complete and systematic records, together with all pertinent data and memoranda" with respect to each swap to which they are a counterparty. See 17 C.F. R. 45.2. Such records must include those demonstrating that they are entitled, with respect to any swap, to make use of the clearing exception in CEA section 2(h)(7). Swap counterparties that are not swap dealers or MSPs must also comply with the Commission's regulations in part 46, which address the reporting of data relating to pre-enactment swaps and data relating to transition swaps.

[603] Nothing in this Guidance should be construed to address the ability of a foreign board of trade to offer swaps to U.S. persons pursuant to part 48 of the Commission's regulations.

Substituted compliance is not applicable where one (or both) swap counterparties is a U.S. person.

Section 2 discusses the Commission's policy under CEA section 2(i) with regard to the application of the Non-Registrant Requirements to cross-border swaps between two non-registrants where both counterparties to the swap are non-U.S. persons. The eligibility of various counterparties to such swaps for substituted compliance is also addressed in section 2.

The application of the specified Dodd-Frank provisions and Commission regulations specified below to swaps between counterparties that are neither swap dealers nor MSPs is summarized in Appendix F to this Guidance, which should be read in conjunction with the rest of this Guidance.

### 1. Swaps between Non-Registrants Where One or More of the Non-Registrants is a U.S. Person

As noted in the Proposed Guidance, to manage risks in a global economy, U.S. persons may need to, and frequently do, transact swaps with both U.S. and non-U.S. counterparties. The swap activities of U.S. persons, particularly those with global operations, frequently occur outside of U.S. borders.

With regard to cross-border swaps between two non-registrants where one (or both) of the counterparties to the swap is a U.S. person (including an affiliate of a non-U.S. person), the Commission's interprets CEA 2(i) such that the parties to the swap generally would be expected to comply with the Non-Registrant Requirements. As the Commission noted in the Proposed Guidance, the risks to U.S. persons and the U.S. financial system do not depend on the location

of the swap activities of U.S. persons.[604] Where one or both of the counterparties to a swap between two non-registrants is a U.S. person, the Commission believes that the U.S. persons' swap activities (whether inside or outside the United States) – due their presence in the U.S. and relationship to U.S. commerce – have a direct and significant connection with activities in, or effect on, U.S. commerce. Therefore, the Commission's policy is that where a swap transaction is between non-registrants, and one or more of the counterparties is a U.S. person, generally the parties to the swap will be expected to comply in full with the Non-Registrant Requirements.[605] In addition, where one or more of the counterparties to a swap between non-registrants is a U.S. person, the Commission's policy generally is that substituted compliance is not available, for the reasons discussed below.

As noted in section D above, the Dodd-Frank Act's required clearing and swap processing requirements protect counterparties from the counterparty credit risk of their original counterparties, which in turn, protects against the accumulation of systemic risk because of the risk mitigation benefits offered by central clearing. Similarly, the trade execution and real-time public reporting requirements serve to promote both pre- and post-trade transparency which, in turn, enhance price discovery and decrease risk. Together, these requirements serve an essential

---

[604] See Proposed Guidance, 77 FR 41234 n. 138. Further, in the Proposed Guidance, the Commission stated that it believes that section 2(i) does not require a transaction-by-transaction determination that a particular swap outside the United States has a direct and significant connection with activities in, or effect on, commerce of the United States in order to apply the swaps provisions of the CEA to such transactions; rather, it is the aggregate of such activities and the aggregate connection of such activities with activities in the U.S. or effect on U.S. commerce that warrants application of the CEA swaps provisions to all such activities. See Hoffmann-La Roche, 542 U.S. at 168 (responding that respondents' recommendation that the court should take account of comity considerations on a case by case basis is "too complex to prove workable").

[605] For the reasons discussed in note 531, supra, one or more of the counterparties to a swap between non-registrants is an international financial institution, the Commission generally would not expect the parties to the swap to comply with the Non-Registrant Requirements, even if the principal place of business of the international financial institution were located in the United States.

role in protecting U.S. market participants and the general market against financial losses. The Commission cannot fully and responsibly fulfill its charge to protect the U.S. markets and market participants through a substituted compliance regime where one counterparty is a U.S. person. Accordingly, the Commission's policy is to expect full compliance with the Non-Registrant Requirements relating to required clearing, trade execution, and real-time public reporting with regard to any swaps between non-registrants where one or both of the counterparties is a U.S. person. For substantially the same reasons, application of U.S. requirements in these transactions is a reasonable exercise of U.S. jurisdiction under principles of foreign relations law.[606]

Large Trader Reporting provides the Commission with data regarding large positions in swaps with a direct or indirect linkage to specified U.S.-listed physical commodity futures contracts, in order to enable the Commission to implement and conduct effective surveillance of these economically equivalent swaps and futures. To facilitate the monitoring of trading across the swaps and futures markets, swaps positions must be converted to futures equivalents for reporting purposes; reportable thresholds are also defined in terms of futures equivalents. As discussed in further detail in section G above, in light of the very specific interest of the Commission in conducting effective surveillance of markets in swaps that have been determined to be economically equivalent to U.S. listed physical commodity futures contracts, and given the anticipated impediments to obtaining directly comparable positional data through any foreign swap data reporting regime, the Commission's policy is to construe CEA section 2(i) in a manner

---

[606] See Restatement §§ 403(2)(a)-(c).

that would not recognize substituted compliance in lieu of compliance with Large Trader Reporting.

As noted in section E, data reported under the SDR Reporting rules provide the Commission with information necessary to better understand and monitor concentrations of risk, as well as risk profiles of individual market participants. Swap data recordkeeping is an important component of an effective internal risk management process. Therefore, the Commission's policy is that generally both SDR Reporting and swap data recordkeeping should apply in full where one of the counterparties to a swap between two non-registrants (non-swap dealers or non-MSPs) is a U.S. person.

As noted above, the clearing of swaps through a DCO mitigates counterparty credit risk and collateralizes the credit exposures posed by swaps. Section 2(h)(1) of the CEA requires a swap to be submitted for clearing to a registered DCO or a DCO that is exempt from registration under the CEA, if the Commission has determined that the swap is required to be cleared.[607] The Commission has adopted a clearing requirement determination pursuant to the CEA and rules under part 50 of the Commission's regulations such that certain classes of swaps are required to be cleared, unless counterparties to the swap qualify for an exception or exemption from clearing

[607] The Commission notes that under CEA section 5b(h), the Commission has discretionary authority to exempt DCOs, conditionally or unconditionally, from the applicable DCO registration requirements. Specifically, section 5b(h) of the Act provides that "[t]he Commission may exempt, conditionally or unconditionally, a derivatives clearing organization from registration under this section for the clearing of swaps if the Commission determines that the [DCO] is subject to comparable, comprehensive supervision and regulation by the Securities and Exchange Commission or the appropriate government authorities in the home country of the organization." Thus, the Commission has discretion to exempt from registration DCOs that, at a minimum, are subject to comparable and comprehensive supervision by another regulator. The Commission further notes that it has not yet exercised its discretionary authority to exempt DCOs from registration, and that until such time as the Commission determines to exercise such authority, swaps subject to the clearing requirement must be submitted to registered DCOs for clearing.

under the CEA or part 50 of the Commission's regulations.[608] In the final rules adopting the Inter-Affiliate Exemption, the Commission stated that a U.S. person that enters into any swap that is required to be cleared is subject to the clearing requirements of the CEA and part 50 of the Commission's regulations.[609] Accordingly, in the context of this Guidance, the Commission's policy is that the clearing requirement under section 2(h)(1) and part 50 of the Commission's regulations applies in full to a swap where at least one of the counterparties to the swap is a U.S. person, without substituted compliance available. But substituted compliance may be available with respect to the clearing requirement for swaps between, on the one hand, a U.S. swap dealer or U.S. MSP acting through its foreign branch or a non-U.S. person that is a guaranteed or conduit affiliate, and on the other hand, a non-U.S. swap dealer, non-U.S. MSP or other non-U.S. person.

With respect to the clearing requirement, the Commission has previously addressed both the scope and process of a comparability determination, which also would apply to the extent that substituted compliance is applicable under this Guidance.[610]

---

[608] In addition to the End-User Exception under CEA section 2(h)(7), which is codified in Commission regulation 50.50, as noted above, the Commission has adopted an exemption from required clearing for swaps between certain affiliated entities, codified at Commission regulation 50.52. See Inter-Affiliate Exemption, 78 FR 21750.

[609] Id. at 21765 (requiring, among other conditions, that eligible affiliate counterparties electing the exemption from clearing for the inter-affiliate swap must clear their swaps with unaffiliated counterparties, and permitting eligible affiliate counterparties located in foreign jurisdictions to clear such swaps pursuant to their applicable foreign jurisdictions' clearing regime, if the Commission determines that such regime is comparable and comprehensive to the U.S. clearing mandate).

[610] In particular, in the Inter-Affiliate Exemption, the Commission permitted eligible affiliate counterparties located outside of the U.S. to comply with a condition of the exemption to clear their swaps with unaffiliated counterparties (not located in the U.S.), to the extent such swaps are subject to the clearing requirement under section 2(h)(1) of the CEA, by complying with the requirements of a foreign jurisdiction's clearing mandate, including any exception or exemption granted under the foreign clearing mandate, provided that the Commission determines that: (i) such foreign jurisdiction's clearing mandate is comparable and comprehensive, but not necessarily identical, to the clearing requirement established under the CEA and part 50 of the Commission's regulations, and (ii) the exception

As for the process for determining comparability of a foreign jurisdiction's clearing mandate, the Commission has also previously stated that it will review the comparability and comprehensiveness of a foreign jurisdiction's clearing mandate by reviewing: (i) the foreign jurisdiction's laws and regulations with respect to its mandatory clearing regime (i.e., jurisdiction-specific review) and (ii) the foreign jurisdiction's clearing determinations with respect to each class of swaps for which the Commission has issued a clearing determination under Commission regulation 50.4 (i.e., product-specific review).[611] In determining whether an exemption or exception under a comparable foreign mandate is comparable to an exception or exemption under the CEA or part 50, the Commission anticipates that it would review, for comparability purposes, the foreign jurisdiction's laws and regulations with respect to its mandatory clearing regime, as well as the relevant exception or exemption, and would exercise broad discretion to determine whether the requirements and objectives of such exemption are consistent with those under the comparable foreign clearing regime.

The Commission is also of the view that where a swap is executed anonymously on a registered DCM or SEF between two non-registrants and cleared by a registered DCO, and one (or both) of the counterparties to the swap is a U.S. person, neither party to the swap should be required to comply with the Non-Registrant Requirements that otherwise apply to the swap, with

---

or exemption is determined to be comparable to an exception or exemption provided under the CEA or part 50 of the Commission's regulations. See 17 CFR 50.52(b)(4)(i).

[611] The Commission further explained that comparability will not require a regime identical to the clearing framework established under the CEA and the Commission regulations. Rather, the Commission anticipates that it will make jurisdiction-specific comparability determinations by comparing the regulatory requirements of a foreign jurisdiction's clearing regime with the requirements and objectives of the Dodd-Frank Act. The Commission further noted that it anticipates that the product-specific comparability determination will necessarily be made on the basis of whether the applicable swap is included in a class of swaps covered under Commission regulation 50.4.

the exception of Large Trader Reporting,[612] SDR Reporting, and swap data recordkeeping.[613] The Commission notes that in this case, the DCM or SEF will fulfill the required clearing, trade execution,[614] and real-time public reporting requirements that apply to the swap.

