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January 24, 2011

David A. Stawick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, DC 20581

Re: Proposed rules: Registration of Swap Dealers and Major Swap Participants (RIN 3038 - AC95)

Dear Mr. Stawick:

The International Swaps and Derivatives Association, Inc. ("**ISDA**")[1] appreciates the opportunity to comment on the proposed regulations (the "**Proposed Regulations**"), promulgated by the Commodity Futures Trading Commission ("**CFTC**" or the "**Commission**") in accordance with section 4s ("**Section 4s**") of the Commodity Exchange Act (the "**CEA**"), which was added to the CEA by the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "**Dodd-Frank Act**"), with respect to the registration of swap dealers ("**SDs**") and major swap participants ("**MSPs**" and, together with SDs, "**Swaps Entities**").

ISDA commends the Commission for its careful consideration of the issues raised by the new registration requirements of the Dodd-Frank Act and respectfully submits the following comments in response to the Proposed Regulations.

I. Phased Implementation

The Commission has proposed a system of phased implementation for the "transitional period" between July 21, 2011, the date by which regulations establishing a process for Swaps Entities' registration are to be in place and the potentially later effective dates of key definitional

[1] ISDA was chartered in 1985 and has over 800 member institutions from 54 countries on six continents. Our members include most of the world's major institutions that deal in privately negotiated derivatives, as well as many of the businesses, governmental entities and other end users that rely on over-the-counter derivatives to manage efficiently the risks inherent in their core economic activities.
Since its inception, ISDA has pioneered efforts to identify and reduce the sources of risk in the derivatives and risk management business through documentation that is the recognized standard throughout the global market, legal opinions that facilitate enforceability of agreements, the development of sound risk management practices, and advancing the understanding and treatment of derivatives and risk management from public policy and regulatory capital perspectives.

rulemakings and rulemakings with respect to capital, margin and a variety of other important aspects of doing business as a SD or an MSP[2]. These potentially later rulemakings will complete the determination of who must register and what the responsibilities of registrants will be. The Commission proposes that "voluntary", provisional registration begin on April 15, 2011.

We appreciate that the Commission has invited comment on alternatives to this system of phased implementation, including the extension of the effective date of the Proposed Regulations until such time as rules further defining the terms "swap dealer" and "major swap participant," and rulemakings implementing the other key requirements become effective. ISDA supports such an extension of the effective date of the Proposed Regulations because an early, provisional registration procedure is not cost-effective or otherwise efficient for potential Swaps Entities (or, we would think, the Commission). At the time of pre-registration, many potential Swaps Entities will not know if they must register or if they will be able to function under the still-developing regulatory regime. Compliance with new regulations may require extensive changes to the way that Swaps Entities presently organize themselves and conduct their business. It is therefore only reasonable that those entities should be aware of all their compliance obligations with certainty *before* they are asked to register – otherwise unnecessary costs and unnecessary disclosure may result,[3] burdening both regulator and regulated.

ISDA further believes that the registration process should be minimally disruptive to ongoing business operations and the swaps markets, irrespective of the date on which registration occurs.[4] Although nominally voluntary, provisional registration from July 21, 2011 onwards will be necessary to avoid business interruption. Given that (i) if a Swaps Entity does not provisionally register in advance, then on the day that it must register, its business must stop, because it will not yet be through the registration process; and (ii) in the Release the stated reason provided for provisional registration is that without such a system, Swaps Entities may not be registered on time, we question how "voluntary" provisional registration will in fact be. Furthermore, the subsequent finalization of each relevant regulation will again threaten business interruption as compliance becomes necessary. ISDA urges the Commission to (i) postpone the effective date of the registration requirements until all important aspects of compliance are settled and (ii) provide for a compliance period after the effective date of the registration requirements. ISDA additionally requests that the CFTC introduce reasonably extended compliance periods into any rulemakings that may be left to later development as a less disruptive, less costly, and generally more appropriate alternative to the threat of business interruption.

There is a growing awareness that the swaps markets and the Commission face a growing "chicken and egg" problem in attempting to develop in a single stroke an entirely new market regulatory

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[2] Section 4s governs registration and regulation of SDs and MSPs, and includes rules relating to capital and margin requirements, reporting and recordkeeping requirements, daily trading records, business conduct standards, documentation standards, duties and designation of a chief compliance officer.

[3] For example, the proposed regulation establishing and governing the duties of swap dealers and major swap participants requires that a Swaps Entity furnish a copy of its written risk management policies and procedures to the Commission upon application for registration. See 75 FR 71397 (November 23, 2010). It is not practical for an entity to develop such a detailed plan to Commission specification until it knows for sure that it will actually be a Swaps Entity.

