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Global Market Structure 10 Years Later:
Where have we been and where are we now?
January 24, 2019
4:00 p.m. – 5:30 p.m.

Chair:
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Panel:
Commissioner Dan Berkovitz (CFTC)
Commissioner Dawn Stump (CFTC)
Allison Lurton (FIA)
Annette Nazareth (Davis Polk)
Ron Oppenheimer (Vitol)
Tom Sexton (NFA)
Robert Steigerwald (Federal Reserve Bank of Chicago)
Submitted by Annette L. Nazareth
American Bar Association Derivatives and Futures Law Committee Annual Winter Meeting
Naples, Florida (January 2019)

"CFTC Proposes Maintaining Swap Dealer De Minimis Registration Threshold at $8 Billion with Expanded Exceptions"
CFTC Proposes Maintaining Swap Dealer *De Minimis* Registration Threshold at $8 Billion with Expanded Exceptions

July 5, 2018

On June 12, 2018, the CFTC published a notice of proposed rulemaking that would make permanent the $8 billion temporary swap dealer *de minimis* registration threshold currently in effect and would make other changes to the *de minimis* exception.

- **De Minimis Registration Threshold Proposal.** As anticipated and foreshadowed by remarks by Chairman Giancarlo, the CFTC proposes to adopt the current *de minimis* registration threshold of $8 billion. The approach, as discussed in the notice of proposed rulemaking, is supported by data analysis in two prior CFTC staff reports and more recent staff analysis, as well as a recommendation by the U.S. Treasury in its 2017 report on capital markets.

- **Three New Exceptions to the De Minimis Calculation.** The CFTC would create three new exceptions to the *de minimis* calculation, two of which would expand the availability of existing exclusions from the definition of swap dealer. Swaps that fit within these new exceptions would not need to be counted towards the *de minimis* registration threshold.
  
  1) A new exception for swaps entered into by an insured depository institution ("IDI") in connection with loans to customers ("IDI *De Minimis Exception*"). The new exception would be available in addition to the existing exclusion for swaps entered into by an IDI in connection with loans but would impose less restrictive conditions for swaps to be eligible;
  
  2) A new exception for swaps entered into to hedge financial or physical positions. This exception would, in effect, provide greater certainty about the range of hedging swaps that need not be counted towards the *de minimis* registration threshold; and

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1. This proposal would not change the $25 million *de minimis* registration threshold for swaps with special entities.

3) A new exception for swaps that result from multilateral portfolio compression exercises, codifying the relief provided by CFTC No-Action Letter 12-62.

- **Swap Notional Calculation Methodology Delegation of Authority.** The CFTC proposes to delegate authority to determine the methodology used to calculate the notional amount for any type of swap to the Director of the Division of Swap Dealer Intermediary Oversight ("DSIO").

The CFTC also invites comments on a range of related issues without proposing specific rule amendments, including whether exchange-traded swaps, cleared swaps and non-deliverable foreign exchange forwards should be excluded from the *de minimis* calculation. Notably, the proposed rule is silent on the cross-border counting issues previously addressed in the 2016 proposed rule on the cross-border application of the *de minimis* registration thresholds.

As discussed further below, Chairman Giancarlo has stated that he is committed to finalizing the proposal before the end of 2018 to provide market participants with greater certainty about their potential swap dealer registration requirements. It is possible, therefore, that some of the proposals or other issues not directly related to the level of the *de minimis* registration threshold for which comments are requested may be addressed at a later time through separate rulemakings. Given that Chairman Giancarlo has announced that he does not intend to seek reappointment when his term ends in April 2019 (though he will remain in office until his successor is appointed), it is possible that any such later changes could be made under a new Chairman.

Comments are due by August 13, 2018.

**De Minimis Registration Threshold Proposal and Timing Issues**

The *de minimis* exception to the swap dealer definition provides that a person is deemed not to be a swap dealer if its swaps entered into in a dealing capacity over the preceding 12-month period, aggregated with the swap dealing positions over the same period of affiliates that are not registered as swap dealers, do not exceed the *de minimis* registration threshold. A person that breaches the threshold must register with the CFTC as a swap dealer within two months of the end of the month in which the breach occurs.

Absent CFTC action, the current *de minimis* registration threshold of $8 billion would automatically drop to $3 billion on December 31, 2019. Given that the *de minimis* calculation must take into account dealing swaps over a preceding 12-month period, a market participant would need to monitor and

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2 The $8 billion phase-in threshold was originally scheduled to expire on December 31, 2017, but the CFTC has twice issued orders extending the deadline. The current order is set to expire on December 31, 2019.
manage its dealing swaps towards the lower $3 billion threshold beginning on January 1, 2019, unless the CFTC takes action. Chairman Giancarlo has recognized the importance of CFTC action well in advance of January 2019 to provide certainty and clarity to market participants that engage in swap dealing activities.

New Exceptions to the De Minimis Calculation

IDI De Minimis Exception

Section 721(d)(i) of the Dodd-Frank Act requires that the CFTC and SEC define the term "swap dealer," and in 2012, the agencies issued a joint final rulemaking defining this term. As part of this effort, the agencies adopted an exclusion that implements the statutory requirement that an IDI not be considered to be a swap dealer to the extent that it offers to enter into a swap with a customer in connection with originating a loan with that customer.

This existing exclusion permits an IDI to exclude swaps it enters into with loan customers when determining whether it is a swap dealer, subject to numerous conditions. In the proposal, the CFTC states that based on information obtained from market participants and analysis of data submitted to swap data repositories, it believes that the existing exclusion is unnecessarily restrictive and limits the ability of an IDI to offer swaps to its customers to properly hedge the risks associated with loans. To address this concern, the CFTC proposes to adopt a new exception to the de minimis calculation in paragraph (4) of the swap dealer definition that would contain requirements that mirror many of the conditions in the existing exclusion in paragraph (5) of the swap dealer definition,4 but with several key restrictions relaxed or eliminated. Unlike under the existing exclusion, under the IDI De Minimis Exception:

- a swap may be entered into more than 180 days following the execution of a loan agreement;
- a swap may be entered into more than 90 days prior to the execution of the loan agreement, provided there is an executed commitment or forward agreement for the loan at the time of the swap's execution;
- the rate, asset, liability or term underlying a swap need not be directly related to a financial term of the loan, so long as the rate, asset, liability or term underlying a swap is related to a financial term of the loan;

4 The CFTC takes the position that a joint rulemaking between the SEC and CFTC is not required with respect to changes to the de minimis exception-related factors in paragraph (4) of the swap dealer definition. See 77 Fed. Reg. at 30634 n.464 ("We do not interpret the joint rulemaking provisions of section 712(d) of the Dodd-Frank Act to require joint rulemaking here, because such an interpretation would read the term 'Commission' out of CEA section 1a(49)(D) . . . which themselves were added by the Dodd-Frank Act.")
Comparison of the Proposed Hedging De Minimis Exception to the Physical Hedging Exclusion

A person would not be required to count a swap towards the swap dealer de minimis registration threshold if the swap meets the requirements below (indicating additions and deletions from the Physical Hedging Exclusion):

