



**Financial Services Agency
Government of Japan**



Bank of Japan

Mr. Gary Gensler
Chairman
U.S. Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581
USA

August 13, 2012

Re: Proposed CFTC Cross-Border Releases on Swap Regulations

Dear Gary,

We appreciate the opportunity to comment on the proposed CFTC cross-border interpretative guidance and exemptive order regarding compliance with certain swap regulations. We are writing to ask the Commission's consideration of our concerns about these proposals, in particular about the application of registration and transaction requirements to operations of foreign financial institutions established outside the US.

As to the extraterritorial application of OTC derivatives regulation of the Dodd-Frank Act, we can understand your concern that risks emanating from an overseas entity of a financial group could directly flow back to the whole group, and this should be avoided. We believe, however, that such extraterritorial application will need to be consistent with the principles of international comity between jurisdictions, as noted in the CFTC proposal. A number of jurisdictions, including Japan, have been making significant progress in implementing the G20 commitments, including mandatory clearing and trade reporting, in an internationally consistent and coordinated manner toward the agreed deadline of end-2012. The regulations which Japan will be implementing from November this year are not identical with US regulations, but are consistent with the objectives of the G20 countries to improve transparency in the derivatives markets, mitigate systemic risk and protect against market abuse, and in this regard share the same goals with the Dodd-Frank Act.

Against this backdrop, we have two overarching concerns and three specific requests to

amend the CFTC proposals as follows.

I. Overarching Concerns

- Avoidance of overlapping or conflicting regulation

First, to the extent that US law subjects Japanese financial institutions established and conducting businesses in Japan to US regulation, then this would inevitably lead to overlapping or conflicting regulation, thus placing undue burden not only on the financial institution itself but also on other market participants as well.

In this regard, FSA Japan has the primary responsibility in determining and implementing appropriate regulation of OTC derivatives market participants and their transactions in Japan. Therefore, we would like to ask the Commission to reconsider the necessity of extraterritorial application of US derivative regulations, including swap dealer registration requirements to Japanese financial institutions established and conducting businesses in Japan.

- Need for international coordination in cross-border regulation

Second, if the scope and timing of application of OTC derivatives regulations to cross-border transactions would be different and inconsistent among jurisdictions, there are risks that the application of a country's regulations to cross-border transactions without proper international coordination would unduly impose additional costs on those transactions and thereby reduce the liquidity of OTC derivatives markets. For example, where the scope of mandatory clearing in terms of products is not identical between jurisdictions and no single CCP is available for clearing the transactions of both counterparties, market participants will not be able to enter into a transaction for fear of finding themselves in breach of either of the two sets of regulations. In this context, FSA Japan intends to address this issue by limiting the scope of mandatory clearing to transactions between large domestic market players at the initial stage of implementation of OTC derivative regulations to enter into force in November this year.

Therefore, we urge the Commission to consider deferring the application of its regulations on cross-border transactions until an internationally consistent approach on how to address cross-border regulation of OTC derivatives would be developed (e.g. for at least one year and renewable, if necessary).

II. Specific Requests

In addition to the overarching concerns above, we have the following three specific requests to amend the CFTC proposals:

1. Further extension of application of substituted compliance, and making clear its details, including due process and timing

2. Deferral of application of CFTC regulations with respect to non-US persons
3. Exclusion of certain transactions from the calculation of swap transactions in regard to the de-minimis threshold for non-US persons

1. Further extension of application of substituted compliance, and making clear its details, including due process and timing

In the proposed CFTC guidance, we recognize that the Commission intends to introduce the concept of substituted compliance for the purpose of avoiding duplicative application of regulation. While we welcome this step, we have two concerns in this regard.

(i) The first concern is that the scope of application of substituted compliance is too narrow. We request it to be further extended, so that overlap or conflict with Japanese regulation could be avoided as much as possible.

As for entity-level regulations, substituted compliance should apply to all types of foreign affiliates of US-based swap dealers, including those with swaps booked in the US. Substituted compliance should also be extended to a broader set of transaction-level requirements. For example, transactions conducted in Japan between Japanese financial institutions and Japanese affiliates of US-based swap dealers (swaps booked in the US) should be subject to substituted compliance. In addition, cross-border transactions between the head offices of Japanese financial institutions and US-based swap dealers should be able to benefit from substituted compliance.