[4] Although the Paperwork Reduction Act section of the release accompanying the Proposed Regulations (the "Release") suggests that it will merely take a matter of minutes for Swaps Entities to complete the forms required by the Proposed Regulations, we are dubious that this is accurate. Additionally, the time and cost burden to those entities of compliance with the attendant rules and regulations cannot be understated.

structure. We share the Commission's goal of implementing appropriate and meaningful regulation and believe that a first step is to provide adequate time for compliance.

II. Allocation of Responsibilities

The Commission has proposed that Swaps Entities will be required to become and remain members of at least one registered futures association. Presently, there is only one such association, the National Futures Association (the "**NFA**") and so the Commission has proposed registration of Swaps Entities through the NFA. The Commission has further proposed three alternatives for monitoring compliance by Swaps Entities with all requirements applicable to them under the CEA and CFTC regulations: (1) the Commission directly and solely responsible; (2) the NFA responsible but with CFTC oversight; or (3) division of responsibilities between the CFTC and the NFA. ISDA favors self-regulation but believes that the swaps market needs self-regulation that is solely focused on swaps and the intricacies of the swaps markets.

The Benefits of Self-Regulation

The United States has a long-established tradition of financial market self-regulation, based on self-regulatory organizations ("**SROs**") acting under the oversight of the Commission and the Securities and Exchange Commission (the "**SEC**"), as the case may be. ISDA believes that SROs help safeguard the integrity of the financial markets. They benefit from the experience of industry participants and the desire of the industry to maintain the highest ethical standards and promote investor confidence. SROs also reduce the costs of regulation to the government and the taxpayer. The Commission and the SEC have recognized the virtues of SROs by ceding to them a host of responsibilities, especially those that are registration and compliance-related.

In the Release, the Commission notes that it presently relies heavily on the NFA as SRO in the futures markets (previously the Commission's most significant market responsibility) with respect to all aspects of the registration process and for monitoring compliance with all subsequent requirements. Presumably the Commission regards this as the most efficient use of its own resources, a judgment that would seem to apply equally to SRO usage in the swaps markets. Chairman Gensler has noted the resource constraints the Commission faces in implementing the Dodd-Frank Act in recent Senate testimony.[5] In light of those resource constraints, the evident benefits of SRO use mean that a system of self-regulation in the swaps market would be optimal for all concerned. In addition to relieving potential resource constraints at the Commission, we believe that having an SRO whose primary mission is to promote market integrity and compliance with defined standards has the additional benefit of being a very efficient means of achieving those objectives. Of course, in light of the fact that NFA has acted as an SRO for the futures industry exclusively, it would be necessary for the organization to develop a range of new capabilities in order to have the expertise necessary to serve as an effective SRO for the swaps industry. ISDA respectfully offers to serve as an expert resource on the swaps market to the appropriate SRO.

III. Section 2(i) of the CEA—Extraterritorial Application of SD and MSP Registration Requirements

In Section E of the Proposed Regulations, the CFTC solicits comment on whether and to what extent it should extend SD and MSP registration requirements to persons engaging in swap dealing

[5] See http://cftc.gov/PressRoom/SpeechesTestimony/ChairmanGaryGensler/opagensler-63.html

activities that "'have a direct and significant connection with activities in, or effect on, US commerce'" or "contravene rules or regulations the Commission may promulgate to prevent evasion." (75 Fed. Reg. 71382.) ISDA may comment more broadly on extraterritoriality in its response to the definitions release ("Definitions Release").[6] However, ISDA is grateful for the CFTC's raising the issue in the present context and will take this opportunity to offer some generalized views. Any comments ISDA now provides on extraterritoriality are subject to continuation in later letters.

It is ISDA's view that, particularly in light of present circumstances, the registration regime should reach only those persons that transact with US customers.[7] Registration itself should be only with respect to US customer business, and regulation following from registration should be considered accordingly. ISDA's position is grounded in (i) principles of statutory interpretation, as set forth in the Supreme Court's recent *Morrison* decision, (ii) Section 721 of the Dodd-Frank Act which expressly authorizes the CFTC to designate a person as a swap dealer for "a single type or single class or category of . . . *activities* and considered not to be a swap dealer for other types, classes, or categories of . . . *activities*," and (iii) principles of international comity, which are codified in part in the Dodd-Frank Act's international harmonization provision.[8] We leave for later letters the equally important and complex topic of regulation of the activities of US SDs and MSPs in foreign jurisdictions, whether by foreign or US regulators.