- **Swaps entered into for the purpose of hedging physical positions:** In, solely for purposes of determining whether a person is a swap dealer, a swap that the person enters into shall be not be considered, if it has exceeded the aggregate gross notional amount threshold set forth in paragraph (4)(D)(A) of this definition, the person may exclude swaps that are entered into for the purpose of hedging, subject to the requirements of paragraphs (4)(D)(1) through (4)(D)(6) of this definition.
- **The person is entering into the swap for the primary purpose of reducing or otherwise mitigating one or more specific risks:** for the person, which includes, without limitation, market risk, price risk, rate risk, basis risk, credit risk, volatility risk, foreign exchange risk, liquidity risk, or similar risks arising in connection with existing or anticipated identifiable assets, liabilities, positions, contracts, or other holdings of the person or any affiliate of the person;
- **For that swap, the person is not the price maker and does not receive or earn a bid/ask spread, fee, commission, or other compensation for entering into the swap:**
- **The person enters into the swap for the purpose of offsetting or mitigating the person's price risks that arise from the potential change in the value of one or several—**
  - Assets that the person owns, produces, manufactures, processes, or merchandises or anticipates owning, producing, manufacturing, processing, or merchandising;
  - Liabilities that the person owns or anticipates incurring; or
  - Services that the person provides, purchases, or anticipates providing or purchasing;
- **The swap represents a substitute for transactions made or to be made or positions taken or to be taken by the person at a later time in a physical marketing channel;**
- **The swap is economically appropriate to the reduction of the person's risks that may arise in the conduct and management of a commercial enterprise engaged in the type of business in which the person is engaged:**
- **The swap is entered into in accordance with sound commercial business practices; and**
- **The person does not enter into the swap in connection with activity structured to evade designation as a swap dealer.**

- a swap does not have to be required by the IDI's underwriting criteria, so long as it is commercially appropriate to hedge risks incidental to the borrower's business (other than for risks associated with an excluded commodity) that may affect the borrower's ability to repay the loan;
- an IDI does not have to fund a specified percentage of a syndicated loan, but if the IDI is the source of less than 5% of a loan, the notional amount of all swaps the IDI enters into in connection with the financial terms of the loan cannot exceed the principal amount of the IDI's loan;
- the aggregate notional amount of all swaps that the customer enters into in connection with the financial terms of the loan is not capped; and
- certain loan credit default swaps and loan total return swaps may be considered valid loan structures that qualify under the exception.

The blackline provided at the end of this memorandum compares the language in the proposed IDI De Minimis Exception against the existing exclusion. The CFTC states that any swap that meets the requirements of the existing exclusion, which the proposal would retain without modification, would also meet the requirements of the proposed IDI De Minimis Exception.

**Hedging De Minimis Exception**

In defining the term swap dealer, the CFTC and SEC provided an exclusion from the de minimis registration threshold for swaps entered into by a person for purposes of hedging physical positions that satisfy specified conditions (the “Physical Hedging Exclusion”). A specific exclusion for swaps entered into for purposes of hedging financial positions was not adopted. In the proposal, the CFTC states that based on feedback from swap market participants, including in connection with Project KISS, it believes that the absence of such a specific exclusion may have caused unnecessary uncertainty in the marketplace.

To address this concern, the CFTC proposes a new exception that would be available for swaps that hedge either physical or financial positions, subject to conditions (the “Hedging De Minimis Exception”). For swaps hedging physical positions, the new exception would be available in addition to the Physical Hedging Exclusion, which the proposal would retain without modification. Like the Physical Hedging Exclusion, the Hedging De Minimis Exception would be a non-exclusive safe harbor.

To qualify for the Hedging De Minimis Exception, a swap would need to be entered into by a person for the “primary purpose of reducing or otherwise mitigating one or more specific risks” to which it is subject. Similar to the Physical Hedging Exclusion, the swap must be economically appropriate to the reduction of the risks that may arise in the conduct and management of an enterprise engaged in the type of business in which the person is engaged and must be entered into in accordance with sound business
practices. Moreover, the swap must not be entered into in connection with activity structured to evade designation as a swap dealer.

Unlike the Physical Hedging Exclusion, the Hedging De Minimis Exception contains an explicit condition that the person entering into the hedging swap must not “be the price maker of the hedging swap” and must not receive or collect a bid/ask spread, fee or commission for entering into the hedging swap (or other compensation separate from the contractual terms of the hedging swap). The CFTC explains that these requirements are designed to ensure that the Hedging De Minimis Exception is not used to exclude swap dealing activity from the de minimis calculation.

The sidebar on the previous page provides a blackline comparing the requirements of the proposed Hedging De Minimis Exception against those of the Physical Hedging Exclusion. The CFTC states that any swap that meets the requirements of the Physical Hedging Exclusion would also meet the requirements of the proposed Hedging De Minimis Exception.

**Portfolio Compression Exception**

The proposed rule would permit a person to exclude from the de minimis calculation any swap that results from multilateral portfolio compression exercises, as defined in the accompanying sidebar, to the extent that the person does not enter into these compression exercises in connection with activity structured to evade swap dealer designation. This proposal codifies relief provided by CFTC No-Action Letter 12-62. The CFTC states that multilateral portfolio compression exercises advance the policy considerations behind swap dealer regulation by reducing counterparty credit risk, lowering the aggregate gross notional amount of outstanding swaps and reducing operating risks by decreasing the number of outstanding swaps, and thus should not be counted towards a person’s de minimis calculation.

**Methodology for Calculating Notional Amounts**

Where notional amount is not a contractual term of the transaction, the methodology for calculating notional amounts may not be clear and there may not be a uniform industry standard practice. In these situations, to provide some clarity to the market, DSIO has in the past issued interpretive responses to frequently asked questions. The proposal would essentially formalize this practice by explicitly authorizing the Commission to approve or establish methodologies for calculating notional amounts for purposes of determining whether a person exceeds the de minimis registration threshold and delegating to the Director of DSIO the authority to make determinations regarding methodologies for calculating notional amounts.

**Other Considerations**

In addition to the proposed rule changes, the CFTC is seeking comment on a variety of related issues, some of which could have significant impact on registration requirements for swap dealers. These include whether the swap dealer de minimis registration threshold should:
• include a minimum dealing counterparty count threshold (e.g., 10) and transaction count threshold (e.g., 500), one or both of which would need to be breached in addition to the *de minimis* registration threshold of $8 billion before an entity is required to register as a swap dealer;
• exclude swaps that are exchange-traded and/or cleared; and
• exclude non-deliverable foreign exchange forward transactions.
Comparison of the Proposed IDI De Minimis Exception to the Existing Exclusion

A person would not be required to count a swap towards the swap dealer de minimis registration threshold if the swap meets the requirements below (indicating material additions and deletions from the existing exclusion):

- **Insured depository institution swaps in connection with originating loans to customers.** Swaps entered into by an insured depository institution have exceeded the aggregate gross notional amount threshold set forth in paragraph (4)(A) of this definition, an insured depository institution may exclude swaps entered into by the insured depository institution with a customer in connection with originating a loan with, to that customer shall not be considered in determining whether the insured depository institution is a swap dealer subject to the requirements of paragraphs (4)(II)(1) through (4)(II)(6) of this definition.