Further, the Commission is of the view that where a swap is executed anonymously between two non-registrants on a registered FBOT and cleared and one (or both) of the counterparties to the swap is a U.S. person, neither party to the swap (as is the case when the swap is executed anonymously on a DCM) should be required to comply with the Non-Registrant Requirements that otherwise apply to the swap, with the exception of Large Trader Reporting, SDR Reporting and swap data recordkeeping. The Commission notes that in this case, the registered FBOT, as would the DCM, will fulfill the required clearing and trade

---

[612] The Commission's part 20 regulations set forth large trader reporting rules for physical commodity swaps. See 76 FF 43851 (Jul. 22, 2011). Part 20 requires routine swaps position reports from clearing organizations, clearing members and swap dealers, and establishes certain non-routine reporting requirements for large swaps traders. Among other things, part 20 requires that a reporting entity, as defined in Commission regulation 20.1, disclose the identity of the counterparty in respect of which positional information is being reported in large swap trader reports and associated filings. See 76 FR. 43851 at 43863-4 n.11.

[613]The Dodd Frank Act added to the CEA provisions requiring the retention and reporting of data related to swap transactions. Section 727 of the Dodd Frank Act added section 2(a)(13)(g), which requires that all swaps, whether cleared or uncleared, be reported to an SDR. Section 728 of the Dodd-Frank Act added section 21(b), which directs the Commission to prescribe standards for swap data recordkeeping and reporting. Section 723 of the Dodd-Frank Act added section 2(h)(5), which addresses the reporting of swap data for swaps executed before the enactment of the Dodd-Frank Act and swaps executed on or after the date of its enactment. The Commission's swap data reporting and recordkeeping requirements are found in part 45, which establishes swap data recordkeeping and SDR reporting requirements; and part 46, which establishes swap data recordkeeping and SDR reporting requirements for pre-enactment and transition swaps (collectively, "historical swaps"). See 77 FR 2136 (Jan. 13, 2012) (part 45); 77 FR 35200 (June 12, 2012) (part 46). Under both part 45 and part 46 (collectively, the "swap data reporting rules") reporting parties have swap data reporting obligations. The swap data reporting rules further prescribe certain data fields that must be included in swap data reporting. See Appendix 1 to part 45; Appendix 1 to part 46. For all swaps subject to the Commission's jurisdiction, each counterparty must be identified by means of a single legal entity identifier ("LEI") in all swap data reporting pursuant to parts 45 and 46. A reporting counterparty, as defined in Commission regulations 45.1 and 46.1, respectively, has obligations that include providing certain data to the SDR relating to the primary economic terms ("PET") of the swap, including the LEI of the non-reporting counterparty.

[614] The Commission clarifies that the trading mandate under CEA section 2(h)(8)(A) is satisfied by trading on a registered DCM or SEF or a SEF that is exempt from registration.

execution requirements[615] that apply to the swap but not, without further action, the real-time public reporting requirements.

The Commission expects that derivatives markets and regulatory regimes will continue to evolve in the future. In order to ensure a level playing field, promote participation in transparent markets, and promote market efficiency, the Commission will, through staff no action letters, extend appropriate time-limited transitional relief to certain European Union-regulated multilateral trading facilities (MTFs), in the event that the Commission's trade execution requirement is triggered before March 15, 2014. Such relief would be available through March 15th for MTFs that have multilateral trading schemes, a sufficient level of pre- and post-trade price transparency, non-discriminatory access by market participants, and an appropriate level of oversight. In addition, the Commission will consult with the European Commission in giving consideration to extending regulatory relief to European Union-regulated trading platforms that are subject to requirements that achieve regulatory outcomes that are comparable to those achieved by the requirements for SEFs. Both parties will assess progress in January 2014.

### 2. Swaps between Non-Registrants that are Both Non-U.S. Persons

As noted above, where a swap is between two non-U.S. persons and neither counterparty is required to register as a swap dealer or MSP, the Commission proposed interpreting CEA section 2(i) so as not to apply the Non-Registrant Requirements,[616] with the exception of Large Trader Reporting.[617]

---

[615] The Commission clarifies that the trading mandate under CEA section 2(h)(8)(A) is satisfied by trading on a registered FBOT.

[616] See the Proposed Guidance, 77 FR at 41234-35.

[617] See id. at 41234 n. 139, 41235.

Section a discusses the Commission's policy on application of Large Trader Reporting to swaps between two non-registrants that are not U.S. persons. Section b discusses the application of the other Non-Registrant Requirements to swaps between two non-registrants that are not U.S. persons, where each of the counterparties to the swap is a guaranteed or conduit affiliate, and the availability of substituted compliance for the parties to such swaps. Section c discusses the Commission's policy on application of the Non-Registrant Requirements other than Large Trader Reporting to swaps between non-registrants that are not U.S. persons where neither or only one of the counterparties is a guaranteed or conduit affiliate.

**a. Large Trader Reporting**

Large Trader Reporting requires routine positional reports from clearing members in addition to clearing organizations and swap dealers. As is the case with swap dealers, routine reports are required from clearing members to the extent that they hold significant positions in the swaps subject to Large Trader Reporting – swaps that are directly or indirectly linked to specified U.S.-listed physical commodity futures contracts. Routine reporting provides essential visibility into the trading activity of large market participants, which enables the Commission to conduct effective surveillance of markets in swaps and futures that have been determined to be economically equivalent. Given the linkage of the swaps covered by Large Trader Reporting to U.S. futures markets, the Commission believes that any non-U.S. clearing member that holds positions in such swaps that are significant enough to trigger routine reporting obligations is engaged in activities that have a direct and significant connection with activities in, or effect on, commerce of the United States. Consistent with the Proposed Guidance, the Commission's

policy, in light of its interpretation of CEA section 2(i), is that any such non-U.S. clearing member should report all reportable positions to the Commission.[618]

Large Trader Reporting also establishes recordkeeping requirements for traders with significant positions in the covered physical commodity swaps. Given the vital role that Large Trader Reporting plays in ensuring that the Commission has access to comprehensive data regarding trading activity in swaps linked to U.S. futures, the Commission's policy, in light of its interpretation of CEA section 2(i), is that non-U.S. persons with positions that meet the prescribed recordkeeping thresholds should comply with the prescribed recordkeeping requirements. The Commission notes that traders, which are not swap dealers or clearing members with routine Large Trader Reporting obligations, may generally keep books and records regarding their transactions in the covered physical commodity swaps and produce them for inspection by the Commission in the record retention format that such traders have developed in the normal course of their business operations.

**b. Swaps Where Each of The Counterparties is Either a Guaranteed or Conduit Affiliate**

In contrast to the Proposed Guidance, where a swap is between two non-registrants that are not U.S. persons, and each of the counterparties to the swap is a guaranteed or conduit affiliate,[619] the parties to the swap generally should be expected to comply with the Non-Registrant Requirements with respect to the transaction. However, where at least one of the

---

[618] To the extent that they transact in the physical commodity swaps covered by the Commission's Large Trader Reporting rules, non-U.S. clearing members also should maintain the records required by such rules.

[619] As noted above, this Guidance uses the term "guaranteed or conduit affiliate" to refer to a non-U.S. person that is guaranteed by a U.S. person or that is an affiliate conduit.

parties to the swap is an "affiliate conduit," the Commission would generally expect the parties to the swap only to comply with (to the extent that the Inter-Affiliate Exemption is elected), the conditions of the Inter-Affiliate Exemption, including the treatment of outward-facing swaps condition in Commission regulation 50.52(b)(4)(i). In addition, the part 43 real-time reporting requirements must be satisfied.

The Commission has not interpreted CEA section 2(i) so as to include a guaranteed or conduit affiliate in the interpretation of the term "U.S. person" solely because of the guarantee or affiliation. Where each of the counterparties to the swap are non-registrants that are guaranteed or conduit affiliates, the Commission believes that the risks to U.S. persons and to the U.S. financial system sufficiently increase so that the additional measure of applying the Non-Registrant Requirements to the swap is warranted (but with substituted compliance available, to the extent applicable).[620] The Commission notes that in the case of guarantees by U.S. persons, if there is a default by the non-U.S. person, the U.S. guarantor generally would be held responsible to settle the obligations. In the case of affiliate conduits, a non-U.S. affiliate could effectively operate as a conduit for the U.S. person, and could be used to execute swaps with counterparties in foreign jurisdictions, outside the Dodd-Frank Act regulatory regime.

Therefore, where a swap is between two non-registrants that are guaranteed or conduit affiliates, the Commission believes that the swap has a "direct and significant connection with activities in, or effect on, commerce of the United States" within the meaning of CEA section 2(i) so that certain Entity-Level and Transaction-Level Requirements would apply to the swap

---

[620] The Commission proposed to interpret section 2(i) so that the Non-Registrant Requirements would not apply to swaps between two non-registrants (whether or not one or more counterparties was guaranteed by a U.S. person), with the exception of Large Trader Reporting. The Commission noted in the Proposed Guidance that it intended to review the issue of affiliate conduits. See Proposed Guidance, 77 FR at 41234-35.

counterparties. Consistent with section 2(i), however, the Commission's policy generally is to make the parties to the swap eligible for substituted compliance (except with regard to Large Trader Reporting, and provided that SDR Reporting would be eligible for substituted compliance only if the Commission has direct access to all of the reported swap data elements that are stored at a foreign trade repository).

#### c. Swaps Where Neither or Only One of the Parties is a Guaranteed or Conduit Affiliate

With respect to swaps between two non-registrants where neither or only one party is a guaranteed or conduit affiliate, the Commission's policy is that the parties to the swap generally should not be expected to comply with the Non-Registrant Requirements, except as described below.

As discussed above, where a counterparty to a swap is a guaranteed or conduit affiliate, the risks to U.S. persons and to the U.S. financial system increase. In the case of guarantees by U.S. persons, if there is a default by the non-U.S. person, the U.S. guarantor would be held responsible to settle the obligations. In the case of affiliate conduits, a non-U.S. affiliate could effectively operate as a "conduit" for the U.S. person, and could be used to execute swaps with counterparties in foreign jurisdictions, outside the Dodd-Frank Act regulatory regime. Nevertheless, the Commission also recognizes that foreign jurisdictions may have an interest in regulating swaps between two non-registrants where both counterparties to the swap are non-U.S. persons. Therefore, consistent with international comity principles, the Commission would generally expect the parties to the swap only to comply with (to the extent that the Inter-Affiliate Exemption is elected), the conditions of the Inter-Affiliate Exemption, including the treatment of outward-facing swaps condition in Commission regulation 50.52(b)(4)(i), and Large Trader

Reporting. The Commission believes that this policy strikes the right balance between U.S. interests in regulating such a swap and the interest of foreign regulators.

