

# COMMITTEE ON CAPITAL MARKETS REGULATION

August 17, 2013

Ms. Elizabeth M. Murphy  
Secretary  
Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549-1090

Mr. Gary Barnett  
Director  
Commodity Futures Trading Commission  
1155 21<sup>st</sup> Street, NW  
Washington, DC 20581

VIA ELECTRONIC MAIL: [rule-comments@sec.gov](mailto:rule-comments@sec.gov); [rule-comments@cftc.gov](mailto:rule-comments@cftc.gov)

Re: Securities and Exchange Commission (the “**SEC**”), “Cross-Border Security-Based Swap Activities; Proposed Rule” (File Number S7-02-13) (the “**Proposed Rule**”); Commodity Futures Trading Commission (the “**CFTC**”), “Interpretive Guidance and Policy Statement Regarding Compliance with Certain Swaps Regulations (RIN 3038–AD85) (the “**Final Guidance**”)

Dear Ms. Murphy and Mr. Barnett:

The Committee on Capital Markets Regulation (the “**Committee**”) is grateful for the opportunity to comment on the Proposed Rule and Final Guidance, addressing the application of the provisions of Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “**Dodd-Frank Act**”) to cross-border swaps.<sup>1</sup>

Founded in 2006, the Committee is dedicated to enhancing the competitiveness of U.S. capital markets and ensuring the stability of the U.S. financial system. Our membership includes thirty-two leaders drawn from the finance, investment, business, law, accounting, and academic communities. The Committee is chaired jointly by R. Glenn Hubbard (Dean, Columbia Business School) and John L. Thornton (Chairman, The Brookings Institution) and directed by Hal S. Scott (Nomura Professor and Director of the Program on International Financial Systems, Harvard Law School). The Committee is an independent and nonpartisan 501(c)(3) research organization, financed by contributions from individuals, foundations, and corporations.

While we applaud the SEC’s and CFTC’s continued efforts to reform the global swaps market, including mandatory central clearing, trade execution, and reporting requirements, the Committee believes that the Proposed Rule and Final Guidance do not allow for sufficient

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<sup>1</sup> A swap is “cross-border” if the counterparties to the swap include a “U.S. person,” as defined by the Proposed Rule and Final Guidance, and a non-U.S. person. *See* Cross-Border Security-Based Swap Activities, Exchange Act Release No. 69490, 78 Fed. Reg. 30968 (proposed May 23, 2013), *available at* <http://www.gpo.gov/fdsys/pkg/FR-2013-05-23/pdf/2013-10835.pdf> ; Interpretive Guidance and Policy Statement Regarding Compliance with Certain Swap Regulations, 78 Fed. Reg. 45292 (July 26, 2013), *available at* <http://www.gpo.gov/fdsys/pkg/FR-2013-07-26/pdf/2013-17958.pdf>.

deference to the laws of foreign jurisdictions with comparable swaps rules. Although the Committee acknowledges that Dodd-Frank's extraterritoriality provisions apply somewhat differently for the SEC and CFTC, the Committee is nevertheless concerned that the agencies are taking unnecessarily divergent approaches to the cross-border application of Title VII. We would encourage the SEC and CFTC to adopt the same cross-border rules, including negotiating joint agreements with international regulators, as necessary, and making joint substituted compliance assessments, where applicable.

The Committee believes that the SEC should play an integral role in the "Common Path Forward" process recently launched by the CFTC and European Commission. The Common Path Forward set forth certain European Union ("E.U.") and CFTC rules deemed sufficiently comparable to allow E.U. and U.S. cross-border swaps counterparties to comply with the rules of either regime, rather than with the rules of both regimes.<sup>2</sup> The Committee recommends that the SEC and the CFTC jointly enter into such an agreement with foreign regulators in order to implement a consistent approach.

In the Final Guidance, the CFTC adopted a new "essentially identical" approach to the cross-border application of Title VII, which will apply to cross-border swaps that are ineligible for substituted compliance.<sup>3</sup> Where the CFTC determines that a foreign regime's rules are essentially identical to the CFTC's rules, it will permit *any* U.S. person and non-U.S. person entering into a cross-border swap to comply with the rules of the foreign regime instead of the CFTC's rules.<sup>4</sup> The Committee commends the CFTC for adopting this approach, as it will avoid the duplicative application of two regime's rules to cross-border swaps involving U.S. persons. The Committee recommends that the SEC adopt a similar approach for any cross-border security-based swaps that are ineligible for substituted compliance.

The Committee is concerned by the agencies' approach to substituted compliance. "Substituted compliance" allows a U.S. person and a non-U.S. person entering into a cross-border swap to comply with a foreign regime's rules instead of the applicable SEC or CFTC rules, if the SEC or CFTC has previously determined that the foreign regime's rules are sufficiently comparable to the relevant SEC or CFTC rules.<sup>5</sup> However, according to the Proposed Rule and Final Guidance, not all cross-border swaps are eligible for such treatment: the counterparties to ineligible cross-border swaps must comply with the SEC's or CFTC's rules regardless of the comparability of the foreign regime's rules.<sup>6</sup> Requiring the counterparties to certain cross-border swaps to comply with the SEC's or CFTC's rules, even if a foreign regime's rules are comparable, will unnecessarily increase the likelihood of a costly overlap of requirements. Further, if a foreign regime's rules are comparable to the SEC's or CFTC's rules, requiring the counterparties to a cross-border swap to comply with the equivalent U.S. rules is unnecessary to

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<sup>2</sup> See Press Release, *The European Commission and the CFTC Reach a Common Path Forward on Derivatives*, CFTC.GOV (July 11, 2013), available at <http://www.cftc.gov/PressRoom/PressReleases/pr6640-13>.