- An insured depository institution shall be considered to have entered into a swap with a customer in connection with originating a loan, as defined in paragraphs (5)(ii) and (iii) of this definition, with that customer only if:
  - **Timing of execution of swap.** The insured depository institution enters into the swap with the customer no earlier than 90 days before and no later than 180 days after the date of execution of the applicable loan agreement, or no earlier than 90 days before and no later than 180 days after any transfer of principal to the customer by the insured depository institution pursuant to the loan, unless an executed commitment or forward agreement for the applicable loan exists, in which event the 90 day restriction does not apply;
  - **Relationship of swap to loan.** The rate, asset, liability or other notional item term underlying such swap is, or is directly related to, a financial term of such loan, which includes, without limitation, the loan's duration, rate of interest, the currency or currencies in which it is made and its principal amount; or
  - Such swap is required, as a condition of the loan, either under the insured depository institution's loan underwriting criteria, to be in place or as is commercially appropriate, in order to hedge price risks incident to the borrower's business and arising from potential changes in the price of a commodity (other than for risks associated with an excluded commodity), that may affect the borrower's ability to repay the loan;
  - **Duration of swap.** The duration of the swap does not extend beyond termination of the loan;
  - **Level of funding of loan.** The insured depository institution is:
    - The sole source of funds to the customer under the loan;
    - The insured depository institution is committed to be, under the terms of the agreements related to the loan, the source of at least 10% of the maximum principal amount under the loan; or
    - If the insured depository institution is committed to be, under the terms of the agreements related to the loan, the source of a less than 10% of the maximum principal amount that is greater than zero, then the aggregate notional amount of all swaps entered into by the insured depository institution with the customer in connection with the financial terms of the loan cannot exceed the principal amount of the insured depository institution's loan;

- The aggregate notional amount of all swaps entered into by the customer in connection with the financial terms of the loan is, at any time, not more than the aggregate principal amount outstanding under the loan at that time; and

- If the swap is not accepted for clearing by a derivatives clearing organization, the insured depository institution reports the swap as required by section 4r of the Act, 7 U.S.C. 6r (except as otherwise provided in section 4r(a)(3)(A), 7 U.S.C. 6r(a)(3)(A), or section 4r(a)(3)(B), 7 U.S.C. 6r(a)(3)(B) of the Act);

- An insured depository institution shall be: The swap is considered to have originated been entered into in connection with originating a loan with a customer if the insured depository institution:
  - Directly transfers the loan amount to the customer;
  - Is a part of a syndicate of lenders that is the source of the loan amount that is transferred to the customer;
  - Purchases or receives a participation in the loan; or
  - Under the terms of the agreements related to the loan, is, or is intended to be, the source of funds for the loan; (D) Otherwise is the source of funds that are transferred to the customer pursuant to the loan or any refinancing of the loan.

- The term loan to which the swap relates shall not include:
  - Any transaction that is a sham, whether or not intended to qualify for the exclusion from the definition of the term swap dealer in this rule exception from the de minimis threshold in this definition; or
  - Any synthetic loan, including, without limitation, a loan credit default swap or loan total return swap.
Submitted by Annette L. Nazareth

American Bar Association Derivatives and Futures Law Committee Annual Winter Meeting

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"CFTC Chairman Giancarlo's White Paper Outlines Specific Recommendations to Cross-Border Swap Regulation"
CFTC Chairman Giancarlo’s White Paper Outlines Specific Recommendations to Cross-Border Swaps Regulation

By Jai R. Massari, Annette L. Nazareth, Gabriel D. Rosenberg & Meghan E. King on October 12, 2018

POSTED IN CFTC, DODD-FRANK, SWAP REGULATION, TITLE VII

After a several-year pause, the CFTC is again re-assessing its approach to cross-border regulation of swap activities. The CFTC’s current approach is embodied in various rulemakings, guidance, orders, and agreements with non-U.S. regulators that have been adopted, issued, and entered into since 2013. The CFTC has, over the past several years, periodically sought to adjust or re-evaluate its approach to cross-border swaps regulation, including in a 2016 Proposed Cross-Border Rule. CFTC Chairman Giancarlo has revived these efforts by issuing a White Paper that sets out guiding principles for the CFTC in interpreting its statutory authority to regulate cross-border swaps activities and recommends five specific areas for reform, which are described below.

While Chairman Giancarlo describes the CFTC’s current approach to cross-border swaps regulation as “over-expansive, unduly complex, and operationally impractical,” and as giving insufficient deference to jurisdictions with regulations deemed by the CFTC to be comparable to the CFTC’s (comparable jurisdictions), the practical results of the White Paper’s recommendations may be a mixed bag in terms of moving towards less expansive, less complex rules. Some recommendations, particularly those for non-U.S. CCPs, non-U.S. trading venues, and non-U.S. swap dealers in comparable jurisdictions, demonstrate a more measured approach to regulation of cross-border and non-U.S. activities. Others, such as the treatment of activities in non-comparable jurisdictions and transactions of non-U.S. persons “arranged, negotiated, or executed” in the United States (ANE), may represent a lengthening of the CFTC’s cross-border reach. In several contexts, the White Paper describes how cross-border swap activities in non-comparable jurisdictions is significantly lower than in comparable jurisdictions, indicating that the Chairman has
already, at least preliminarily, determined which jurisdictions are likely to be comparable or not.

The White Paper is not a rule proposal, nor does it have any immediate effect. It instead is intended for consideration by the full Commission. Given that the CFTC is now at full strength, and has two new Commissioners who each bring significant experience in these matters, it will be interesting to see whether and when the full Commission will take up formal rulemaking proposals. Chairman Giancarlo has hinted that a rulemaking focusing on amendments to the swap execution facility (SEF) rules, consistent with his first white paper on that topic, will be forthcoming shortly.

We describe the White Paper's key cross-border reform proposals below, highlighting how these proposals would modify currently applicable requirements.

Registration of Non-U.S. CCPs

Under the CEA and CFTC guidance, a non-U.S. CCP may not provide clearing services to U.S. customers without being registered as a derivatives clearing organization (DCO). The CFTC has, to date, individually exempted four non-U.S. CCPs from its DCO registration requirements, permitting them to clear the proprietary swap positions of U.S. clearing members and their affiliates, without being so registered. Even an exempted non-U.S. CCP may not clear for U.S. customers of a non-U.S. or U.S. clearing member. This limitation has posed challenges for both non-U.S. CCPs and U.S. market participants, as swap clearing requirements have come into effect in more jurisdictions and uncleared swap margin requirements are fully implemented, which may encourage the largest market participants to prefer cleared transactions.

The White Paper recommends expanding the use of the CFTC's exemptive authority for non-U.S. CCPs that (1) are subject to comparable, comprehensive supervision and regulation in their home countries and (2) do not pose substantial risk to the U.S. financial system. These CCPs would be permitted to provide clearing services to U.S. customers indirectly through non-U.S. clearing members, without the non-U.S. CCP having to register as a DCO or its non-U.S. clearing members having to register as FCMs. This approach addresses the limitation of the exemptive orders granted to date and is consistent with the CFTC's cross-border approach to futures clearing.
Non-U.S. CCPs that are deemed by the CFTC to pose substantial risk to the U.S. financial system or that are in non-comparable jurisdictions would continue to be required to register with the CFTC as DCOs if they provide clearing services to U.S. customers.

Registration of Non-U.S. Trading Venues

Currently, other than for certain specified EU trading venues, the CFTC's SEF registration requirement applies to any multilateral swap trading platform located outside the United States, if the venue directly or indirectly permits access to U.S. persons or persons located in the United States, including personnel and agents of non-U.S. persons located in the United States. Consistent with Chairman Giancarlo's long-standing views on the harms of the bifurcation of trading pools, the White Paper recommends additional deference to local law for non-U.S. swap trading venues in comparable jurisdictions. Specifically, the White Paper recommends that a non-U.S. swap trading venue located in a comparable jurisdiction be exempt from the CFTC's SEF registration requirements even where it provides direct or indirect access to U.S. persons that are ECPs. This approach is consistent with the treatment of derivatives trading venues in the 2017 CFTC – EC agreement, under which MTFs and OTFs are exempt from CFTC SEF registration requirements and CFTC regulation of DCMs and SEFs is deemed equivalent to the relevant requirements in the EU.

Trading venues in non-comparable jurisdictions would be required to register as SEFs (or DCMs) if they provide direct or indirect access to U.S. persons. This registration requirement would, however, be subject to a materiality threshold to be set by the CFTC based on criteria designed to reflect a level of trading involving U.S. persons that would not rise to the "direct and significant" standard of Section 2(i) of the CEA.