## V. Appendix A – The Entity-Level Requirements

### A. First Category of Entity-Level Requirements

The First Category of Entity-Level Requirements includes capital adequacy, chief compliance officer, risk management, and swap data recordkeeping (except certain aspects of swap data recordkeeping relating to complaints and sales materials).

#### 1. Capital adequacy

Section 4s(e)(2)(B) of the CEA specifically directs the Commission to set capital requirements for swap dealers and MSPs that are not subject to the capital requirements of U.S. prudential regulators (hereinafter referred to as "non-bank swap dealers or MSPs").[621] With respect to the use of swaps that are not cleared, these requirements must: "(1) [h]elp ensure the safety and soundness of the swap dealer or major swap participant; and (2) [be] appropriate for the risk associated with the non-cleared swaps held as a swap dealer or major swap

---

[621] See 7 U.S.C. 6s(e)(2)(B). Section 4s(e) of the CEA explicitly requires the adoption of rules establishing capital and margin requirements for swap dealers and MSPs, and applies a bifurcated approach that requires each swap dealer and MSP for which there is a U.S. prudential regulator to meet the capital and margin requirements established by the applicable prudential regulator, and each swap dealer and MSP for which there is no prudential regulator to comply with the Commission's capital and margin regulations. See 7 U.S.C. 6s(e). Further, systemically important financial institutions ("SIFIs") that are not FCMs would be exempt from the Commission's capital requirements, and would comply instead with Federal Reserve Board requirements applicable to SIFIs, while nonbank (and non-FCM) subsidiaries of U.S. bank holding companies would calculate their Commission capital requirement using the same methodology specified in Federal Reserve Board regulations applicable to the bank holding company, as if the subsidiary itself were a bank holding company. The term "prudential regulator" is defined in CEA section 1a(39) as the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Farm Credit Administration, and the Federal Housing Finance Agency. See 7 U.S.C. 1a(39). In addition, in the proposed capital regulations for swap dealers and MSPs, the Commission solicited comment regarding whether it would be appropriate to permit swap dealers and MSPs to use internal models for computing market risk and counterparty credit risk charges for capital purposes if such models had been approved by a foreign regulatory authority and were subject to periodic assessment by such foreign regulatory authority. See Proposed Capital Requirements, 76 FR 27802.

participant."[622] Pursuant to section 4s(e)(3), the Commission proposed regulations, which would require non-bank swap dealers and MSPs to hold a minimum level of adjusted net capital (i.e., "regulatory capital") based on whether the non-bank swap dealer or MSP is: (i) also a FCM; (ii) not an FCM, but is a non-bank subsidiary of a bank holding company; or (iii) neither an FCM nor a non-bank subsidiary of a bank holding company.[623] The primary purpose of the capital requirement is to reduce the likelihood and cost of a swap dealer's or MSP's default by requiring a financial cushion that can absorb losses in the event of the firm's default.

2. **Chief compliance officer**

Section 4s(k) requires that each swap dealer and MSP designate an individual to serve as its chief compliance officer ("CCO") and specifies certain duties of the CCO.[624] Pursuant to section 4s(k), the Commission adopted regulation 3.3, which requires swap dealers and MSPs to designate a CCO who would be responsible for administering the firm's compliance policies and procedures, reporting directly to the board of directors or a senior officer of the swap dealer or MSP, as well as preparing and filing with the Commission a certified report of compliance with the CEA. The chief compliance function is an integral element of a firm's risk management and

---

[622] See 7 U.S.C. 6s(e)(3)(A).

[623] See 7 U.S.C. 6s(e). See also Proposed Capital Requirements, 76 FR 27802. "The Commission's capital proposal for [swap dealers] and MSPs includes a minimum dollar level of $20 million. A non-bank [swap dealer] or MSP that is part of a U.S. bank holding company would be required to maintain a minimum of $20 million of Tier 1 capital as measured under the capital rules of the Federal Reserve Board. [A swap dealer] or MSP that also is registered as an FCM would be required to maintain a minimum of $20 million of adjusted net capital as defined under [proposed] section 1.17. In addition, an [swap dealer] or MSP that is not part of a U.S. bank holding company or registered as an FCM would be required to maintain a minimum of $20 million of tangible net equity, plus the amount of the [swap dealer's] or MSP's market risk exposure and OTC counterparty credit risk exposure." See id. at 27817.

[624] See 7 U.S.C. 6s(k).

oversight and the Commission's effort to foster a strong culture of compliance within swap dealers and MSPs.

### 3. **Risk management**

Section 4s(j) of the CEA requires each swap dealer and MSP to establish internal policies and procedures designed to, among other things, address risk management, monitor compliance with position limits, prevent conflicts of interest, and promote diligent supervision, as well as maintain business continuity and disaster recovery programs.[625] The Commission adopted implementing regulations (23.600, 23.601, 23.602, 23.603, 23.605, and 23.606).[626] The Commission also adopted regulation 23.609, which requires certain risk management procedures for swap dealers or MSPs that are clearing members of a derivatives clearing organization ("DCO").[627] Collectively, these requirements help to establish a robust and comprehensive internal risk management program for swap dealers and MSPs, which is critical to effective systemic risk management for the overall swaps market.

---

[625] 7 U.S.C. 6s(j).

[626] See Final Swap Dealer and MSP Recordkeeping Rule, 77 FR 20128 (relating to risk management program, monitoring of position limits, business continuity and disaster recovery, conflicts of interest policies and procedures, and general information availability, respectively).

[627] Customer Documentation Rule, 77 FR 21278. Also, swap dealers must comply with Commission regulation 23.608, which prohibits swap dealers providing clearing services to customers from entering into agreements that would: (i) disclose the identity of a customer's original executing counterparty; (ii) limit the number of counterparties a customer may trade with; (iii) impose counterparty-based position limits; (iv) impair a customer's access to execution of a trade on terms that have a reasonable relationship to the best terms available; or (v) prevent compliance with specified time frames for acceptance of trades into clearing.

i. Swap data recordkeeping (except certain aspects of swap data recordkeeping relating to complaints and sales materials)

CEA section 4s(f)(1)(B) requires swap dealers and MSPs to keep books and records for all activities related to their business.[628] Sections 4s(g)(1) and (4) require swap dealers and MSPs to maintain trading records for each swap and all related records, as well as a complete audit trail for comprehensive trade reconstructions.[629] Pursuant to these provisions, the Commission adopted regulations 23.201and 23.203, which require swap dealers and MSPs to keep records including complete transaction and position information for all swap activities, including documentation on which trade information is originally recorded. Pursuant to regulation 23.203, records of swaps must be maintained for the duration of the swap plus 5 years, and voice recordings for 1 year, and records must be "readily accessible" for the first 2 years of the 5 year retention period. Swap dealers and MSPs also must comply with Parts 43, 45 and 46 of the Commission's regulations, which, respectively, address the data recordkeeping and reporting requirements for all swaps subject to the Commission's jurisdiction, including swaps entered into before the date of enactment of the Dodd-Frank Act ("pre-enactment swaps") and swaps entered into on or after the date of enactment of the Dodd-Frank Act but prior to the compliance date of the swap data reporting rules ("transition swaps").[630]

---

[628] 7 U.S.C. 6s(f)(1)(B).

[629] 7 U.S.C. 6s(g)(1).

[630] 17 CFR 46.1 et seq.; Proposed Data Rules, 76 FR 22833.

### B. Second Category of Entity-Level Requirements

The Second Category of Entity-Level Requirements includes SDR Reporting, certain aspects of swap data recordkeeping relating to complaints and marketing and sales materials under Commission regulations 23.201(b)(3) and 23.201(b)(4) and Large Trader Reporting.

#### 1. SDR Reporting

CEA section 2(a)(13)(G) requires all swaps, whether cleared or uncleared, to be reported to a registered SDR.[631] CEA section 21 requires SDRs to collect and maintain data related to swaps as prescribed by the Commission, and to make such data electronically available to particular regulators under specified conditions related to confidentiality.[632] Part 45 of the Commission's regulations (and Appendix 1 thereto) sets forth the specific swap data that must be reported to a registered SDR, along with attendant recordkeeping requirements; and part 46 addresses recordkeeping and reporting requirements for pre-enactment and transition swaps ("historical swaps"). The fundamental goal of the part 45 rules is to ensure that complete data concerning all swaps subject to the Commission's jurisdiction is maintained in SDRs where it will be available to the Commission and other financial regulators for fulfillment of their various regulatory mandates, including systemic risk mitigation, market monitoring and market abuse prevention. Part 46 supports similar goals with respect to pre-enactment and transition swaps and ensures that data needed by regulators concerning "historical" swaps is available to regulators through SDRs. Among other things, data reported to SDRs will enhance the Commission's understanding of concentrations of risks within the market, as well as promote a

---

[631] 7 U.S.C. 2(a)(13)(G).

[632] 7 U.S.C. 24a.

more effective monitoring of risk profiles of market participants in the swaps market. The Commission also believes that there are benefits that will accrue to swap dealers and MSPs as a result of the timely reporting of comprehensive swap transaction data and consistent data standards for recordkeeping, among other things. Such benefits include more robust risk monitoring and management capabilities for swap dealers and MSPs, which in turn will improve the monitoring of their current swaps market positions.

### 2. Swap data recordkeeping relating to complaints and marketing and sales materials

CEA section 4s(f)(1) requires swap dealers and MSPs to "make such reports as are required by the Commission by rule or regulation regarding the transactions and positions and financial condition of the registered swap dealer or major swap participant."[633] Additionally, CEA section 4s(h) requires swap dealers and MSPs to "conform with such business conduct standards … as may be prescribed by the Commission by rule or regulation."[634] Pursuant to those authorities, the Commission promulgated final rules that set forth certain reporting and recordkeeping for swap dealers and MSPs.[635] Commission Regulation 23.201 states that "[e]ach swap dealer and major swap participant shall keep full, complete, and systematic records of all activities related to its business as a swap dealer or major swap participant." Such records must include, among other things, "[a] record of each complaint received by the swap dealer or major

---

[633] 7 U.S.C. 6s(f)(1).

[634] 7 U.S.C. 6s(h)(1). See 7 U.S.C. 6s(h)(3).

[635] Final Swap Dealer and MSP Recordkeeping Rule, 77 FR 20128.

swap participant concerning any partner, member, officer, employee, or agent,"[636] as well as "[a]ll marketing and sales presentations, advertisements, literature, and communications."[637]

### 3. Physical commodity large swaps trader reporting (Large Trader Reporting)

CEA section 4t[638] authorizes the Commission to establish a large trader reporting system for significant price discovery swaps (of which the economically equivalent swaps subject to the Commission's part 20 rules are a subset). Pursuant thereto, the Commission adopted its Large Trader Reporting rules (part 20 of the Commission regulations), which require routine reports from swap dealers, among other entities, that hold significant positions in swaps that are linked, directly or indirectly, to a prescribed list of U.S.-listed physical commodity futures contracts.[639] Additionally, Large Trader Reporting requires that swap dealers, among other entities, comply with certain recordkeeping obligations.

---

[636] 17 CFR 23.201(b)(3)(i).

[637] 17 CFR 23.201(b)(4).

[638] 7 U.S.C. 6t.