(ii) The second concern is that the details, including the procedure and implementation timeline of “substituted compliance” are not clear in the proposal. The Commission proposes that it would make comparability determinations on an individual requirement basis, such as mandatory clearing and trade execution facility, rather than the foreign legislative/regulatory regime as a whole. We believe this determination should be made on a country-by-country basis, and in a comprehensive manner, from the viewpoint of whether or not foreign regulation is broadly in alignment with US regulation and consistent with the overall objectives of the G20 commitments. The determination should also take into account such elements as further regulations to be introduced in a phased manner and the necessity of different regulation in light of divergent practices in non-US markets.

Furthermore, when certain requirements under Japanese regulations are not identical to those of the US at a particular point in time, it would not be acceptable for us that the Commission applies its regulations in addition to Japanese regulations in place to address the differences. In other words, substituted compliance should respect foreign regulations as a set, not on a piecemeal basis.

2. Deferral of application of CFTC regulations with respect to non-US persons

As noted above, we believe that CFTC regulations, including swap dealer registration should, as a matter of principle, not be applied to Japanese financial institutions established and conducting businesses in Japan. Even if Japanese financial institutions would be required to register as swap dealers under limited circumstances, these requirements should be the least onerous, and a sufficient preparation period needs to be ensured.

In this regard, according to the CFTC rule, the application for registration as swap dealer will need to be filed within 60 days after the final rule on the definition of swaps is published in the US federal register. Although this deadline is applied to non-US persons, as well as US persons, we request that the swap dealer registration requirement (along with other obligations that registration entails) should not apply to non-US persons before (i) the details, including the procedure and implementation timeline of substituted compliance become clear, and (ii) the assessment by the Commission for substituted compliance is completed and agreed with interested parties.

3. Exclusion of certain transactions from the calculation of swap transactions in regard to the de-minimis threshold for non-US persons

Third, the following types of swap transactions should be excluded from the calculation of swap transactions in regard to the de-minimis threshold in determining the need for swap dealer registration for non-US persons, if non-US persons are required to register under limited circumstances.

(i) Transactions between non-US affiliates of non-US persons under common control and US persons

We believe that only transactions with US persons conducted by Japanese financial institutions established in Japan should be included in determining the need for registration as swap dealer. In other words, transactions with US persons conducted by entities under common control of Japanese financial institutions established outside Japan (e.g. in the UK and Hong Kong) should not be included in the calculation of swap transactions in regard to the de-minimis threshold, with respect to the Japanese financial institutions established in Japan.

Furthermore, even if Japanese financial institutions are to be registered as swap dealers, their subsidiaries, sister companies or parent companies which conduct transactions with US persons below the de-minimis threshold should not be required to register as swap dealers.

(ii) Transactions between US branches of non-US persons and US persons

According to the proposed guidance, we understand Japanese financial institutions

established in Japan do not need to include the notional value of swap transactions with US persons in which their US affiliates engage, when calculating the swap transactions in regard to the de-minimis threshold. In parallel with this, we believe that transactions between US branches of Japanese financial institutions and US persons should also be excluded from the de-minimis threshold calculation for Japanese financial institutions.

We would like to kindly request that the Commission take into account the above and amend the proposed guidance and order in accordance with our requests. Should you have any questions concerning the above, please do not hesitate to contact us.

Sincerely yours,

Handwritten signature of Masamichi Kono in black ink, consisting of four characters in Japanese (河野正通) followed by a stylized signature.

Masamichi Kono
Vice Commissioner for International Affairs
Financial Services Agency
Government of Japan

Handwritten signature of Hideo Hayakawa in black ink, written in a cursive style.

Hideo Hayakawa
Executive Director
Bank of Japan

Cc : Commissioner Ms. Jill E. Sommers, CFTC
Commissioner Mr. Bart Chilton, CFTC
Commissioner Mr. Scott D. O'Malia, CFTC
Commissioner Mr. Mark P. Wetjen, CFTC

Chairman Mary L. Schapiro, SEC

Under Secretary for International Affairs Lael Brainard, U.S. Department of the Treasury