27 August 2012

Hon. Gary Gensler
Chairman
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington DC 20581, USA

Dear Chairman Gensler,

CFTC's Proposed Guidance on Cross-Border Application of Certain Swap Provisions of Commodity Exchange Act ("Proposed Guidance")

1. We, the undersigned, are a group of financial regulators in the Asia Pacific region with a mutual interest in ensuring the smooth and effective implementation of the G20-agreed reforms of OTC derivatives markets in our jurisdictions. We welcome the release of the Proposed Guidance by the CFTC to clarify how it intends to apply the Commodity Exchange Act to cross-border swap dealing activities involving non-US persons, and acknowledge the CFTC's efforts to consider the impact of the swap provisions on non-US markets and participants. However, we are concerned that some of the proposed requirements as they currently stand may have significant effects on financial markets and institutions outside of the US. We believe a failure to address these concerns could have unintended consequences, including increasing market fragmentation and, potentially, systemic risk in these markets, as well as unduly increasing the compliance burden on industry and regulators. We therefore think it necessary to share with you our specific concerns, as well as some suggestions to mitigate these concerns, so that any unintended and adverse consequences for global markets and institutions can be averted.

Major issues and suggestions

2. Currently, various national authorities around the globe (including those represented in this letter) are taking active steps to implement in their jurisdictions the reform measures endorsed by the G20 leaders in respect of OTC derivatives markets,

with a view to promoting transparency and confidence in derivatives markets and reducing systemic risks arising from activities in such markets.

3. However, the CFTC Proposed Guidance, that subjects non-US persons to the swap dealer ("SD") or major swap participant ("MSP") registration requirements as well as entity-level and transaction-level requirements, may have the following consequences:

- Affected non-US persons will have to comply with two sets of regulations, which may be overlapping and conflicting, imposed by the US and individual non-US regimes. This is compounded by the lack of clarity and specificity in a number of areas of the Proposed Guidance.

- Potential market disruption or fragmentation, with consequently increased risks to systemic stability and market liquidity in our markets, may arise as market participants may have to change their business models or even withdraw from certain businesses, all within a relatively short period of time. The impact from any resulting (likely significant) increase in compliance costs and the potential reduction in liquidity of OTC derivatives markets should not be under-estimated.

4. In our view, while the approach proposed by the CFTC is a useful first step, further changes are needed to the Proposed Guidance to achieve an internationally harmonised approach and avoid creating frictions in the international market place, given the cross-border nature of OTC derivative markets and the concerns expressed in this letter and also by other regulators.

5. We would thus urge the CFTC to consider the following suggestions:

(i) ***Re-assess scope and timing for implementing the Proposed Guidance***: We suggest that a re-assessment of the CFTC's proposed approach should be made to avoid any unintended and adverse implications for global markets and institutions. This should preferably be done together with engagement with affected jurisdictions (including ourselves) to address their concerns before

finalising the Proposed Guidance. We seek further dialogue with the CFTC to do so. Consideration should also be given to deferring the application of the relevant requirements until there is international consensus on how such cross-border transactions should be regulated.

Rather than a rule-by-rule or case-by-case approach as it is currently proposed, an approach that looks at substantive regulatory outcomes (where appropriate) or an expansion to place greater reliance on the regulatory and supervisory regimes of other regulators would better achieve the concept of international comity which the CFTC is seeking.

(ii) ***Provide more guidance and clarity on assessment of substituted compliance and definition of US person*** : Notwithstanding the suggestions in Paragraph 5(i), we believe the Proposed Guidance would benefit from greater clarity and detail regarding the application of the swap provisions. In particular, (a) the definition of "US person"; and (b) the criteria, procedures and implementation timeline for "substituted compliance" in respect of each of the CFTC's entity-level requirements and transaction-level requirements could each be further clarified. We would welcome dialogue with the CFTC on these areas.

We note that the proposed definition of "US person" is high-level and different from that used in other regulations (e.g. Reg S.). Market practitioners have also highlighted that it is not easy to identify if a counterparty is a US person. Uncertainty will increase the risk for, and costs of, market participants in assessing the full impact of the Proposed Guidance (e.g. the registration requirements).

On substituted compliance, the Proposed Guidance contains broad language to the effect that the CFTC would determine comparability for the purposes of "substituted compliance"[1]. However, it is unclear on how comparability will be assessed and whether there will be interim measures prior to finalising the

[1] Considerations include (i) the "scope and objectives" of the regulatory requirements imposed by a non-US regulator; (ii) the comprehensiveness of the regulator's supervisory compliance programme; and (iii) the regulator's power to support and enforce its oversight of non-US SDs and MSPs operating in its jurisdiction.

assessment as no further details or elaboration are provided in the Proposed Guidance.