[639] Large Trader Reporting for Physical Commodity Swaps, 76 FR 43851. The rules require routine position reporting by clearing organizations, as well as clearing members and swap dealers with reportable positions in the covered physical commodity swaps. The rules also establish recordkeeping requirements for clearing organizations, clearing members and swap dealers, as well as traders with positions in the covered physical commodity swaps that exceed a prescribed threshold. In general, the rules apply to swaps that are linked, directly or indirectly, to either the price of any of the 46 U.S.-listed physical commodity futures contracts the Commission enumerates (Covered Futures Contracts) or the price of the physical commodity at the delivery location of any of the Covered Futures Contracts.

## VI. Appendix B – The Transaction-Level Requirements

The Transaction-Level Requirements cover a range of Dodd-Frank requirements: some of the requirements more directly address financial protection of swap dealers (or MSPs) and their counterparties; others address more directly market efficiency and/or price discovery. Further, some of the Transaction-Level Requirements can be classified as Entity-Level Requirements and applied on a firm-wide basis across all swaps or activities. Nevertheless, in the interest of comity principles, the Commission believes that the Transaction-Level Requirements may be applied on a transaction-by-transaction basis.

### A. Category A: Risk Mitigation and Transparency

#### 1. Required clearing and swap processing

Section 2(h)(1) of the CEA requires a swap to be submitted for clearing to a DCO if the Commission has determined that the swap is required to be cleared, unless one of the parties to the swap is eligible for an exception from the clearing requirement and elects not to clear the swap.[640] Clearing via a DCO mitigates the counterparty credit risk between swap dealers or MSPs and their counterparties.

Commission regulations implementing the first designations of swaps for required clearing were published in the Federal Register on December 13, 2012.[641] Under Commission regulation 50.2, all persons executing a swap that is included in a class of swaps identified under Commission regulation 50.4 must submit such swap to an eligible derivatives clearing

---

[640] 7 U.S.C. 2(h)(1), (7).

[641] 77 FR 72284.

organization (DCO) for clearing as soon as technologically practicable after clearing, but in any event by the end of the day of execution.

Regulation 50.4 establishes required clearing for certain classes of swaps. Currently, those classes include, for credit default swaps: specified series of untranched North American CDX indices and European iTraxx indices; and for interest rate swaps: fixed-to-floating swaps, basis swaps, forward rate agreements referencing U.S. Dollar, Euro, Sterling, and Yen, and overnight index swaps referencing U.S. Dollar, Euro, and Sterling. Each of the six classes is further defined in Commission regulation 50.4. Swaps that have the specifications identified in the regulation are required to be cleared and must be cleared pursuant to the rules of any eligible DCO unless an exception or exemption specified in the CEA or the Commission's regulations applies.

Generally, if a swap is subject to Section 2(h)(1)(A) of the CEA and part 50 of the Commission's regulations, it must be cleared through an eligible DCO, unless: (i) one of the counterparties is eligible for and elects the End-User Exception under Commission regulation 50.50;[642] or (ii) both counterparties are eligible for and elect an Inter-Affiliate Exemption under Commission regulation 50.52. To elect either the end-user exception or the Inter-Affiliate Exemption, the electing party or parties and the swap must meet certain requirements set forth in the regulations.

Closely connected with the clearing requirement are the following swap processing requirements: (i) Commission regulation 23.506, which requires swap dealers and MSPs to submit swaps promptly for clearing; and (ii) Commission regulations 23.610 and 39.12, which

---

[642] See End-User Exception to the Clearing Requirement for Swaps, 77 FR 42560 (Jul. 19, 2012).

establish certain standards for swap processing by DCOs and/or swap dealers and MSPs that are clearing members of a DCO.[643] Together, required clearing and swap processing requirements promote safety and soundness of swap dealers and MSPs, and mitigate the credit risk posed by bilateral swaps between swap dealers or MSPs and their counterparties.[644]

### 2. Margin and segregation requirements for uncleared swaps

Section 4s(e) of the CEA requires the Commission to set margin requirements for swap dealers and MSPs that trade in swaps that are not cleared.[645] The margin requirements ensure that outstanding current and potential future risk exposures between swap dealers and their counterparties are collateralized, thereby reducing the possibility that swap dealers or MSPs take on excessive risks without having adequate financial backing to fulfill their obligations under the uncleared swap. In addition, with respect to swaps that are not submitted for clearing, section 4s(l) requires that a swap dealer or MSP notify the counterparty of its right to request that funds provided as margin be segregated, and upon such request, to segregate the funds with a third-party custodian for the benefit of the counterparty. In this way, the segregation requirement enhances the protections offered through margining uncleared swaps and thereby provides additional financial protection to counterparties. The Commission is working with foreign and

---

[643] See Final Customer Documentation Rules, 77 FR 21278.

[644] See section IV.H, supra, regarding the application of required clearing rules to market participants that are not registered as swap dealers or MSPs, including the circumstances under which the parties to such swaps would be eligible for substituted compliance.

[645] See 7 U.S.C. 6s(e). See also Proposed Margin Requirements, 76 FR at 23733-40. Section 4s(e) explicitly requires the adoption of rules establishing margin requirements for swap dealers and MSPs, and applies a bifurcated approach that requires each swap dealer and MSP for which there is a prudential regulator to meet the margin requirements established by the applicable prudential regulator, and each swap dealer and MSP for which there is no prudential regulator to comply with the Commission's margin regulations. In contrast, the segregation requirements in section 4s(1) do not use a bifurcated approach – that is, all swap dealers and MSPs are subject to the Commission's rule regarding notice and third party custodians for margin collected for uncleared swaps.

domestic regulators to develop and finalize appropriate regulations for margin and segregation requirements.

### 3. Trade execution

Integrally linked to the clearing requirement is the trade execution requirement, which is intended to bring the trading of mandatorily cleared swaps that are made available to trade onto regulated exchanges or execution facilities. Specifically, section 2(h)(8) of the CEA provides that unless a clearing exception applies and is elected, a swap that is subject to a clearing requirement must be executed on a DCM or SEF, unless no such DCM or SEF makes the swap available to trade.[646] Commission regulations implementing the process for a DCM or SEF to make a swap available to trade were published in the Federal Register on June 4, 2013.[647] Under Commission regulations 37.10 and 38.12, respectively, a SEF or DCM may submit a determination for Commission review that a mandatorily cleared swap is available to trade based on enumerated factors. By requiring the trades of mandatorily cleared swaps that are made available to trade to be executed on an exchange or an execution facility – each with its attendant pre- and post-trade transparency and safeguards to ensure market integrity – the trade execution requirement furthers the statutory goals of financial stability, market efficiency, and enhanced transparency.

### 4. Swap trading relationship documentation

CEA section 4s(i) requires each swap dealer and MSP to conform to Commission standards for the timely and accurate confirmation, processing, netting, documentation and

---

[646] See 7 U.S.C. 2(h)(8).

[647] 78 FR 33606.

valuation of swaps.[648] Pursuant thereto, Commission regulation 23.504(a) requires swap dealers and MSPs to "establish, maintain and enforce written policies and procedures" to ensure that the swap dealer or MSP executes written swap trading relationship documentation.[649] Under Commission regulation 23.504, the swap trading relationship documentation must include, among other things: all terms governing the trading relationship between the swap dealer or MSP and its counterparty; credit support arrangements; investment and re-hypothecation terms for assets used as margin for uncleared swaps; and custodial arrangements.[650] Further, the swap trading relationship documentation requirement applies to all swaps with registered swap dealers and MSPs. In addition, Commission regulation 23.505 requires swap dealers and MSPs to document certain information in connection with swaps for which exceptions from required clearing are elected.[651] A robust swap documentation standard may promote standardization of documents and transactions, which are key conditions for central clearing, and lead to other operational efficiencies, including improved valuation and risk management.

5. **Portfolio reconciliation and compression**

CEA section 4s(i) directs the Commission to prescribe regulations for the timely and accurate processing and netting of all swaps entered into by swap dealers and MSPs. Pursuant to CEA section 4s(i), the Commission adopted regulations (23.502 and 23.503), which require swap dealers and MSPs to perform portfolio reconciliation and compression, respectively, for all

---

[648] See 7 U.S.C. 6s(i).

[649] See Final Confirmation Rules, 77 FR 55904.

[650] The requirements under section 4s(i) relating to trade confirmations is a Transaction-Level Requirement. Accordingly, Commission regulation 23.504(b)(2) requires a swap dealer's and MSP's swap trading relationship documentation to include all confirmations of swaps, will apply on a transaction-by-transaction basis.

[651] See Final Confirmation Rules, 77 FR at 55964.

swaps.[652] Portfolio reconciliation is a post-execution risk management tool to ensure accurate confirmation of a swap's terms and to identify and resolve any discrepancies between counterparties regarding the valuation of the swap. Portfolio compression is a post-trade processing and netting mechanism that is intended to ensure timely, accurate processing and netting of swaps.[653] Regulation 23.503 requires all swap dealers and MSPs to participate in bilateral compression exercises and/or multilateral portfolio compression exercises conducted by a third party.[654] The rule also requires policies and procedures for engaging in such exercises for uncleared swaps with non-swap dealers and non-MSPs upon request. Further, participation in multilateral portfolio compression exercises is mandatory for dealer-to-dealer trades.

6. **Real-time public reporting**

Section 2(a)(13) of the CEA also directs the Commission to promulgate rules providing for the public availability of swap transaction and pricing data on a real-time basis.[655] In accordance with this mandate, the Commission promulgated part 43 of its regulations, which provide that all "publicly reportable swap transactions" must be reported and publicly disseminated, and which establish the method, manner, timing and particular transaction and pricing data that must be reported by parties to a swap transaction.[656] The real-time

---

[652] See id.

[653] For example, the reduced transaction count may decrease operational risk as there are fewer trades to maintain, process, and settle.

[654] See 17 CFR 23.503(c); Confirmation NPRM, 75 FR 81519.

[655] See 7 U.S.C. 2(a)(13). See also Real-Time Reporting Rule, 77 FR at 1183.

[656] Part 43 defines a "publicly reportable swap transaction" as: (i) any swap that is an arm's-length transaction between two parties that results in a corresponding change in the market risk position between the two parties; or (ii) any termination, assignment, novation, exchange, transfer, amendment, conveyance, or extinguishing of rights or obligations of a swap that changes the pricing of a swap. See Real-Time Reporting Rule, 77 FR 1182. Additionally, the Commission adopted regulation 23.205, which directs swap dealers and MSPs to undertake such reporting and to

dissemination of swap transaction and pricing data supports the fairness and efficiency of markets and increases transparency, which in turn improves price discovery and decreases risk (e.g., liquidity risk).[657]

### 7. Trade confirmation

Section 4s(i) of the CEA[658] requires that each swap dealer and MSP must comply with the Commission's regulations prescribing timely and accurate confirmation of swaps. The Commission has adopted regulation 23.501, which requires, among other things, a timely and accurate confirmation of swap transactions (which includes execution, termination, assignment, novation, exchange, transfer, amendment, conveyance, or extinguishing of rights or obligations of a swap) among SDs and MSPs by the end of the first business day following the day of execution.[659] Timely and accurate confirmation of swaps – together with portfolio reconciliation and compression – are important post-trade processing mechanisms for reducing risks and improving operational efficiency.[660]

### 8. Daily trading records

Pursuant to section CEA 4s(g), the Commission adopted regulation 23.202, which requires swap dealers and MSPs to maintain daily trading records, including records of trade information related to pre-execution, execution, and post-execution data that is needed to

---

have the electronic systems and procedures necessary to transmit electronically all information and data required to be reported in accordance with part 43. See Final Swap Dealer and MSP Recordkeeping Rule, 77 FR at 20205.

