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December 19, 2016

Mr. Timothy G. Massad
Chairman
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581, USA

Dear Tim,

Cross-Border Swap Rule

We are writing to convey our collective views to the request for comments from the Commodity Futures Trading Commission (CFTC) with respect to Cross-Border Application of the Registration Thresholds and External Business Conduct Standards Applicable to Swap Dealers and Major Swap Participants (Proposed Rule). We appreciate the ongoing dialogue between the CFTC and the Asia-Pacific Regional Committee (APRC) of the International Organization of Securities Commissions (IOSCO) in relation to the regulatory frameworks for OTC derivatives markets.

We understand that the CFTC has concerns that risks emanating from a non-US entity could adversely affect its US counterparty, potentially leading to adverse effects on US economy. However, we believe that such concerns will need to be addressed in accordance with the principles of international comity between jurisdictions, as noted in the G20 leaders' declaration in 2013. In particular, many non-US entities and Foreign Consolidated Subsidiaries (FCS) are currently regulated by their local non-US regulators and are already or will soon be subject to the G20 OTC derivatives reforms imposed by their local regulators. We should therefore be able to defer to each other, based on similar outcomes, in a non-discriminatory way, paying due respect to home country regulatory regimes. Otherwise, the extra-territorial application of registration requirements will lead to overlapping regulation, placing an additional burden on market participants and result in market fragmentation and liquidity decrease.

In this regard, the Proposed Rule could have a significant impact on the Asia Pacific financial markets, local market participants and US entities conducting business in the Asia Pacific region. APRC members share the objectives of building resilient and efficient derivatives markets and maintaining financial stability, and we look forward to working with you to find efficient and effective ways based on mutual cooperation and deference.

Key points which APRC members would like to convey are as follows:

1. Limited benefits from expanded extra-territorial reach, while imposing disproportionately high costs on affected regional entities



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- Other Non-US Persons' swap transactions with US Persons, US Persons' foreign branches, US guaranteed entities, and FCS are already or can be subject to the CFTC's rules on reporting, clearing, trading and margin requirements on the later entities.
- We believe that the CFTC's current requirements are appropriately robust and provide adequate data, transparency and risk mitigation measures for the CFTC to assess and thereby minimize any potential risks arising from such transactions that may have a claw-back effect on the US economy and US entities.
- In addition, we believe that Other Non-US persons in these Asia Pacific jurisdictions are unlikely to have a direct and significant impact on US economy. For instance, a number of such Non-US financial institutions solely enter a hedge transaction with a subsidiary of US Persons or FCS in Asia Pacific region to reduce the risks in their core banking business, and they do not have a presence in US.
- For the above reasons, requiring Other Non-US Persons to register as new non-US Swap Dealer does not appear to provide significant added benefit or comfort. This is especially the case for Non-US Persons who deal with branches of US Persons or FCS in their home jurisdictions.
- While the benefits are limited, there would be high costs for Other Non-US Persons to implement infrastructure for counting and monitoring of de-minimis threshold for Swap Dealer (SD) registration. In addition to a few dozens of non-US firms in Asia Pacific which are likely to newly exceed the registration threshold, a greater number of financial groups which remain below threshold will need to continuously monitor their trading amount with US related entities.
- Unlike global financial institutions, the resources of regional financial groups¹ in Asia Pacific region can be limited, and the Proposed Rule will pose disproportionate burden² on them compared with their risk profile and business model. They will have difficulty in concurrently complying with two sets of regulations, i.e. local regulations as well as CFTC related regulations.

2. Market fragmentation leading to negative implications on liquidity and pricing

Impact on Other Non-US Persons

- In order to avoid counting and preparing for possible registration as a non-US SD, some local market participants may cease their dealings with FCS and foreign branches of US Persons which may be the primary pool of liquidity in US dollar products.

¹ According to the estimates provided by some market participants and our member authorities, a few dozens of non-US financial groups in some jurisdictions of Asia Pacific region are now likely to exceed the SD registration threshold of 8 billion US dollar under the proposed calculation. The current aggregation rule is likely to contribute to bringing Asia Pacific financial groups within the scope of SD registration. The possible reduction of the de-minimis threshold to 3 billion US dollar on 31 December 2018 will exacerbate the duplicative regulatory burden to this region further.