Non-U.S. Swap Dealer Registration and Regulation

While recognizing that the activities of a non-U.S. swap dealer may pose "direct and significant" risks to the U.S. financial system, the White Paper challenges the existing calibration of the 2013 Cross-Border Guidance's requirements for non-U.S. swap dealers under this standard. For example, the White Paper suggests that the CFTC should take into account the effects of non-U.S. regulatory regimes, including
mandatory clearing, in determining whether swap activities give rise to direct and significant risks it the U.S. financial system.

The White Paper recommends modifications to the CFTC current guidelines for non-U.S. persons in measuring their swap dealing activities towards the swap dealer de minimis registration threshold and in the availability of substituted compliance for non-U.S. swap dealers.

- **Guaranteed Entity.** A non-U.S. person whose swaps are guaranteed by a U.S. person would need to count all dealing swaps toward its de minimis A Guaranteed Entity in a comparable jurisdiction would be eligible for substituted compliance with the applicable requirements. This de minimis counting requirement is generally consistent with the approach in the 2013 Cross-Border Guidance and the 2016 Proposed Cross-Border Rule, but the White Paper recommends making substituted compliance more broadly available to a Guaranteed Entity that is a registered swap dealer.

- **Foreign Consolidated Subsidiaries (FCS)\(^{[1]}\) and other non-U.S. Persons.** The White Paper recommends that FCS in comparable jurisdictions and all other non-U.S. persons should count dealing swaps only with U.S. persons and Guaranteed Entities. They further would be able to exclude swaps (1) with a Guaranteed Entity that is a CFTC-registered swap dealer or is affiliated with a registered swap dealer; (2) with a Guaranteed Entity guaranteed by a non-financial guarantor; or (3) with the foreign branch of a U.S. bank that is a CFTC-registered swap dealer. This recommendation represents a scaling back of de minimis threshold requirements proposed in 2016, particularly as they relate to FCS. Under the 2016 Proposed Cross-Border Rule, an FCS would have had to count dealing swaps with all persons towards its de minimis In addition, a non-U.S. person would have had to count dealing swaps with FCS toward its de minimis threshold. The White Paper does not make a specific recommendation on the treatment of FCS in non-comparable jurisdictions, on the basis that the treatment of such FCS “raises more complex issues.”

In addition, the White Paper recommends that FCS and non-U.S. persons in comparable jurisdictions should be permitted to rely on substituted compliance with the applicable requirements, which would make substituted compliance more broadly available.
Clearing and Trade Execution

The White Paper recommends that the CFTC give more deference to clearing and trade execution requirements in jurisdictions with comparable regulation. It also recommends the CFTC apply more scrutiny in determining whether a non-U.S. clearing requirement is comparable to the CFTC’s than when making such a determination for a non-U.S. trade execution requirement. This recommendation is based on the clearing requirement being more central to systemic risk considerations. Trade execution, in contrast, relates to market structure and trade practices which Chairman Giancarlo believes is more appropriately in the purview of the local regulators.

In terms of application of the CFTC’s clearing and trade execution requirements, the White Paper would broaden the availability of substituted compliance in comparable jurisdictions for some transactions of non-U.S. persons. Specifically, it recommends that a non-U.S. person, including a Guaranteed Entity or an FCS, in a comparable jurisdiction be permitted to rely on substituted compliance for the CFTC’s swap clearing and trade execution requirements, regardless of counterparty type. Thus, a non-U.S. person could comply with a local clearing requirement under local standards when executing a swap in a jurisdiction with comparable regulation with a U.S. person counterparty. Under the 2013 Cross-Border Guidance, substituted compliance is not be available for a non-U.S. person when transacting with a U.S. person.

For non-comparable jurisdictions, the White Paper recommends differing application of the clearing requirements based upon whether a U.S. person is a foreign branch of a U.S. bank, a Guaranteed Entity, or another non-U.S. person. The White Paper makes no specific recommendation on the treatment of FCS under this requirement. The White Paper also does not outline an approach to the application of the CFTC’s trade execution requirement in non-comparable jurisdictions and notes that it may be better to deal with these non-U.S. jurisdictions on a case-by-case basis.

ANE Transactions

Under CFTC staff-no action letters, a swap between two non-U.S. persons does not become subject to CFTC transaction-level regulations by virtue of being ANE in the United States. The White Paper re-examines the treatment of such ANE swaps, including based upon whether a counterparty is located in a comparable jurisdiction.
The White Paper champions the principle of “one unified marketplace, under one set of comparable trading rules and under one competent regulator” in considering ANE transactions.

The White Paper makes two general points about the application of swaps regulations to ANE transactions: (1) if a swap is executed in the United States, U.S. swap trade execution and clearing rules should apply and (2) a swap ANE in the United States by personnel or agents of a non-U.S. person should not be counted toward the non-U.S. person’s *de minimis* threshold if the non-U.S. dealer is in a comparable jurisdiction. The White Paper also suggests that swaps between non-U.S. persons arranged or negotiated on a SEF should be subject to U.S. regulations, by virtue of being arranged or negotiated subject to the rules of the SEF, and that a swap bilaterally arranged and negotiated (but not executed) in the United States is a “U.S. trade” also subject to CFTC rules, though substituted compliance may be appropriate. The White Paper suggests that the CFTC staff will need to further consider these issues and recommends that they attempt to draw regulatory lines that capture ANE transaction activity that has a direct and significant effect on the U.S. financial system and exclude other more incidental activity.

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[1] Section 2(i) of the Commodity Exchange Act (CEA) prohibits the CFTC from regulating swap 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. 7 U.S.C. § 2(i).


[3] FCS are non-U.S. persons whose operating results, financial position, and statement of cash flows are consolidated, in accordance with U.S. Generally Accepted Accounting Principles, with those of an ultimate parent entity that is a U.S. person.

Submitted by Annette L. Nazareth
American Bar Association Derivatives and Futures Law Committee Annual Winter Meeting
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"CFTC Staff Provides Time Limited De Minimis Relief to a Regional BHC and its IDI Subsidiaries"
CFTC Staff Provides Time Limited *De Minimis* Relief to a Regional BHC and its IDI Subsidiaries

By Annette L. Nazareth & Hilary Sunghee Seo on September 7, 2018

POSTED IN BANK REGULATION, SWAP REGULATION

Last week, the CFTC’s Division of Swap Dealer and Intermediary Oversight ("DSIO") issued time limited no-action relief to a regional commercial bank holding company and its insured depository institution ("IDI") subsidiaries from having to count certain loan-related swaps toward its swap dealer *de minimis* threshold. Currently, an IDI is permitted to exclude from its *de minimis* threshold calculation swaps entered into with customers in connection with originating a loan, provided various conditions are satisfied (the "IDI Exclusion"). One of those conditions is that the swap be entered into no later than 180 days after the date of the execution of the applicable loan agreement or transfer of principal to the customer (the "180 Day Requirement"). The no-action relief would permit an IDI to exclude swaps from its *de minimis* threshold calculation during the relief period if the swap would satisfy the IDI Exclusion but for the 180 Day Requirement and the swap counterparty is an existing loan client whose annual revenues are under $750 million. In addition, the aggregate notional amount of swaps entered into in reliance of the no-action relief must not exceed $1.5 billion at any time during the relief period. The relief terminates on December 31, 2018, at which point the aggregate notional amount of dealing swaps entered into by the IDI and its affiliates (excluding any affiliate that is registered as a swap dealer) for the previous 12 months would need to be below the $8 billion *de minimis* threshold or the requirement to register as a swap dealer would be triggered.