[657] See Real-Time Reporting Rule, 77 FR at 1183.

[658] 7 U.S.C. 6s(i).

[659] See Final Confirmation Rules, 77 FR 55904.

[660] In addition, the Commission notes that regulation 23.504(b)(2) requires that the swap trading relationship documentation of swap dealers and MSPs must include all confirmations of swap transactions.

conduct a comprehensive and accurate trade reconstruction for each swap. The final rule also requires that records be kept of cash or forward transactions used to hedge, mitigate the risk of, or offset any swap held by the swap dealer or MSP.[661] Accurate and timely recordkeeping regarding all phases of a swap transaction can serve to greatly enhance a firm's internal supervision, as well as the Commission's ability to detect and address market or regulatory abuses or evasion.

### B. Category B: External Business Conduct Standards

Pursuant to CEA section 4s(h), the Commission has adopted external business conduct rules, which establish business conduct standards governing the conduct of swap dealers and MSPs in dealing with their counterparties in entering into swaps.[662] Broadly speaking, these rules are designed to enhance counterparty protection by significantly expanding the obligations of swap dealers and MSPs towards their counterparties. Under these rules, swap dealers and MSPs will be required, among other things, to conduct due diligence on their counterparties to verify eligibility to trade, provide disclosure of material information about the swap to their counterparties, provide a daily mid-market mark for uncleared swaps and, when recommending a swap to a counterparty, make a determination as to the suitability of the swap for the counterparty based on reasonable diligence concerning the counterparty.

---

[661] See Final Swap Dealer and MSP Recordkeeping Rule, 77 FR 20128.

[662] See 7 U.S.C. 6s(h). See also External Business Conduct Rules, 77 FR at 9822-29.

## VII. Appendix C – Application of the Entity-Level Requirements to Swap Dealers and MSPs*

| | |
|---|---|
| **U.S. Swap Dealer or MSP (including an affiliate of a non-U.S. person). Also applies when acting through a foreign branch.**[1] | Apply |
| **Non-U.S. Swap Dealer or MSP (including an affiliate of a U.S. person).** | First Category:[2] Substituted Compliance<br><br>Second Category:[3] Apply for U.S. counterparties; Substituted Compliance for SDR reporting with non-U.S. counterparties that are not guaranteed or conduit affiliates; Substituted compliance (except for Large Trader Reporting) with non-U.S. counterparties[4] |

***The Appendices to the Guidance should be read in conjunction with the rest of the Guidance.**

[1] Both Entity-Level and Transaction-Level Requirements are the ultimate responsibilities of the U.S.-based swap dealer or MSP.

[2] First Category is capital adequacy, Chief Compliance Officer, risk management, and swap data recordkeeping (except Commission regulations 23.201(b)(3) and (4)).

[3] Second Category is SDR Reporting, certain aspects of swap data recordkeeping relating to complaints and marketing and sales materials (Commission regulations 23.201(b)(3) and (4)), and Large Trader Reporting.

[4] Substituted compliance does not apply to Large Trader Reporting, i.e., non-U.S. persons that are subject to part 20 would comply with it in the same way that U.S. persons comply. With respect to the SDR Reporting requirement, the Commission may make substituted compliance available only if direct access to swap data stored at a foreign trade repository is provided to the Commission.

## VIII. Appendix D – Application of the Category A Transaction-Level Requirements to Swap Dealers and MSPs*

(Category A includes (1) Clearing and swap processing; (2) Margining and segregation for uncleared swaps; (3) Trade Execution; (4) Swap trading relationship documentation; (5) Portfolio reconciliation and compression; (6) Real-time public reporting; (7) Trade confirmation; and (8) Daily trading records).**

| | **U.S. Person (other than Foreign Branch of U.S. Bank that is a Swap Dealer or MSP)** | **Foreign Branch of U.S. Bank that is a Swap Dealer or MSP** | **Non-U.S. Person Guaranteed by, or Affiliate Conduit[1] of, a U.S. Person** | **Non-U.S. Person Not Guaranteed by, and Not an Affiliate Conduit[1] of, a U.S. Person** |
|---|---|---|---|---|
| **U.S. Swap Dealer or MSP (including an affiliate of a non-3U.S. person)** | Apply | Apply | Apply | Apply |
| **Foreign Branch of U.S. Bank that is a Swap Dealer or MSP** | Apply | Substituted Compliance | Substituted Compliance[2] | Substituted Compliance[2] |
| **Non-U.S. Swap Dealer or MSP (including an affiliate of a U.S. person)** | Apply | Substituted Compliance | Substituted Compliance | Do Not Apply |

*The Appendices to the Guidance should be read in conjunction with the rest of the Guidance.

** Where one of the counterparties is electing the Inter-Affiliate Exemption, the Commission would expect the parties to the swap to comply with the conditions of the Inter-Affiliate

Exemption, including the treatment of outward-facing swaps condition in Commission regulation 50.52(b)(4)(i).

[1] Factors that are relevant to the consideration of whether a non-U.S. person is an "affiliate conduit" include whether: (i) the non-U.S. person is majority-owned, directly or indirectly, by a U.S. person; (ii) the non-U.S. person controls, is controlled by, or is under common control with the U.S. person; (iii) the non-U.S. person, in the regular course of business, engages in swaps with non-U.S. third party(ies) for the purpose of hedging or mitigating risks faced by, or to take positions on behalf of, its U.S. affiliate(s), and enters into offsetting swaps or other arrangements with such U.S. affiliate(s) in order to transfer the risks and benefits of such swaps with third-party(ies) to its U.S. affiliates; and (iv) the financial results of the non-U.S. person are included in the consolidated financial statements of the U.S. person. Other facts and circumstances also may be relevant.

[2] Under a limited exception, where a swap between the foreign branch of a U.S. swap dealer or U.S. MSP and a non-U.S. person (that is not a guaranteed or conduit affiliate) takes place in a foreign jurisdiction other than Australia, Canada, the European Union, Hong Kong, Japan, or Switzerland, the counterparties generally may comply only with the transaction-level requirements in the foreign jurisdiction where the foreign branch is located if the aggregate notional value of all the swaps of the U.S. swap dealer's foreign branches in such countries does not exceed 5% of the aggregate notional value of all of the swaps of the U.S. swap dealer, and the U.S. person maintains records with supporting information for the 5% limit and to identify, define, and address any significant risk that may arise from the non-application of the Transaction-Level Requirements.

**Notes**:

[1] The swap trading relationship documentation requirement applies to all transactions with registered swap dealers and MSPs.

[2] Participation in multilateral portfolio compression exercises is mandatory for dealer to dealer trades.

## IX. Appendix E – Application of the Category B Transaction-Level Requirements to Swap Dealers and MSPs*

(Category B is External Business Conduct Standards).

| | **U.S. Person (other than Foreign Branch of U.S. Bank that is a Swap Dealer or MSP)** | **Foreign Branch of U.S. Bank that is a Swap Dealer or MSP** | **Non-U.S. Person Guaranteed by, or Affiliate Conduit[1] of, a U.S. Person** | **Non-U.S. Person Not Guaranteed by, and Not an Affiliate Conduit[1] of, a U.S. Person** |
|---|---|---|---|---|
| **U.S. Swap Dealer or MSP (including an affiliate of a non-U.S. person)** | Apply | Apply | Apply | Apply |
| **U.S. Swap Dealer or MSP (when it solicits and negotiates through a foreign subsidiary or affiliate)** | Apply | Do Not Apply | Do Not Apply | Do Not Apply |
| **Foreign Branch of U.S. Bank that is a Swap Dealer or MSP** | Apply | Do Not Apply | Do Not Apply | Do Not Apply |

| | | | | |
|---|---|---|---|---|
| **Non-U.S. Swap Dealer or MSP (including an affiliate of a U.S. person)** | Apply | Do Not Apply | Do Not Apply | Do Not Apply |

***The Appendices to the Guidance should be read in conjunction with the rest of the Guidance.**

[1] Factors that are relevant to the consideration of whether a non-U.S. person is an "affiliate conduit" include whether: (i) the non-U.S. person is majority-owned, directly or indirectly, by a U.S. person; (ii) the non-U.S. person controls, is controlled by, or is under common control with the U.S. person; (iii) the non-U.S. person, in the regular course of business, engages in swaps with non-U.S. third party(ies) for the purpose of hedging or mitigating risks faced by, or to take positions on behalf of, its U.S. affiliate(s), and enters into offsetting swaps or other arrangements with such U.S. affiliate(s) in order to transfer the risks and benefits of such swaps with third-party(ies) to its U.S. affiliates; and (iv) the financial results of the non-U.S. person are included in the consolidated financial statements of the U.S. person. Other facts and circumstances also may be relevant.

## X. Appendix F – Application of Certain Entity-Level and Transaction-Level Requirements to Non-Swap Dealer/Non-MSP Market Participants*

(The relevant Dodd-Frank requirements are those relating to: clearing, trade execution, real-time public reporting, Large Trader Reporting, SDR Reporting and swap data recordkeeping).**

| | **U.S. Person (including an affiliate of non-U.S. person)** | **Non-U.S. Person Guaranteed by, or Affiliate Conduit[1] of, a U.S. Person** | **Non-U.S. Person Not Guaranteed by, or Affiliate Conduit[1] of, by U.S. Person** |
|---|---|---|---|
| **U.S. Person (including an affiliate of non-U.S. person)** | Apply | Apply | Apply |
| **Non-U.S. Person Guaranteed by, or Affiliate Conduit[1] of, a U.S. person** | Apply | Substituted Compliance[2] | Do Not Apply |
| **Non-U.S. Person Not Guaranteed by, or Affiliate Conduit[1] of, U.S. Person** | Apply | Do Not Apply | Do Not Apply |

*The Appendices to the Guidance should be read in conjunction with the rest of the Guidance.

** Where one of the counterparties is electing the Inter-Affiliate Exemption, the Commission would generally expect the parties to the swap to comply with the conditions of the Inter-Affiliate Exemption, including the treatment of outward-facing swaps condition in Commission regulation 50.52(b)(4)(i).

[1] Factors that are relevant to the consideration of whether a non-U.S. person is an "affiliate conduit" include whether: (i) the non-U.S. person is majority-owned, directly or indirectly, by a U.S. person; (ii) the non-U.S. person controls, is controlled by, or is under common control with the U.S. person; (iii) the non-U.S. person, in the regular course of business, engages in swaps with non-U.S. third party(ies) for the purpose of hedging or mitigating risks faced by, or to take positions on behalf of, its U.S. affiliate(s), and enters into offsetting swaps or other arrangements with such U.S. affiliate(s) in order to transfer the risks and benefits of such swaps with third-party(ies) to its U.S. affiliates; and (iv) the financial results of the non-U.S. person are included in the consolidated financial statements of the U.S. person. Other facts and circumstances also may be relevant.