<sup>3</sup> See Final Guidance, *supra* note 1, at 45292.

<sup>4</sup> *Id.* at 45353 (noting that 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").

<sup>5</sup> See *id.* at 45340 (discussing the CFTC's approach on "substituted compliance" for cross-border swap transactions); Proposed Rule, *supra* note 1, at 31085 (discussing the SEC's approach on "substituted compliance" for cross-border swap transactions).

<sup>6</sup> See Final Guidance, *supra* note 1, at 45347; Proposed Rule, *supra* note 1, at 31093.

mitigate systemic risk. The Committee therefore recommends that any swap involving a U.S. person and a non-U.S. person should be eligible for substituted compliance.

In determining whether a foreign regime's rules are comparable to the SEC's rules, the SEC will separately assess four categories of a foreign regime's rules (*e.g.*, rules related to clearing, trade execution, trade reporting, and the entity-level rules for swap dealers).<sup>7</sup> The Committee commends the SEC's approach, since a foreign regime may be comparable in some respects but not in others. By contrast, the CFTC's thirteen categories for assessing a foreign regime's rules may complicate and extend the review process without ensuring a better result.<sup>8</sup> The Committee encourages the CFTC and SEC to work together to define an optimal number of assessment categories and create a review process that is both effective and avoids imposing unnecessary and duplicative burdens.

The Committee has identified important differences between the Final Guidance and Proposed Rule with respect to the eligibility of certain classes of swaps for substituted compliance. Essentially, the SEC has allowed for a broader substituted compliance regime, with more cross-border security-based swaps eligible for substituted compliance than is true for swaps falling under the CFTC's jurisdiction.

Set forth below are five key differences identified by the Committee between the SEC and CFTC approaches to substituted compliance. The Committee generally favors the SEC's approach to the issue of substituted compliance and encourages the two agencies to coordinate their approaches.

- U.S. person (other than a foreign branch of a U.S. swap dealer or major swaps participant) transacting with a foreign branch of a U.S. bank that is a swap dealer. *For example, a U.S. fund entering into a swap or security-based swap with the U.K. branch of a U.S. bank.*
  - CFTC: No substituted compliance available.<sup>9</sup>
  - SEC: Substituted compliance, if the foreign regime is comparable to the SEC rules.<sup>10</sup>
- U.S. person (other than a foreign branch of a U.S. swap dealer or major swaps participant) transacting with a foreign bank registered as a swap dealer. *For example, a U.S. fund entering into a swap or security-based swap with a large U.K. bank.*
  - CFTC: No substituted compliance available.<sup>11</sup>
  - SEC: Substituted compliance, if the foreign regime is comparable to the SEC rules.<sup>12</sup>
- U.S. person (not registered as a U.S. swap dealer or major swaps participant) transacting with a foreign person (not registered as a U.S. swap dealer or major

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<sup>7</sup> Proposed Rule, *supra* note 1, at 30975 n.43.

<sup>8</sup> Final Guidance, *supra* note 1, at 45336, 45340.

<sup>9</sup> *Id.* at 45348, 45350.

<sup>10</sup> Proposed Rule, *supra* note 1, at 31094.

<sup>11</sup> Final Guidance, *supra* note 1, at 45348.

<sup>12</sup> Proposed Rule, *supra* note 1, at 31094.

swaps participant). *For example, a U.S. fund entering into a swap or security-based swap with an E.U. fund or small E.U. bank.*

- *CFTC*: No substituted compliance available.<sup>13</sup>
  - *SEC*: Substituted compliance, if the foreign regime is comparable to the *SEC* rules.<sup>14</sup>
- U.S. branch of a foreign swap dealer or major swaps participant transacting with any counterparty (U.S. or foreign). *For example, the U.S. branch of a large foreign bank entering into a swap or security-based swap with another large foreign bank.*
- *CFTC*: No substituted compliance available.<sup>15</sup>
  - *SEC*: Substituted compliance, if the foreign regime is comparable to the *SEC* rules and the transaction takes place outside the United States.<sup>16</sup>
- U.S. swap dealer or major swaps participant (not transacting through its foreign branch) transacting with any counterparty (U.S. or foreign). *For example, a large U.S. bank entering into a swap or security-based swap with a large E.U. bank.*
- *CFTC*: No substituted compliance available.<sup>17</sup>
  - *SEC*: Substituted compliance, if the foreign regime is comparable to the *SEC* rules and the transaction takes place outside the United States.<sup>18</sup>

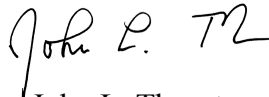
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Thank you very much for your consideration of the Committee's position with regard to these matters. Should you have any questions or concerns, please do not hesitate to contact the Committee's Director, Prof. Hal S. Scott ([hscott@law.harvard.edu](mailto:hscott@law.harvard.edu)), at your convenience.

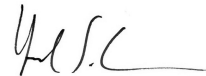
Respectfully submitted,



R. Glenn Hubbard  
Co-CHAIR



John L. Thornton  
Co-CHAIR



Hal S. Scott  
DIRECTOR

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<sup>13</sup> Final Guidance, *supra* note 1, at 45348.

<sup>14</sup> Proposed Rule, *supra* note 1, at 31094.

<sup>15</sup> Final Guidance, *supra* note 1, at 45350.

<sup>16</sup> Proposed Rule, *supra* note 1, at 31094.

<sup>17</sup> Final Guidance, *supra* note 1, at 45347, 45350.

<sup>18</sup> Proposed Rule, *supra* note 1, at 31094.