In the request for relief, the banking group represented that a meaningful number of its clients are small and medium-sized commercial entities that have long established relationships with the group and look to it and its IDI subsidiaries to help their overall capital and risk mitigation needs. Given historically low interest rates, many of those clients chose not to enter into swaps to hedge interest rate risks at
the time of a loan. Due to recent changes in the interest rate environment, clients now wish to enter into swaps to hedge their loan-related risks. If outside the 180 day window, however, those swaps would not qualify for the IDI Exception. The banking group noted that this phenomenon was creating a temporary spike in demand for swaps that would not qualify for the IDI Exclusion and placed its IDI subsidiaries in the untenable position of either having to turn away those small and medium-sized commercial clients – who typically do not have established trading relationships with other swap dealers and may find it challenging to quickly find a cost effective alternative provider in an environment where speed is important due to fast changing interest rates – or be forced to breach the de minimis threshold and have to register as a swap dealer, even though their business models and swap dealing volumes would not make it commercially feasible to sustain such registration status. The letter pointed out that neither of these outcomes would be consistent with the CFTC's policy goal of supporting small and regional banks' ancillary dealing activities to meet end-users' risk mitigation needs.

Recently, the CFTC proposed a new exception to the de minimis threshold calculation that would have the effect of relaxing some of the conditions to the existing IDI Exclusion. If adopted as proposed, it would be possible for IDIs to exclude from their de minimis threshold calculation loan related swaps entered into more than 180 days following the execution of a loan agreement, provided the other specified conditions in the rule are satisfied.
Submitted by Annette L. Nazareth

American Bar Association Derivatives and Futures Law Committee Annual Winter Meeting
Naples, Florida (January 2019)

“CFTC Adopts Final Rule Amendments Simplifying CCO Duties and Annual Report Rules for FCMs, Swap Dealers and MSPs”
CFTC Adopts Final Rule Amendments Simplifying CCO Duties and Annual Report Rules for FCMs, Swap Dealers and MSPs

By Annette L. Nazareth & Meghan E. King on August 29, 2018

POSTED IN CFTC, DODD-FRANK, FINAL RULE, SWAP REGULATION, TITLE VII

The CFTC unanimously approved Final Rule amendments on August 21, 2018 to the regulations governing chief compliance officer ("CCO") duties and annual compliance reporting requirements for FCMs, swap dealers and MSPs ("Registrants"). These amendments are the first substantive rule amendments to be adopted under Chairman Giancarlo’s Project KISS—an agency-wide effort to simplify and modernize CFTC rules, regulations and practices to make them more efficient and less onerous for regulated entities.

As amended, the Final Rule:

- Eliminates the requirement that the CCO annual report address “each” applicable regulatory requirement when assessing its written policies and procedures.

- Permits dual Registrants to submit a single CCO annual report covering the annual reporting requirements relevant to multiple registration categories.

- Permits affiliated Registrants to incorporate by reference in their CCO annual reports sections from an annual report prepared by an affiliated Registrant within the current or immediately preceding reporting period.

- Modifies CCO responsibilities by:
  - adding “in all material respects” to the requirement to certify that information in the CCO annual report is accurate and complete;
- clarifying that the CCO must take “reasonable steps” to (i) resolve material conflicts of interest, (ii) ensure that the Registrant establishes, maintains and reviews written policies and procedures for the remediation of noncompliance issues, and (iii) ensure that the Registrant establishes written procedures for the handling of noncompliance issues;
- removing the requirement to consult with the board or senior officer in connection with establishing procedures for addressing noncompliance issues. The CFTC notes that routine noncompliance issues may be resolved in the normal course of business; and
- limiting the CCO’s duty to administer policies and procedures to those specifically related to the Registrant’s business as an FCM, swap dealer or MSP, as applicable.

- Implements technical changes that largely align with market practice and the SEC’s analogous rules for security-based swap dealers. Consistent with the CFTC’s goal of harmonizing its rules with those of the SEC, the changes include:
  - clarifying the reporting line of the CCO by defining the term “senior officer” as “the chief executive officer or other equivalent officer of a registrant”;
  - requiring that if the Registrant has an audit committee, then the CCO shall furnish the CCO annual report to the audit committee not later than its next scheduled meeting after the date on which the CCO annual report is furnished to the CFTC, but in no event more than 90 days after the Registrant provides the CFTC with such report; and
  - clarifying that the resources discussion in the CCO annual report should be limited to those resources allocated to the specific activities for which the entity is registered.

The CFTC confirmed in the adopting release that any existing substituted compliance determinations relating to the CCO rules are not affected by the rulemaking. The CFTC also expressly declined to address the requirement that the Volcker Rule compliance program be included in the CCO annual report. The adopting release notes, however, that the CFTC may address the requirement in future guidance or rulemakings.
In addition to the Final Rule, the CFTC also provided updated guidance in a new Appendix C to Part 3 regarding the CCO annual report's form and content. Appendix C supersedes CFTC Staff Advisory No. 14-153. The appendix provides greater clarity on the form and content of the CCO annual report, including that:

- the description of written policies and procedures may be appropriately brief;
- the CFTC expects a comprehensive description of the assessment process and the results of the effectiveness of the assessment;
- the CCO annual report contain the identification and discussion of each area of improvement and the discussion of what changes are recommended to address each area of improvement;
- for each area of improvement, the CCO annual report should include a discussion of the proposed improvements, the time frame for their implementation and cross-references to the regulation(s) that the recommended changes would address;
- the discussion of areas for improvement and recommended changes should reflect continuity from one reporting cycle to the next, such that CCO annual reports filed in the current cycle address the outcomes, monitoring and testing of changes that were proposed in the prior cycle, to the extent such changes were implemented in the current period;
- the CCO annual report describe the standard used to determine a noncompliance event's materiality, a description of each material noncompliance event, discussion on the course of remediation, how the implementation of remediation is being executed, any testing of the remediation and the results from such testing; and
- the discussion of resources set aside for compliance with the Commodity Exchange Act and CFTC regulations should contain the following specific types of information:
  - budget allocated;
  - full-time compliance staffing levels;
  - partially allocated staff counts (if applicable), with information on how much of each employee's time is devoted to such compliance;
  - managerial resources;
• general infrastructure information;
• if applicable, use of third-party vendors and outsourcing; and
• any material deficiencies in compliance resources, and if there are no material deficiencies in the resources devoted to compliance, an express statement to that effect.

The Final Rule will be effective on September 26, 2018. This means that Registrants with fiscal years ending June 30th should comply with the amendments, as their reports are due at the end of September. It is unclear whether this tight deadline will pose challenges to such Registrants, since most of the amendments streamline or simplify existing requirements.

Law Clerk Daniela Dekhtyar-McCarthy contributed to this post.
Submitted by Kenneth M. Raisler

American Bar Association Derivatives and Futures Law Committee Annual Winter Meeting

Naples, Florida (January 2019)

CFTC Chairman Releases White Paper on “Cross-Border Swaps Regulation Version 2.0”

White Paper Proposes New Approach to Providing Exemptions and Other Relief from CFTC’s Dodd-Frank Swaps Rules for Certain Non-U.S. Clearinghouses, Trading Venues, and Swap Dealing Businesses
SUMMARY
On October 1, 2018, Commodity Futures Trading Commission ("CFTC") Chairman Christopher Giancarlo released a white paper titled “Cross-Border Swaps Regulation Version 2.0: A Risk-Based Approach with Deference to Comparable Non-U.S. Regulation” (the “White Paper”). The release of the White Paper follows Chairman Giancarlo’s remarks at a City of London event on September 4, 2018 and directs the CFTC to modify its approach to cross-border regulation in a way that is “better calibrated to mitigate systemic risk” and that fosters “innovation, competition, and international cooperation.”

The White Paper begins with a broad review of U.S. and global swaps reform efforts and then sets forth a set of principles to guide the cross-border application of the CFTC’s Dodd-Frank swaps rules. Next, it reviews the CFTC’s approach to applying its Dodd-Frank swaps rules in the cross-border context and recommends a series of improvements, exemptions and relief that would address non-U.S. clearinghouses, trading venues, and swap dealing businesses.