We are of the view that one useful point of reference for substituted compliance assessment would be the foreign regime's compliance with applicable global standards set by international standard-setting bodies like the CPSS, IOSCO and the Basel Committee on Banking Supervision. Moreover, just as the CFTC has proposed requirements which are tailored to the US market, there is also a need for other regulators to cater for special characteristics of their local markets. For example, in the case of Hong Kong, Australia and Singapore, we are studying whether local market liquidity can justify implementation of mandatory trading of OTC derivatives products on exchanges or electronic trading platforms, and the form of trading venue which will best suit the purpose of improving pre-trade price transparency. This will affect our timing for implementing mandatory trading in practice (although the powers for imposing such trading obligation will be in place). In addition, the CFTC has recognised that the pace of implementation of OTC derivatives reforms by different jurisdictions may vary, and we suggest that the approval for "substituted compliance" should take into account, among other things, the proposed regulations, and the progress in introducing these regulations, in "potentially comparable" jurisdictions.

(iii) ***Allow transitional arrangements for application of Proposed Guidance to non-US entities***: To minimise the risk of market disruption and fragmentation in respect of the conduct of OTC derivatives transactions outside the US that will likely be captured under the Proposed Guidance, we strongly recommend the CFTC to consider more flexible transitional arrangements that will allow market participants to carry on such transactions as usual as it reviews jurisdictions for the purpose of "substituted compliance", in line with the spirit of international comity.

(iv) ***Consider further temporary exemptive relief for non-US SDs and MSPs***: We note that certain requirements, e.g. capital and margin rules, the SEF rules, may not be finalised before the swap dealer registration deadline. It is thus strange for

non US-based entities to register without having certainty on the full implications of the registration.

In addition, certain SD requirements may conflict with domestic requirements. For example, non-US SDs that are regulated as banks may be prohibited by local privacy laws from transferring customer data to the US for reporting swap transactions. To avoid legal risk, non-US SDs may be unable to continue dealing with non-US customers in the OTC derivatives market unless (a) their customers provide explicit consent to the release of their data in order to meet the US reporting requirements; or (b) "substituted compliance" is permitted.

As such, we request that the CFTC considers delaying the registration requirement for non-US SDs until there is clarity of the above issues.

Furthermore, we have two comments with respect to the proposed granting of temporary exemptive relief order, to allow non-US SDs and MSPs to delay compliance with certain entity-level and transaction-level requirements. First, we suggest that the "non-affiliate" condition is removed or modified as it will capture foreign affiliates that operate independently from the US SD (and are not under the SD's majority control) and whose swaps with non-US counterparties are unlikely to have significant systemic risk implications for the US. Second, while we appreciate the intent of this temporary relief, it is subject to progress made on operationalising "substituted compliance" as well as more clarity on the conditions to which the relief is subject.

(v) ***Consider proportional regulatory approach to central counterparties ("CCPs") in non-US jurisdictions with relatively small OTC derivatives markets***: We would strongly encourage the US authorities to develop a simplified and pragmatic process for (a) recognising or exempting non-US CCPs (including those that operate in relatively small OTC derivatives markets) that are regulated by competent authorities subscribing to relevant CPSS / IOSCO standards; and (b) handling applications for "substituted compliance" with priority (provided that clear guidance on application criteria and procedures is available to potential

applicants). In formulating this process, the CFTC is also requested to have regard to the potential impact on non-US CCPs and markets as explained below.

Under the Proposed Guidance, non-US SDs, which may be significant liquidity providers in foreign jurisdictions, will be required to centrally clear their OTC derivatives transactions with (a) US counterparties or (b) non-US counterparties that are guaranteed by US persons (although "substituted compliance" may be permitted for transactions described in (ii)) through registered or registration-exempted Derivatives Clearing Organisations ("DCOs"). If the CFTC mandates clearing for products that are also traded in our markets, it will be critical that CCPs operating in those markets be able to obtain approval from the CFTC as a registered DCO (or be exempted from registration) in good time, to allow participants to clear mandated transactions.

Failure of a CCP to obtain approval as a registered DCO (or be exempted from registration) in time may lead to the following consequences:

- The mandated transactions may be channelled to registered DCOs which are now global facilities. This raises concerns over the potential over-concentration of risks in such CCPs.

- Certain US SDs operating in the Asia Pacific region are major liquidity providers in local markets. If they are not allowed to use clearing platforms other than DCOs that are US-registered or exempt from registration, and other smaller local / regional players can only access central clearing indirectly, the overall capacity of these players to further provide liquidity in local / regional OTC derivatives markets may be curtailed.

- This development may also undermine the financial viability of local / regional CCPs, in turn resulting in such CCPs ceasing to provide important clearing services for products that are unique to our financial markets and not cleared through foreign CCPs registered as DCOs,

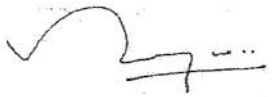
potentially increasing systemic risk in such markets and impacting the stability of US markets and/or major participants as well.

- Lastly, local and regional market participants who do not have direct access to global CCPs may have to face the credit risk of a small group of clearing agents who are likely to be the same global dealers with whom they are dealing, potentially restricting their counterparty risk management capacity. This also adds to, and further concentrates, the risks at the major clearing members.

6 We appreciate the opportunity to provide our comments to the Proposed Guidance and look forward to our continued cooperation and engagement with the CFTC and other regulators to provide globally harmonised regulations for an efficient and robust OTC derivatives market.

Yours sincerely,

Belinda Gibson
Deputy Chairman
Australian Securities and Investments Commission



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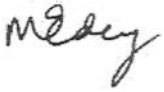

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