[2] Substituted compliance does not apply to Large Trader Reporting, i.e., non-U.S. persons that are subject to part 20 would comply with it in the same way that U.S. persons comply. With respect to the SDR Reporting requirement, the Commission may permit substituted compliance only if direct access to swap data stored at a foreign trade repository is provided to the Commission.

Issued in Washington, DC, on July 17, 2013, by the Commission.

Melissa D. Jurgens,

Secretary of the Commission.

**Appendices to Interpretive Guidance and Policy Statement Regarding Compliance with Certain Swap Regulations – Commission Voting Summary and Statements of Commissioners**

NOTE: The following appendices do not constitute a part of the Interpretive Guidance and Policy Statement itself.

**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 – Statement of Chairman Gary Gensler**

I support the Interpretive Guidance and Policy Statement Regarding Compliance with Certain Swap Regulations (Guidance) and the related phase-in exemptive order also being adopted today. With this Commission action another important step has been taken to make swaps market reform a reality.

This Guidance is being adopted just shy of the third anniversary of President Obama signing the Dodd-Frank Act, and that law was historic. It was an historic answer to an historic problem: the near collapse of the American economy driven, in part, by the unregulated derivatives marketplace. Congress and the President were clear in their intention to bring transparency to this marketplace, to lower risk to the public, and to ensure the regulation of swap dealers and major swap participants.

In 2008, when both the financial system and the financial regulatory system failed the public, Americans paid the price through the crisis with their jobs, their pensions, and their homes. We lost 8 million jobs in that crisis and thousands of businesses shuttered. The swaps market was central to the crisis and financial institutions operating complicated swaps businesses and offshore entities nearly toppled the economy. Congress responded. Americans are remarkably resilient – but the public really does expect us to learn from the lessons of the crisis, and to do everything possible to prevent this from happening to any of us again.

It's pretty straightforward, I think. Even though we oversee, here at the CFTC, a complex and sometimes difficult to understand market (my mom consistently asks me, “Gary, what are swaps?”), the questions the American people are looking for us to answer are simple: Have we lowered risk? Have we brought transparency to these markets? Have we promoted competition and openness in these markets so that end users can get the greatest benefit when they seek to

lower their risk and focus on what they do well – which is employing people, innovating and moving our economy forward? That is why reform matters.

Five years after the crisis and three years after Dodd-Frank passed, market participants are coming into compliance with the common sense reforms that Congress and the President laid out. Through Dodd-Frank and the rules that this agency has put in place, no longer will the markets be opaque and dark, and we will have transparency in the markets. In fact, throughout this year, for the first time, the public and regulators have benefitted from reporting to swap data repositories and reporting to the public. And later this year, starting actually in August, facilities called swap execution facilities will start so that the public can benefit from greater openness and competition before the transaction occurs. And by the end of this year, there are likely to be trade execution mandates for interest rate and credit derivative index products, as well.

Central clearing became required for the broader market earlier this year, with key phase in dates to come this Fall and Winter, as well. We have 80 swap dealers, and, yes, two major swap participants, now provisionally registered. As part of the responsibilities accompanying registration, they're responsible for sales practice, record keeping and other business conduct requirements that help lower the risk to the public.

Yesterday, we took another significant step when we and the European Commission announced a path forward regarding joint understandings regarding the regulation of cross border derivatives. I want to publicly thank Commissioner Michel Barnier, his Director General Jonathan Faull, and their staffs, the staffs at the European Securities Market Authority, and Steven Maijoor's leadership, for collaborating throughout the reform process. This was a significant step forward in harmonizing and giving clarity to the markets as to when there might be jurisdictional overlaps with regard to this reform.

Today, we are considering two important actions, the Guidance, as well as a related phase-in exemptive order. And as you probably have heard me say before, the nature of modern finance is that financial institutions commonly set up hundreds, even thousands of legal entities around the globe. In fact, the U.S.'s largest banks each have somewhere between 2,000 and 3,000 legal entities around the globe. Some of them have hundreds of legal entities just in the Cayman Islands alone. We have to remind ourselves that the largest banks and institutions are global in nature, and when a run starts on any part of an overseas affiliate or branch of a modern financial institution, risk comes crashing right back to our shores.

Similarly, if it's an EU financial institution and it has some guaranteed affiliate in the U.S. or overseas that gets into trouble, that risk can flow back to their shores. That's why, together both we and Europe recognize the importance of covering guaranteed affiliates, whether they're guaranteed affiliates of a U.S. person or of an EU person.

There's no question to me, at least, that the words of Dodd-Frank addressed this (i.e., risk importation) when they said that a direct and significant connection with activities and/or effect on commerce in the United States covers these risks that may come back to us.

I want to publicly thank Chairman Barney Frank along with Spencer Bachus, Frank Lucas, and Collin Peterson, and their staffs for reaching out to the CFTC and the public to ask how to best address offshore risks that could wash back to our economy in Dodd-Frank.

In addition, we should not forget the actual events over the past several years that remind us of the risks to the U.S. that can be posed by offshore entities:

AIG nearly brought down the U.S. economy. Lehman Brothers had 3,300 legal entities, including a London affiliate that was guaranteed here in the U.S., and it had 130,000 outstanding swap transactions. Citigroup had structured investment vehicles that were set up in the Cayman

Islands, run out of London, and yet were central to not one, but two bailouts of that institution. Bear Stearns, in 2007 had two sinking hedge funds that had to be bailed out by Bear Stearns – and, yes, those hedge funds were organized in the jurisdiction of the Cayman Islands.

More than a decade earlier, I was working in my position as Assistant Secretary of the United States Department of the Treasury. I found myself making a call from Connecticut to then Treasury Secretary Robert Rubin to report that Long Term Capital Management's $1.2 trillion swaps book was not only going to go down within a day or two, but that the business – that we thought was in Connecticut – was actually incorporated in the Cayman Islands as a PO Box facility.

Even last year, we had yet another reminder that branches of big U.S. banks can bring risk back to the US. Even though they were not the risks as large as I've just related, JPMorgan Chase's Chief Investment Office's credit default swaps were executed primarily in the U.K. branch.

Each of these examples demonstrated a direct and significant connection with activities and/or an effect on commerce in the United States. Congress knew this painful history when it provided the cross border provisions of swaps market reform. And as market participants asked the CFTC to provide interpretive guidance on Congress's word, I believe that we have had to keep this painful history in mind. Two and a half years ago, the CFTC started working on guidance, which was published for notice and comment in June 2012, and for which we sought further input on in December 2012. We have greatly benefitted from this public input. The Guidance the Commission will adopt today incorporates the public's input and, I think, appropriately interprets the cross border provisions of Dodd-Frank.

There are four areas that I think really are important:

First, the CFTC interprets the cross-border provisions to cover swaps between non U.S. swap dealers and guaranteed affiliates of U.S. Persons, as well as swaps between two guaranteed affiliates that are not swap dealers. The guidance does, as was proposed, recognize and embrace the concept of substituted compliance where there are comparable and comprehensive rules abroad. But the history of AIG, Lehman Brothers, Citigroup and the others, and of guaranteed affiliates, is a strong lesson that Congress knew when we were approaching these issues.

Second, the definition of U.S. person in this guidance captures offshore hedge funds and collective investment vehicles that have their principal place of business here in the U.S., or that are majority owned by U.S. persons. Addressing ourselves to guidance, and yet forgetting the lessons of Long Term Capital Management or Bear Stearns, is not in my opinion what Congress wanted.

Third, under the guidance, foreign branches, like the JPMorgan's U.K. branch, of U.S. swap dealers may also comply with Dodd-Frank through substituted compliance if they are appropriately ring-fenced – that is, they are truly branches where employees and the booking and the taxes are actually offshore in the foreign branch. The Guidance allows, if there are comparable and comprehensive regimes overseas and supervisory authorities overseas looking at those branches, that those branches can avail themselves to substituted compliance in the manner offshore guaranteed affiliates would.

Lastly, the guidance provides that swap dealers, foreign or U.S., transacting with U.S. persons (whether they be in New Jersey, Maryland, Michigan, Arkansas, Iowa – I have to get all the right states, recognizing where my fellow Commissioners come from) anywhere in the United States, must comply with Dodd-Frank's swap market reform. The guidance does provide, though, that U.S. Persons can meet international people anonymously, and not only on our

exchanges called designated contract markets, but also on the new swap execution facilities, as well as foreign boards of trade. International parties trading on those platforms do not have to worry about whether those swaps might make them a swap dealer, or whether they need to worry about certain transaction level requirements. And I think that was important to maintain and promote the liquidity of these three very important types of platforms – foreign boards of trade, swap execution facilities, and designated contract markets.

In conclusion, I will be voting in support of the Guidance and the related phase-in exemptive order also being adopted today. I'll say more about the exemptive order in my statement of support for that document, but I think these are both critical steps for the Commission and swaps reform. They add to the approximately 56 final guidance and rules that this Commission has adopted. We're well over 90 percent through the various rule and guidance writing. And the markets are probably well towards half way implementing these reforms. I have a deep respect for how much work market participants are doing to come into compliance.

So now, 3-years after the passage of financial reform, and a full year after the Commission proposed guidance with regard to the cross border application of reform, it is time for reforms to properly apply to and cover those activities that, as identified by Congress in section 722(d) of the Dodd-Frank Act, have "a direct and significant connection with activities in, or effect on, commerce of the United States." With the additional transitional phase in period provided by this Order, it is now time for the public to get the full benefit of the transparency and the measures to reduce risk included in Dodd Frank reforms.

**Appendix 3 – Dissenting Statement of Commissioner Scott D. O'Malia**

I respectfully dissent from the Commodity Futures Trading Commission's (the "Commission" or "CFTC") approval of its interpretive guidance and policy statement

("Guidance") regarding the cross-border application of the swaps provisions of the Commodity Exchange Act ("CEA"), as well as from the Commission's approval of a related exemptive order ("Exemptive Order").

When I voted in July 2012 to issue for public comment the proposed interpretive guidance and policy statement ("Proposed Guidance"),[1] I made clear that if I had been asked to vote on the Proposed Guidance as final, my vote would have been no. I then laid out my concerns with the Proposed Guidance, all relating to the Commission's unsound interpretation of section 2(i) of the CEA,[2] which governs the extraterritorial application of the CEA's swaps provisions. Regrettably, the Guidance fails to address these concerns and constitutes a regulatory overreach based on a weak foundation of thin statutory and legal authority.

Like the Proposed Guidance, the Guidance: (1) fails to articulate a valid statutory foundation for its overbroad scope and inconsistently applies the statute to different activities; (2) crosses the line between interpretive guidance and rulemaking; and (3) gives insufficient consideration to international law and comity. These shortcomings are compounded by serious procedural flaws in the Commission's treatment of international harmonization and substituted compliance, as well as in its issuance of the Exemptive Order.

**Lack of Statutory Foundation**

Section 2(i) of the CEA[3] as amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act")[4] provides, in part, that the

---

[1] Cross-Border Application of Certain Swaps Provisions of the Commodity Exchange Act, 77 Fed. Reg. 41214 (July 12, 2012).