PRINCIPLES TO GUIDE THE CROSS-BORDER APPLICATION OF THE CFTC’S SWAPS RULES
The White Paper acknowledges that, among regulators of the world’s major derivatives markets, the CFTC was the first regulatory agency to implement most of the swaps market reforms agreed upon by the G20. However, the White Paper goes on to observe that, as other jurisdictions have now adopted swap reforms, the CFTC’s early approach and its over-expansive assertion of jurisdiction is resulting in increased transaction costs and a fragmented global swaps market. From these observations, the White Paper identifies six principles that it asserts should guide the reform of the cross-border application of the CFTC’s Dodd-Frank swaps rules:

- **Principle 1**: The CFTC should recognize the distinction between swaps reforms intended to mitigate systemic risk and reforms designed to address particular market and trading practices that may be adapted appropriately to local market conditions.

  The White Paper draws a distinction between swaps reforms that are “designed to mitigate systemic risk” – such as swaps clearing, margin for uncleared swaps, dealer capital, and recordkeeping and regulatory reporting – and swaps reforms that “address market and trading practices” – such as public trade reporting and price transparency, trading platform design, trade
execution methodologies and mechanics, and personnel qualifications, examinations and regulatory oversight. Reforms in the former category seek to mitigate the type of risk that may have a “direct and significant” connection with the United States, while reforms in the latter category are adapted to each specific jurisdiction and thus lack such a “direct and significant” connection with the United States. Based upon this distinction, the White Paper recommends that regulations addressing market and trading practices should be of secondary importance when the CFTC determines the extraterritorial application of its swaps rules.

- **Principle 2: The CFTC should pursue multilateralism, not unilateralism, for swaps reforms that are designed to mitigate systemic risk.**

  The White Paper suggests that the CFTC pursue multilateralism in its cross-border approach and exercise deference to the regulatory frameworks of its non-U.S. counterparts. Comity, not uniformity, should inform the CFTC’s approach and it should ensure that its rules do not unnecessarily conflict with the rules of its non-U.S. counterparts. Multilateralism also requires the CFTC to be committed to the work of international bodies, such as the International Organization of Securities Commissions (IOSCO) and Financial Stability Board (FSB) and other governmental or industry groups such as the committee on Payments and Market Infrastructures (CPMI)-IOSCO, the Basel Committee on Banking Supervision (BCBS)-IOSCO, and the OTC Derivatives Coordination Group, as high-quality international standards can facilitate regulatory coordination between the CFTC and non-U.S. regulatory bodies.

- **Principle 3: The current division of global swaps market into separate U.S. person and non-U.S. person marketplaces should be ended. Markets in regulatory jurisdictions that have adopted the G20 swaps reforms should each function as a unified marketplace, under one set of comparable trading rules and under one competent regulator.**

  According to the White Paper, the implementation of the CFTC’s swap execution facility (SEF) regime in 2013 and mandatory SEF trading in 2014 has caused fragmentation of global swaps markets. Major financial centers around the globe have been forced to create separate execution facilities for U.S. market participants and non-U.S. market participants to engage in swaps trading. Such fragmentation not only increases price and transaction volatility, but also diminishes these markets’ resilience in the event of global market shocks. The White Paper advocates that this fragmentation should be reduced by having each regulatory jurisdiction that has adopted G20 swaps reforms function as a unified marketplace with one set of comparable trading rules.

- **Principle 4: The CFTC shall be a rule maker, not a rule taker, in overseeing U.S. markets.**

  The CFTC is statutorily empowered to oversee and regulate the U.S. derivatives trading markets, and therefore entitled to the deference of non-U.S. regulators for its regulation of activities conducted within the U.S. The White Paper observes that, while it should work cooperatively with international efforts and seek to reconcile its rules with those adopted by non-U.S. regulators, the
CFTC has discretion to impose regulation different from that of its non-U.S. counterparts if the
CFTC deems it appropriate to do so.

- **Principle 5:** The CFTC should act with deference to non-U.S. regulators in jurisdictions that have
  adopted comparable G20 swaps reforms, seeking stricter comparability for substituted
  compliance for requirements intended to address systemic risk and more flexible comparability for
  substituted compliance for requirements intended to address market and trading practices.

Substituted compliance is a key component of the CFTC’s cross-border approach, allowing non-
U.S. entities to satisfy the CFTC’s requirements by complying with comparable rules promulgated
by regulatory bodies in their home jurisdictions. So far, however, the CFTC has conducted its
substituted compliance analysis through “granular, rule-by-rule comparison,” without tailoring its
approach to different types of requirements. The White Paper recommends a bifurcated
approach to substituted compliance analysis. For requirements that address jurisdiction-specific
market and trading practices, the CFTC should adopt a more flexible standard, focusing on
whether a non-U.S. regulator’s regime, in the aggregate, can achieve comparable regulatory
outcomes to CFTC regulation. By contrast, for requirements that address systemic risk, such as
requirements for regulatory reporting, the standard should be stricter and the CFTC should look
into the details of the regulation of its non-U.S. counterparts. The non-U.S. regulator must show
a high degree of comparability to achieve substituted compliance for these requirements.

- **Principle 6:** The CFTC should act to encourage adoption of comparable swaps reform regulation
  in non-U.S. jurisdictions that have not adopted swaps reform for any significant swaps trading
  activity.

The White Paper advocates deference for non-U.S. jurisdictions that have adopted G20 swaps
reforms comparable to the CFTC’s regime. For non-U.S. jurisdictions that have not adopted such
reforms, the White Paper recommends applying U.S. rules to U.S.-related entities, subject to
materiality thresholds, instead of taking a deferential approach.

**SPECIFIC RECOMMENDATIONS**

Based on the six principles set forth above, the White Paper makes certain recommendations for the
CFTC’s cross-border approach to non-U.S. central counterparties (“CCPs”), non-U.S. trading venues,
non-U.S. swap dealers, clearing and trade execution requirements and ANE transactions. The
recommendations follow a general framework that would seek to impose regulation based on whether
the regulated entities or swap activities are based in (1) the United States, (2) a Comparable Jurisdiction
(jurisdictions that have adopted reforms comparable to the CFTC’s regime) or (3) a Non-Comparable
Jurisdiction (jurisdictions that have not adopted reforms comparable to the CFTC’s regime).

Key recommendations of the White Paper are described below, and the definitions of certain key terms
used in the White Paper are attached to this Memorandum as Appendix A.
Non-U.S. Central Counterparties

In 2016, the CFTC and the European Commission (the “EC”) agreed to a common approach to cross-border swaps CCPs (the “2016 Agreement”). The White Paper acknowledges the historical significance of the 2016 Agreement and recommends that the CFTC build upon the 2016 Agreement and its framework of comity to develop a new approach towards the cross-border regulation of non-U.S. CCPs.

1) United States

The CFTC should continue to require a CCP located within the United States that seeks to clear swaps to register with the CFTC and be subject to the CFTC’s full oversight and regulation.

2) Comparable Jurisdictions

Title VII of the Dodd-Frank Act permits the CFTC to exempt a non-U.S. CCP from registration for the clearing of swaps if the CFTC determines that the CCP is subject to “comparable, comprehensive supervision and regulation” by appropriate government authorities in the CCP’s home country. The comparability determination focuses on whether the home country’s supervisory and regulatory framework can achieve a “comparable outcome” as the CFTC’s regulation of registered Derivatives Clearing Organizations (“DCO”). In the past the CFTC has already exercised its authority to exempt certain non-U.S. CCPs, but the White Paper recommends that the CFTC expand the use of this authority for non-U.S. CCPs that do not pose substantial risk to the U.S. financial system. Under the proposed approach, exempted non-U.S. CCPs would be permitted to provide clearing services to U.S. customers indirectly through non-U.S. clearing members, without the non-U.S. CCP or its non-U.S. clearing members having to register as a DCO or Futures Commission Merchant (“FCM”), respectively.