² According to market participants, an estimate of initial legal cost for non-US SD registration could be over 1 million US dollar per entity. On-going compliance cost need to be included in additional costs.



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- Market fragmentation may occur, resulting in two different pools of liquidity; one for US Persons and non-US SD (US pool) and the other one for Other Non-US Persons (non-US pool). This may lead to wider spreads and lower liquidity.
- Even if there are entities willing to act as bridges between these two pools, transaction premium will be incurred and ultimately passed on to end users.
- The risk of market fragmentation is much higher than in the case of other transactional requirements imposed on transactions with US Persons such as margin requirements, because SD registration subjects registrants to a much higher level of compliance burden; the CFTC's comprehensive regulatory regimes including substantial entity-level and transaction-level rules.

Impact on US end users

- In some jurisdictions, local market participants are the main liquidity providers for local currency OTC derivatives products. FCS and foreign branches of US corporates in turn rely principally on these local market participants as liquidity providers.
 - As mentioned above, Other Non-US Person may need to cease trading with FCS and foreign branches of US Persons, due to its concerns that it may exceed the de-minimis threshold.
 - This will result in liquidity in local currency OTC derivatives products drying up for FCS and foreign branches of US corporates operating in some Asia Pacific markets, which will in turn affect their ability to hedge their commercial activities or provide products for their customers.
- **In view of the concerns set out above, we would therefore like to suggest that the CFTC reconsider the proposed change of counting swap transactions between an Other Non-US Person and an FCS/ foreign branch of a US Person for Other Non-US Person's de-minimis threshold calculation.**

3. Current progress of OTC derivatives reforms contributing to minimising risks of claw-back to US economy

- Recent regulatory reforms such as clearing mandate, margin requirements or trading mandate contribute to the establishment of more robust risk management in the market. For instance, when the transactions are cleared by a CCP, the potential risks and impacts which may be transferred to the US are effectively minimized. In a similar way, when margins are exchanged in accordance with internationally agreed requirements, the potential risks and impacts transferred to the US financial system would be very limited.
- **In this respect, we suggest that transactions that are centrally cleared or subject to margin requirements should be excluded from the scope of threshold calculations. We also suggest that, where a trading venue has qualified for non-action relief³, transactions on such venues also be excluded from the scope of threshold calculations.**

³ At present, CFTC issued non-action relief in this regard to a Qualifying Australian Licensed Market.



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4. Uncertainties surrounding new definitions

- The Proposed Rule addresses application of registration thresholds and some external business conduct standards only and leaves uncertainties on new requirements on transactions by FCS and Arrange, Negotiate and Execute (ANE) transactions. We are concerned that such uncertainties may hinder market activities.
 - We understand that the proposed definitions of FCS and ANE transactions would apply not only for the purposes of the Proposed Rule but also for future cross-border rulemakings.
- **Before the proposed definitions are adopted, additional information on full requirements to be imposed, their timing and possible exemptions need to be provided.**

5. Need for clear outcome-based substituted compliance framework

- If the Proposed Rule is to go ahead in its current form, adequate time is needed prior to the implementation for conducting substituted compliance determination for Asian Pacific jurisdictions.
 - Timing for substituted compliance coming into effect is critical. Substituted compliance should be effective before the Proposed Rule takes effect, not after. Otherwise, market participants would be subject to duplicative and overlapping sets of requirements in their local jurisdiction and under the CFTC rules. If substituted compliance cannot come into effect before the Proposed Rule takes effect, no action relief will be needed until substituted compliance can be put in place to reduce compliance burden.
- **We seek clear guidance from the CFTC on procedures required for substituted compliance determination so that preparation can start as soon as possible. In this context, we believe that adaptation of an outcome-based approach instead of a rule by rule approach is important in its substituted compliance determination.**

We hope that these comments will contribute to your rulemaking process and we look forward to continued cooperation between the CFTC and APRC with the aim of delivering globally coordinated regulations for an efficient and resilient OTC derivatives market.



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Yours sincerely,

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Ryozo Himino
Chairman
IOSCO Asia-Pacific Regional Committee

Cc: Commissioner Ms. Sharon Y. Bowen, CFTC

Commissioner Mr. J. Christopher Giancarlo, CFTC