[2] 7 U.S.C. §§ 1 et seq.

[3] § 2(i).

Commission's swap authority "shall not apply" to activities outside the United States unless those activities "have a direct and significant connection with activities in, or effect on, commerce of the United States . . . ."[5] This provision is clearly a limitation on the Commission's authority.[6] It follows that the Commission must properly articulate how and when the "direct and significant" standard is met in order to apply Commission rules to swap activities that take place outside of the United States.

The Guidance, however, fails to do so. Instead, it treats section 2(i) as a ready tool to expand authority rather than as a limitation. The statutory analysis section of the Guidance is insufficient to support the broad sweep of extraterritorial activities that the Guidance contemplates would fall under the Commission's jurisdiction, relying heavily on a comparison to somewhat similar statutory language whose wholly different context renders the comparison unpersuasive. The Guidance makes no mention of statutes that may be more analogous to the CEA, such as the securities or banking laws.[7] Because the "direct and significant" standard is never defined, the Guidance's attempts to link certain requirements imposed on market participants to the "direct and significant" standard do not establish the requisite jurisdictional nexus.[8]

---

[4] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 124 Stat. 1376 (2010).

[5] § 2(i)(1).

[6] Stated another way, section 2(i)(1) may be read as the following: "[The CEA's swaps provisions enacted by the Dodd-Frank Act] <u>may</u> apply to activities outside the United States <u>only if</u> those activities have a direct and significant connection with activities in, or effect on, commerce of the United States."

[7] For a recent statutory analysis of the extraterritorial application of the Securities and Exchange Act of 1934, <u>see Morrison v. Nat'l Australia Bank</u>, 561 U.S. __ (2010).

[8] <u>See Appalachian Power Co. v. Envtl. Prot. Agency</u>, 208 F.3d 1015, 1027 (D.C. Cir. 2000) (vacating agency guidance interpreting statutory language with practical binding effect because it did not define subparts of the interpreted term and should have been promulgated as a legislative rule under the APA).

I would also like to point out that CEA section 2(i) contains a second clause, which allows for the limited application of the Commission's swap rules to activities outside the United States when they violate the Commission's anti-evasion rules.[9] Pursuant to this clause, the Commission promulgated section 1.6 under Part 1 of its regulations.[10] Rather than relying on section 1.6 to address its concerns about evasion, the Commission chose simply to reference the same concerns in justifying its overbroad reach in the Guidance.

With such an unsound foundation for the Commission's extraterritorial authority under the "direct and significant" standard, I am not surprised that the Guidance often applies section 2(i) of the CEA inconsistently and arbitrarily. Examples of inconsistency abound.

For instance, just as with the Proposed Guidance, the Guidance does not provide a basis for its reasoning that all Transaction-Level Requirements described in the Guidance satisfy the "direct and significant" standard under section 2(i). As I stated in my concurrence to the Proposed Guidance, trade execution and real-time public reporting requirements, although important for transparency purposes, do not raise the same systemic risk concerns that clearing and margining for uncleared swaps do. The Guidance acknowledges this point, but does not go on to sufficiently explain why they should be, and are, treated equally. The Guidance also acknowledges that clearing and margining, because of their implications for systemic risk, could be classified as Entity-Level Requirements, but it does not explain why are they are not. The

---

[9] 7 U.S.C. § 2(i)(2) ([The CEA's swaps provisions enacted by the Dodd-Frank Act] "shall not apply to activities outside the United States unless those activities . . . contravene such rules or regulations as the Commission may prescribe or promulgate as are necessary or appropriate to prevent the evasion of any provision of [the CEA enacted by the Dodd-Frank Act]").

[10] 17 CFR § 1.6.

Guidance's failure to give meaning to the "direct and significant" standard in its discussion of these requirements is glaring.

Inconsistent application can also be seen within a specific Transaction-Level Requirement, for example reporting to swap data repositories ("SDRs"). The Guidance allows non-U.S. swap dealers ("SDs") and major swap participants ("MSPs") to utilize substituted compliance for SDR reporting of their swaps with non-U.S. counterparties, but it does not allow for substituted compliance for non-U.S. SD and MSPs' trades with U.S. counterparties. Again, the Commission fails here to give real meaning to "direct and significant" in order to adequately explain its reasoning for this distinction. The rationale is even weaker given the fact that substituted compliance is available for swaps with non-U.S. counterparties only under the condition that the Commission has direct access to the relevant data at the foreign trade repository. In either case, the Commission will have direct access to the relevant data, whether substituted compliance is available or not. This raises the question: if the outcome is the same, why is the distinction made? If it is different, the Guidance does not explain how or why – despite requiring data at foreign trade repositories to be essentially the same as data at domestic SDRs, before the Commission even contemplates substituted compliance for SDR reporting.

Yet another example of inconsistent application of section 2(i) involves the requirement of physical commodity large swaps trader reporting ("Large Trader Reporting"). In contrast to SDR reporting, the Guidance does not allow substituted compliance for Large Trader Reporting, even for swaps between a non-U.S. registrant and a non-U.S. counterparty. The Commission's flimsy rationale is that Large Trader Reporting involves data conversion to "futures equivalent" units, and that it would cost too much time and resources for the Commission to conduct this conversion on data that it could access in a foreign trade repository. Here again, the "direct and

significant" standard is nowhere to be found. Moreover, the Commission overstates the burden of the "futures equivalent" conversion and, more generally, the significance of Large Trader Reporting in its oversight duties, while understating the availability of data collected through SDR reporting, with its eligibility for substituted compliance, to achieve the same regulatory objectives.

**Interpretive Guidance Versus Rulemaking**

The imposition of requirements on market participants raises another of my major concerns with the Guidance. I strongly disagree with the Commission's decision to issue its position on the cross-border application of its swaps regulations in the form of "interpretive guidance" instead of promulgating a legislative rule under the Administrative Procedure Act ("APA").[11]

Simply putting the guise of "guidance" on this document does not change its content or consequences. Where agency action has the practical effect of binding parties within its scope, it has the force and effect of law, regardless of the name it is given.[12] Legally binding regulations that impose new obligations on affected parties – "legislative rules" – must conform to the APA.[13] On its face, the Guidance sets out standards that it contemplates will be regularly applied by staff to cross-border activities in the swaps markets. Market participants cannot afford to ignore detailed regulations imposed upon their activities that may result in enforcement or other

---

[11] 5 U.S.C. §§ 551 et seq.

[12] See Gen. Elec. Co. v. Envtl. Prot. Agency, 290 F.3d 377, 380 (D.C. Cir. 2002) (finding that a guidance document is final agency action); Appalachian Power, 208 F.3d at 1020-21.

[13] See Chrysler Corp. v. Brown, 441 U.S. 281, 302-03 (1979) (agency rulemaking with the force and effect of law must be promulgated pursuant to the procedural requirements of the APA).

penalizing action.[14] This point is underlined by the fact that, as I discuss below, Commission staff no-action letters have been issued in connection with compliance obligations that have essentially been imposed by the Guidance.[15] All of this leads to the logical conclusion that the Guidance has a practical binding effect and should have been promulgated as a legislative rule under the APA.

There are important policy and legal considerations that weigh strongly in support of rulemaking in accordance with the APA. Not only do the safeguards enacted by Congress in the APA ensure fair notice and public participation, they help to ensure reasoned decision-making and accountability. In addition, the APA requires that courts take a "hard look" at agency action.[16]

---

[14] "A document will have practical binding effect before it is actually applied if the affected private parties are reasonably led to believe that failure to conform will bring adverse consequences . . . ." *Gen. Elec.*, 290 F.3d at 383 (quoting Anthony, Robert A., Interpretive Rules, Policy Statements, Guidances, Manuals, and the Like—Should Federal Agencies Use Them to Bind the Public?, 41 Duke L. J. 1311 (1992)) (vacating an agency's guidance document that the court found to have practical binding effect and where procedures under the APA were not followed).

[15] A no-action letter is issued by a division of the Commission and states that, for the reasons and under the conditions described therein, it will not recommend that the Commission commence an enforcement action against an entity or group of entities for failure to comply with obligations imposed by the Commission.

[16] The "arbitrary and capricious" standard of review of agency action under the APA is a rationality analysis also known as the hard-look doctrine:

> Under the leading formulation of this doctrine, "the agency must examine the relevant data and articulate a satisfactory explanation for its action including a 'rational connection between the facts found and the choices made.' " The court "consider[s] whether the decision was based on a consideration of the relevant factors and whether there has been a clear error of judgment." In addition, the agency may not "entirely fail[] to consider an important aspect of the problem," may not "offer[] an explanation for its decision that runs counter to the evidence before the agency," nor offer an explanation that is "so implausible that it could not be ascribed to a difference in view or the product of agency expertise." The agency must also relate the factual findings and expected effects of the regulation to the purposes or goals the agency must consider under the statute as well as respond to salient criticisms of the agency's reasoning.

Stack, Kevin M., Interpreting Regulations, 111 Mich. L. Rev. 355, 378-79 (2012) (internal citations omitted).

By issuing "interpretive guidance" instead of rulemaking, the Commission has also avoided analyzing the costs and benefits of its actions pursuant to section 15(a) of the CEA,[17] because the CEA requires the Commission to consider costs and benefits only in connection with its promulgation of regulations and orders. Compliance with the Commission's swaps regulations entails significant costs for market participants. Avoiding cost-benefit analysis by labeling the document as guidance is unacceptable.

In my concurrence to the Proposed Guidance, I suggested that the Commission should at least prepare a report analyzing the costs attributable to the breadth of the Commission's new authority under CEA section 2(i). I am disappointed, but not surprised, that the Commission has not taken up my suggestion.

**Insufficient Consideration of Principles of International Comity**

Also in my concurrence to the Proposed Guidance, I pointed out that the Commission's approach gave insufficient consideration to principles of international comity. The Guidance suffers from the same shortcoming.

The Commission does describe principles of international comity in the Guidance, as it did in the Proposed Guidance. However, mere citation is meaningless if unaccompanied by adherence. With an interpretation of section 2(i) that essentially views the Commission's jurisdiction as boundless, roping in all transactions with U.S. persons regardless of the location or the regulations that foreign regulators may have in place, the reality is that the Commission's approach is unilateral and does not give adequate consideration to comity principles.

---

[17] 7 U.S.C. § 19(a).

These principles are crucial given the global, interconnected nature of today's swaps markets. Properly considering these principles – in addition to indicating respect for the international system and the legitimate interests of other jurisdictions – strengthens, not weakens, the Commission's ability to effectively regulate swaps markets.

**On the Path Forward to Harmonization, But a Flawed Process**

In order to implement principles of international comity and develop a harmonized global regulatory system that is both effective and efficient, I have consistently called for meaningful cooperation with foreign regulators. I initially did so in my concurrence to the Proposed Guidance, and the necessity of greater collaboration was subsequently driven home by the number and tone of comment letters on the Proposed Guidance submitted by foreign regulators.[18] Then, when the Commission finalized a cross-border exemptive order last December with an expiration date of July 12,[19] in my concurring statement I again urged the Commission and foreign regulators to engage in meaningful, substantive discussions.