However, non-U.S. CCPs that clear swaps for U.S. persons and are deemed by the CFTC to “pose substantial risk specific to the U.S. financial system” would continue to be required to register with and be regulated by the CFTC, even if they are located in a Comparable Jurisdiction.

3) Non-Comparable Jurisdictions

For non-U.S. CCPs in Non-Comparable Jurisdictions that seek to clear swaps for U.S. persons, the White Paper recommends that they be required to register as DCOs with the CFTC. The White Paper also suggests that the CFTC consider providing relief from DCO registration for non-U.S. CCPs whose members are foreign branches of U.S. banks that are registered as swap dealers (the “Foreign Branches”). The Foreign Branches would be required to limit their clearing activities to proprietary and affiliate accounts or clearing customers that are non-U.S. persons. The relief is also subject to reporting by the non-U.S.
CCPs and the negotiation and execution of a Memorandum of Understanding (MOU) with the non-U.S. CCP’s home country regulator.

Non-U.S. Trading Venues
Under the Commodity Exchange Act (the “CEA”), no person may operate a facility for the trading or processing of swaps unless the facility is registered as an SEF or designated contract market (DCM). The CFTC currently requires registration of all non-U.S. trading venues, and some non-U.S. trading platforms have excluded U.S. market participants in order to avoid compliance with this registration requirement. To remedy this situation, the White Paper proposes the following changes:

1) United States
For swap trading venues located within the United States that meet the definition of SEF in Section 1a(50) of the CEA, the CFTC should continue to require registration as an SEF or DCM with the CFTC.

2) Comparable Jurisdictions
Title VII of the Dodd-Frank Act permits the CFTC to exempt, conditionally or unconditionally, a non-U.S. swaps trading venue from registration based on the CFTC’s comparability determination. The White Paper recommends a general exemption from SEF registration for non-U.S. trading venues that are regulated in Comparable Jurisdictions with respect to all types of swaps. This would permit non-U.S. trading venues to have U.S. participants without being required to register with the CFTC, and would also permit U.S. participants to satisfy their trade execution requirements on those platforms.

3) Non-Comparable Jurisdictions
The White Paper recommends the general approach of requiring non-U.S. trading venues in Non-Comparable Jurisdictions to register as SEFs or DCMs “if they provide U.S. persons access to the trading venue directly or indirectly through a non-U.S. intermediary, subject to an appropriate materiality threshold.” While the precise standard for the materiality threshold should be determined by the CFTC based on appropriate data, it should be based on “a level of trading involving U.S. persons that does not meet the Section 2(i) ‘direct and significant’ standard,” so as to allow non-U.S. trading venues in Non-Comparable Jurisdictions to provide trading services to U.S. persons on a limited basis without registration.

Non-U.S. Swap Dealers
A person is deemed to be a swap dealer as a result of its swap dealing activity if, during the preceding 12 months, the aggregate gross notional amount of the swap dealing exceeds the de minimis threshold. The rule’s domestic application is relatively straightforward. Extraterritorially, the CFTC has divided non-U.S. swap dealers into three categories based on the different levels of risk they pose to the United States:
Guaranteed Entities, Foreign Consolidated Subsidiaries (FCS) and Other Non-U.S. Persons. The White Paper points out that the current approach of the CFTC with respect to non-U.S. swap dealers fails to properly take into consideration whether the activity of non-U.S. swap dealers truly poses a “direct and significant” risk to the U.S. financial system and is therefore overly broad in its application. To properly assess whether an activity poses a “direct and significant” risk, the White Paper makes the following recommendations:

1) **United States**
   
   The CFTC should continue to require U.S. persons to count all of their swap dealing transactions toward the *de minimis* threshold, including transactions conducted through a Foreign Branch, whether with U.S. or non-U.S. persons.

2) **Comparable Jurisdictions**
   
   Guaranteed Entities should be required to count all of their swap dealing activity toward their *de minimis* threshold, regardless of the status of their counterparties. FCSs and Other Non-U.S. Persons should be required to count swap dealing activity with U.S. persons and Guaranteed Entities, except swaps with: (1) Guaranteed Entities that are registered as swap dealers (or are affiliated with a registered swap dealer); (2) Guaranteed Entities that are guaranteed by a non-financial guarantor; or (3) Foreign Branches of U.S. banks that are registered as swap dealers. Guaranteed Entities, FCSs and Other Non-U.S. Persons should be able to rely on substituted compliance with respect to applicable requirements. In addition, all non-U.S. dealers should be permitted to exclude from their *de minimis* threshold swaps executed anonymously on a registered or exempt SEF, DCM, or Foreign Boards of Trade (FBOT) and cleared by a registered or exempt clearing organization, even if the dealing activity involves U.S. persons.

3) **Non-Comparable Jurisdictions**
   
   For Guaranteed Entities and Other Non-U.S. Persons in Non-Comparable Jurisdictions, the recommended approach is the same as that in Comparable Jurisdictions. The treatment of FCSs is more complex, and depends on the status of an FCS. For example, FCSs that are part of bank holding companies and are subject to consolidated supervision and regulation by the Federal Reserve Board should be permitted to limit the swaps they would need to count toward its *de minimis* threshold (possibly subject to a materiality threshold). For FCSs that are part of non-financial organizations headquartered in the United States, it may be appropriate to treat them as Other Non-U.S. Persons as they do not pose systemic risk to the U.S. financial system.
Clearing and Trade Execution Requirements
The White Paper points out that swaps clearing and trade execution requirements have different policy objectives – “swaps clearing is focused primarily on managing and mutualizing the accumulation of counterparty credit risk; whereas swaps trade execution is primarily concerned with market integrity and trade practice issues.” Based on this distinction, the White Paper recommends the following approach:

1) United States
For U.S. persons (including Foreign Branches), the CFTC’s swaps clearing and trade execution requirements should remain unchanged for all applicable swaps, unless an exception or exemption applies.

2) Comparable Jurisdictions
Substituted compliance would allow a non-U.S. person, including a Guaranteed Entity and an FCS, in Comparable Jurisdictions to satisfy the CFTC’s clearing and trade execution requirements by complying with the rules of its home jurisdiction. Because of the different policy objectives of clearing and trade execution requirements, the CFTC must apply different standards when engaging in substituted compliance analysis – a stricter standard for reviewing clearing requirements and a more flexible, outcome-focused standard for reviewing trade execution requirements.

3) Non-Comparable Jurisdictions
The application of the CFTC’s swap clearing requirements in Non-Comparable Jurisdictions is more complex. All swaps of Foreign Branches that are subject to the clearing requirements should continue to be subject to such requirements, except for swaps with Other Non-U.S. Persons in Non-Comparable Jurisdictions, which are subject to the clearing requirements only if they meet a materiality threshold. The CFTC’s clearing requirements would also apply to all applicable swaps between Guaranteed Entities and: (1) U.S. persons, including Foreign Branches; (2) Guaranteed Entities; and (3) Other Non-U.S. Persons, unless the swaps are subject to initial and variation margin requirements for uncleared swaps that are consistent with the standards established by the BCBS-IOSCO Working Group on Margining Requirements. The same treatment applies to all applicable swaps between Other Non-U.S. Persons and (1) U.S. persons, including Foreign Branches and (2) Guaranteed Entities. The White Paper notes that the clearing requirements for FCSs will need to be developed by the CFTC at a later time, as the correct approach will depend on the treatment of FCSs under other CFTC cross-border rules.

ANE Transactions
The White Paper advocates a territorial approach to the regulation of ANE Transactions (swap transactions between two non-U.S. counterparties that are “arranged, negotiated, or executed” within the
United States by personnel or agents of a non-U.S. person located in the United States). The White Paper notes that its suggestions for ANE Transactions should be read in conjunction with the proposals put forth in the April 2018 CFTC White Paper, written by Chairman Giancarlo and Bruce Tuckman, titled “Swaps Regulation Version 2.0: An Assessment of the Current Implementation of Reform and Proposals for Next Steps.”

Chairman Giancarlo sets forth two preliminary points for the proposed approach to regulating ANE Transactions: first, if a swap is executed in the United States, the territorial approach would require the counterparties to follow the CFTC trade execution rules; second, ANE Transactions, by their definition, do not pose systemic risk to the U.S. financial system and should not be counted toward the \textit{de minimis} threshold for non-U.S. dealers in Comparable Jurisdictions. The White Paper then analyzes two scenarios where ANE Transactions may occur:

1. A third-party U.S. intermediary located in the United States, such as an Introducing Broker (IB), arranges or negotiates swaps among multiple non-U.S. participants. In this scenario, the U.S. intermediary should be an SEF under the approach to SEF registration advocated in the April 2018 White Paper, and the execution of the trade would be subject to the rules of the SEF.

2. A U.S.-based agent/employee of a non-U.S. swap dealer arranges or negotiates a swap by the non-U.S. swap dealer with a non-U.S. person, where the trade is executed and booked outside the United States. The U.S.-based agent/employee’s activity happens within the United States, which makes this transaction a U.S. trade and subject to U.S. execution rules under the White Paper’s territorial approach.

Based on the principles set forth in the White Paper, Chairman Giancarlo intends to direct the CFTC staff to develop and publish new rule proposals to address a range of cross-border issues in swaps reform – from the registration and regulation of swap dealers and major swap participants to the registration of non-U.S. CCPs and swaps trading venues. The resulting rulemakings would replace the cross-border guidance issued by the CFTC in 2013 and the cross-border rules proposed by the CFTC in 2016, as well as address certain positions taken in CFTC staff advisories and no-action letters.

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Appendix: Core Definitions

U.S. Person Definition

“U.S. person” is defined to mean:

1. A natural person who is a resident of the United States;
2. An estate of a decedent who was a resident of the United States at the time of death;
3. A corporation, partnership, limited liability company, business or other trust, association, joint-stock company, fund or any form of entity similar to any of the foregoing (other than an entity described in paragraph (1) or (5) (legal entity), in each case that is organized or incorporated under the laws of the United States or that has its principal place of business in the United States, including any branch of the legal entity;
4. A pension plan for the employees, officers or principals of a legal entity described in paragraph (3) above, unless the pension plan is primarily for foreign employees of such entity;
5. A 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;
6. A 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 owned by one or more persons described in paragraphs (1) through (5) above and for which such person(s) bears unlimited responsibility for the obligations and liabilities of the legal entity, including any branch of the legal entity; or
7. An 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 paragraphs (1) through (6) above.

Definition of Foreign Branch

A “foreign branch” is a non-U.S. branch of a U.S. swap dealer that:

1. Is a “foreign branch,” as defined in the applicable banking regulation, of a U.S. bank that is subject to Regulation K or the FDIC International Banking Regulation;
2. 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; and
3. Is subject to substantive regulation in banking or financing in the jurisdiction where it is located.

The CFTC also will consider other relevant facts and circumstances.

Meaning of the Term “Guaranteed”

A “guarantee” would include arrangements, pursuant to which one party to a swap has rights of recourse against a guarantor, with respect to its counterparty’s obligations under the swap. For these purposes, a party to a swap has rights of recourse against a guarantor if the party has a conditional or unconditional legally enforceable right to receive or otherwise collect, in whole or in part, payments from the guarantor with respect to its counterparty’s obligations under the swap.

This “guarantee” definition also encompasses any arrangement pursuant to which the guarantor itself has a conditional or unconditional legally enforceable right to receive or otherwise collect, in whole or in part, payments from any other guarantor with respect to the counterparty’s obligations under the swap.
The Definition of “Foreign Consolidated Subsidiary”

“Foreign consolidated subsidiary” is defined to mean a non-U.S. person in which an ultimate parent entity that is a U.S. person (“U.S. ultimate parent entity”) has a controlling financial interest, in accordance with U.S. generally accepted accounting principles, such that the U.S. ultimate parent entity includes the non-U.S. person’s operating results, financial position and statement of cash flows in the U.S. ultimate parent entity’s consolidated financial statements, in accordance with U.S. generally accepted accounting principles.

The term “U.S. ultimate parent entity” is defined to mean the parent entity in a consolidated group in which none of the other entities in the consolidated group has a controlling interest, in accordance with U.S. generally accepted accounting principles.
Ten years ago, when the leaders of the G20 nations were struggling to respond to the financial crisis, they agreed to develop a co-ordinated response to change the handling of over-the-counter derivatives. These transactions are used to manage risks such as interest rate changes and credit exposure. During the crisis, the risk of individual parties defaulting on these contracts exposed the global financial system to vulnerabilities.

The G20 leaders believed that we could better manage the risks associated with these tools by running the transactions through a regulated central counter party, often called a clearing house. Listed futures and options contracts have long used clearinghouses to mitigate default risks, which formed the basis for extending the regime to over-the-counter derivatives.

Today, global regulators have implemented central clearing mandates for numerous products and updated the rules for the CCPs that now manage more risk. Mission accomplished? Not quite. Unfortunately, territorial skirmishes are setting up a duplicative, confusing web of requirements for clearinghouses that will create compliance conflicts and vulnerabilities rather than a harmonised, more resilient financial system.
It is time to recommit to ensuring that our alliance remains strong. Regulatory conflicts that may ultimately result in global market fragmentation are at odds with our shared mission. We at the US Commodity Futures Trading Commission should lead the way by re-evaluating our approach to overseas CCPs. We were the first country to implement new clearing rules for OTC derivatives and were determined to require any foreign-regulated clearinghouse wishing to offer these products to US clients to register with the CFTC.

Today, we can re-assess because other countries and the EU have implemented their own comparable reforms. We are already empowered to do so. The US Congress recognised that consistency, not duplication, is the goal: it gave the CFTC the authority to exempt a third-country CCP from registration if we determine that it is subject to comparable, comprehensive rules and supervision at home. It is time to revisit the rationale of compelled registration for comparably regulated foreign CCPs.

Likewise, I encourage fellow regulators around the world to perform similar reviews of their approaches to cross-border oversight of foreign CCPs. Unfortunately, the EU appears to be moving in the opposite direction. It is working on legislation that seeks to replicate the elements of the CFTC regime that I believe are ripe for review, and applies them even more broadly.

I understand that individual jurisdictions sometimes need to recalibrate their rules, based on new circumstances, but in doing so we cannot forget the necessity of co-ordination. Unilateral over-reach leads to retaliatory and counterproductive responses.

Let us refocus on the original mission, keeping in mind three key points. First, clearinghouses were determined to be a potential solution, not a contributing factor, to the financial crisis. Second, both the EU and the US have implemented the fundamental G20 standards and, third, both sides have mutually recognised that their requirements are equivalent or comparable. We should build upon, rather than ignore, our progress. If we remain committed to applying comparable regulations globally, there is no need to duplicate supervisory requirements.

Having only recently joined the CFTC I was not involved in the initial regulatory efforts to apply the G20 standards. Perhaps I would have sought to do things differently, but rather than pass judgment, I am committed now to advancing a co-ordinated approach. We must reset our focus and recognise that our shared objectives are mission critical, not mission impossible.

The writer is a CFTC commissioner and the views expressed are her own