I am pleased that over the past several months, this engagement has taken place and progress has been made toward harmonization. However, we are not where we need to be: many

---

[18] The Commission received comment letters from, among others: Jonathan Faull, European Commission; Steven Maijoor, European Securities and Markets Authority; David Lawton and Stephen Bland, UK Financial Services Authority; Pierre Moscovici, France Ministry of Economy and Finance, Christian Noyer, Autorite de controle prudential, and Jacques Delmas-Marsalet, Autorite des marches financiers; Patrick Raaflaub and Mark Branson, Swiss Financial Market Supervisory Authority; Masamichi Kono, Japan Financial Services Agency, and Hideo Hayakawa, Bank of Japan; K.C. Chan, Financial Services and Treasury Bureau of the Hong Kong Special Administrative Region; Belinda Gibson, Australian Securities and Investments Commission, Malcolm Edey, Reserve Bank of Australia, Arthur Yuen, Hong Kong Monetary Authority, Keith Lui, Hong Kong Securities and Futures Commission, and Teo Swee Lian, Monetary Authority of Singapore. These and all public comment letters on the Proposed Guidance are available at: http://comments.cftc.gov/PublicComments/CommentList.aspx?id=1234&ctl00_ctl00_cphContentMain_MainContent_gvCommentList.

[19] Final Exemptive Order Regarding Compliance With Certain Swap Regulations, 78 Fed. Reg. 858 (January 7, 2013). The document was adopted by the Commission in December 2012 and published in the Federal Register in January 2013.

outstanding issues and questions remain, from data privacy concerns, to the implications of other jurisdictions still finalizing their regulations, to a lack of a clear, consistent and transparent framework for substituted compliance. It would have made sense for these issues to be addressed in the Guidance – but they are not. The looming July 12 expiration of the December exemptive order and the resulting time crunch cannot reasonably be cited as the reason for this failure, because July 12 is an artificial date; it could have been pushed back in order to reach the right outcome with the right process.

Instead, while we are moving toward a workable outcome on harmonization, the process by which we are getting there is patently unacceptable. The most glaring example of this flawed process is this week's publication of a Commission staff no-action letter allowing substituted compliance for certain of the Transaction-Level Requirements.[20] It boggles the mind to think that a staff letter issued by a single division, with no input from the Commission, would be used as the vehicle for addressing such a major issue.[21] Making matters worse, this no-action letter is outside the scope of a forthcoming Commission decision regarding the comparability of European rules. And the relief is not time-limited, thereby creating an effect similar to a rulemaking. Consequently, this indefinite exclusion not only preemptively overrides a Commission decision, but it also seems to provide relief beyond that contemplated by the

---

[20] No-Action Relief for Registered Swap Dealers and Major Swap Participants from Certain Requirements under Subpart I of Part 23 of Commission Regulations in Connection with Uncleared Swaps Subject to Risk Mitigation Techniques under EMIR, CFTC Letter No. 13-45 (July 11, 2013).

[21] I have set forth in note 18 some of the comment letters that the Commission has received from foreign supervisors and regulators. By allowing substituted compliance to be addressed through a no-action letter, is the Commission implying that, *e.g.*, the Bank of Japan should accede to, *e.g.*, decisions of the CFTC Division of Swap Dealer and Intermediary Oversight? If so, I find such implication inappropriate.

Guidance, which calls for a re-evaluation of all substituted compliance determinations within four years of the initial determination.

Unfortunately, this is not the first instance in recent times of staff no-action letters being used to issue Commission policy. Not only are they an improper tool to get around formal Commission action, their prolific use is a reflection of the ad-hoc, last-minute approach that has been far too prevalent lately at the Commission. I cannot emphasize this enough: the Commission must stop this approach and get back to issuing policy in a more formal, open and transparent manner.

**Substituted Compliance**

In my discussions with fellow regulators abroad and international regulatory bodies, it is clear that there are varying degrees of reforms being developed and implemented in respective jurisdictions: some are comparable to U.S. regulations and some are less stringent, but there are some that exceed the Commission's own requirements. I would have preferred the Commission to take the past year following the release of the Proposed Guidance to engage our international colleagues and to involve the International Organization of Securities Commissions ("IOSCO") in order to resolve the issue of harmonizing our rules. Under this approach, we could finalize our guidance upon completion of the international harmonization process, allowing us to take into account any shortcomings in that process. Instead, we have chosen the reverse order: to impose statutorily weak guidance, with all its no-action riders and exemptions, with only the promise of further negotiations with our foreign counterparts.

Given the way the Commission has proceeded up to this point, it is my hope that the harmonization work lying ahead will be undertaken in a more transparent manner and not done through the abused no-action process that lacks any formal Commission process or oversight.

Further, I hope that the process of substituted compliance will offer the opportunity for other regulatory bodies to engage directly with the full Commission, so that we can better understand how our rules and theirs will work and can minimize the likelihood of regulatory retaliation and inconsistent, duplicative, or conflicting rules. I believe the Commission has worked too hard to develop principles and standards that will encourage greater transparency, open access to clearing and trading and improved market data to let them go to waste due to a lack of global regulatory harmonization.

I want to work with other home country regulators to ensure there is not an opportunity for entities to exploit regulatory loopholes. The stark reality is that this Commission is not the global regulatory authority and does not have the resources to support such a mission. Therefore, our best and most effective solution is to engage in a fully transparent discussion on substituted compliance and to do so immediately.

**Exemptive Order**

In an effort to mitigate the broad reach of the Guidance and accommodate its last-minute finalization, and in a moment of humility, the Commission has agreed to delay the application of certain elements of the Commission's swaps regulations with its approval of the Exemptive Order. The Exemptive Order provides relief ranging from 75 days (for application of the expanded U.S. person definition, for example) to December 21, 2013 (for Entity-Level and Transaction-Level Requirements for non-U.S. SDs and MSPs in certain jurisdictions). The Commission is issuing the Exemptive Order pursuant to section 4(c) of the CEA.[22]

---

[22] Section 4(c) of the CEA grants the Commission the authority to "exempt any agreement, contract, or transaction (or class thereof) that is otherwise subject to subsection (a) (including any person or class of persons offering, entering into, rendering advice or rendering other services with respect to, the agreement, contract, or transaction) . .

Even though the Exemptive Order goes into effect immediately, the Commission has included a post hoc 30-day comment period. I support the additional time that the Exemptive Order provides for market participants to comply with the Commission's last-minute Guidance, but I cannot support a final order that blatantly ignores the APA-mandated comment periods for Commission action, especially when I advocated for a relief package that would have provided for public comment over a month ago.[23]

**Additional Concerns**

In addition to the above, the Guidance leaves me concerned in a number of other areas. I am concerned about whether the definition of U.S. person contained herein provides the necessary clarity for market participants, particularly as its enumerated prongs are explicitly deemed to form a non-exhaustive list. I question whether the Commission has done enough to harmonize its cross-border approach with that of the Securities and Exchange Commission (which is being issued through notice-and-comment rulemaking instead of interpretive guidance, I should note), in particular with regard to the definitions of U.S. person and foreign branches. I

. ." 7 U.S.C. § 6(c). Section 4(a) applies to "any person to offer to enter into, to enter into, to execute, to confirm the execution of, or to conduct any office or business anywhere in the United States, its territories or possessions, for the purpose of soliciting, or accepting any order for, or otherwise dealing in, any transaction in, or in connection with, a contract for the purchase or sale of a commodity for future delivery (other than a contract which is made on or subject to the rules of a board of trade, exchange, or market located outside the United States, its territories or possessions) . . . ." 7 U.S.C. § 6(a).

[23] The Exemptive Order claims, unconvincingly, that it falls under a good-cause exception to notice-and-comment requirements provided for by the APA under section 553(b)(B): "Except when notice and hearing is required by statute, this subsection does not apply… (B) when the agency for good cause finds (and incorporates the finding and a brief statement of reasons therefore in the rules issued) that notice and public procedure thereon are impracticable, unnecessary, or contrary to the public interest." 5 U.S.C. § 553(b)(B) (emphasis added). However, section 4(c) of the CEA clearly provides that the Commission may grant exemptive relief only by "rule, regulation, or order after notice and opportunity for hearing" (emphasis added). 7 U.S.C. § 6(c). The APA further provides under section 559 that it does not "limit or repeal additional requirements imposed by statute or otherwise recognized by law." 5 U.S.C. § 559. The CEA also grants emergency powers to the Commission under exigent circumstances. See, e.g., 7 U.S.C. § 12a(9). In addition, courts have narrowly construed the good-cause exception and placed the burden of proof on the agency. See Tenn. Gas Pipeline Co. v. Fed. Energy Regulatory Comm'n, 969 F.2d 1141 (D.C. Cir. 1992); Guardian Fed. Sav. & Loan Ass'n v. Fed. Sav. & Loan Ins. Corp., 589 F.2d 658, 663 (D.C. Cir. 1978).

also am concerned about whether the Guidance creates an uneven playing field for U.S. firms, which would be a plainly unacceptable outcome to me. I am concerned that the Guidance is overlapping, duplicative, and perhaps even contradictory with other provisions in the Dodd-Frank Act that mitigate systemic risk and allocate responsibility for administering its complex and comprehensive regulatory regime to multiple agencies under Title I, Title II, and even within Title VII.[24] In addition, I am concerned that the Guidance practically ignores the hugely important matter of protecting customer funds, specifically in connection with bankruptcies, which has critical cross-border implications as vividly demonstrated by the recent collapse of MF Global.[25] Finally, I am concerned about whether in overreaching to rope in entities into U.S. jurisdiction that would more appropriately be regulated elsewhere pursuant to an effective system of substituted compliance, the Guidance will have the perverse effect of creating more risk to the U.S. system and more risk to U.S. taxpayers.

**Conclusion**

For an administrative agency, good government combines good substance – based on a faithful, appropriate reading of the guiding statute – and good process. The Guidance falls woefully short on both counts. Therefore, I respectfully dissent from the decision of the

---

[24] *See, e.g.*, 7 U.S.C. § 6s(d)(2) ("The Commission may not prescribe rules imposing prudential requirements on swap dealers or major swap participants for which there is a prudential regulator."); 7 U.S.C. § 6b-1(b) ("The prudential regulators shall have exclusive authority to enforce the provisions of section 4s(e) with respect to swap dealers or major swap participants for which they are the prudential regulator.")

[25] In a recent op-ed article James Giddens, the bankruptcy trustee for MF Global's U.S.-registered entities, points out that serious concerns regarding the harmonization, or lack thereof, of bankruptcy regimes were identified during the resolution of Lehman Brothers in 2008 (he was then the liquidation trustee for Lehman Brothers's U.S. broker-dealer), only for similar failings to appear with MF Global. He urges clearer and more consistent cross-border rules regarding the protection of customer money in advance of any future multinational financial company meltdown. Giddens, James, How to Avoid the Next MF Global Surprise: Change Cross-Border Rules to Stop Raids on U.S. Customer Accounts, Wall St. J., July 9, 2013.

Commission to approve the Guidance and Exemptive Order for publication in the Federal Register.