Limits of Registration

Section 722 of the Dodd-Frank Act provides that the CFTC's jurisdiction under Title VII shall not extend "to activities outside the United States unless those activities—(1) have a direct and significant connection with activities in, or effect on, commerce of the United States; or (2) contravene such rules or regulations as the Commission may prescribe or promulgate as are necessary or appropriate to prevent the evasion of any provision of [the Wall Street Transparency and Accountability] Act." *Morrison* dictates that Section 722 be read narrowly. This is even more the case when the operative statutory provision under consideration makes no mention of extraterritorial application. Given that Section 731 *itself* does not expressly address extraterritorial application, principles of statutory construction mandate that there be a strong presumption against its application extraterritorially.[9]

Even if principles of statutory construction did not mandate such a reading, a narrow reading of Section 722, consistent with the message of *Morrison* and principles of international comity, embodied in part in the international harmonization provision of the Dodd-Frank Act (§ 752), require that the CFTC should nevertheless decline to take an expansive view of its jurisdiction, at least until it has coordinated with foreign regulators on the establishment of consistent international registration standards.[10] The international harmonization provision contemplates that other

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[6] Further Definition of "Swap Dealer," "Security-Based Swap Dealer," "Major Swap Participant," "Major Security-Based Swap Participant" and "Eligible Contract Participant," Release No. 34-63452, File No. S7-39-10, RIN 3038-AD06 (CFTC), RIN 3235-AK65 (SEC), 75 Fed. Reg. 80174 (Dec. 21, 2010).

[7] "US customer" should refer to non-SDs and non-MSPs that are US persons and "US persons" should be defined at least as narrowly as it is defined in SEC Regulation S.

[8] The Dodd-Frank Act § 752.

[9] *Morrison*, 130 S. Ct. at 2878 ("When a statute gives no clear indication of an extraterritorial application, it has none.")

[10] CFTC Global Markets Advisory Committee Meeting, Tr. 100:3-5 (Oct. 5, 2010) (CFTC General Counsel Dan Berkovitz stated that there is "no bright-line rule that says * * * the statute applies to its fullest extent in every single possible application.").

countries will regulate their own swap dealing activities and does not provide for US authorities to regulate those same swap dealing activities concurrently. And, as the Supreme Court said in *Morrison*, "[even] when a statute provides for some extraterritorial application, the presumption against extraterritoriality operates to limit that provision to its terms."[11]

Above all, the practicalities of implementing any registration regime, especially in a short time frame, dictate that registration parameters be clearly defined and reasonably limited. A bright line limiting registration to persons that transact with US customers would:

- promote stability and legal certainty in light of the short time frame in which the CFTC must implement the registration provisions;
- facilitate prompt compliance with the registration provisions by allowing for a clear determination of the persons that must register;
- increase the CFTC's ability to effectively oversee and implement registration of a clearly-identifiable group of persons; and
- reinforce the CFTC's commitment to respecting principles of international comity.

General Principles

We suggest that several broad principles may be helpful going forward:

- Registration should be limited to persons that meet the definition of SD or MSP solely on the basis of their business with US customers, and it should be solely US customer business that is subject to any attendant regulation.
- To the extent registration is to be required, the CFTC should adapt registration requirements for foreign registrants whose home countries have enacted and implemented comparable registration regulations that do not conflict with US regulations. As foreign regulators work to adopt their regulatory regimes, we urge the CFTC to coordinate with them on phase-in of respective implementation and compliance requirements. In determining comparability, ISDA urges an "in substance" assessment of comparability that does not require a one-to-one matching of discrete regulations. So, for example, in circumstances where swap dealers are in some other capacity comprehensively regulated (*e.g.*, as a bank or broker-dealer authorized to deal swaps), and so in some fashion registered, the comparability requirement would be met. (Without deference to home country regulation, registration may be prohibitively expensive, operationally impractical and impossible to achieve within the time frame set for implementation. Such circumstances will promote regulatory arbitrage and separation of markets.)
- When a foreign registrant's home country has comparable registration regulations that directly conflict with CFTC regulations, the CFTC should consider principles of international comity in determining whether and to what extent those registrants should be further regulated by the CFTC (we would expect that when the relevant "actor" is outside of the United States, the CFTC would generally defer to foreign regulation). Of course, the home country regulator has the greatest interest in, and is in the best position to, regulate foreign persons.
- Inter-affiliate and inter-bank branch trades should not count for purposes of characterizing an entity as an SD or MSP, and should not be the basis for attendant

[11] *Morrison*, 130 S. Ct. at 2883 (citing *Microsoft Corp. v. AT & T Corp.*, 550 U.S. 437 455-456, 127 S. Ct. 1746 (2007).

regulation. These are simply mechanisms for risk allocation within corporate groups, rather than new positions.

ISDA stresses that principles of restraint and regard for comity are vital in this context, with respect to foreign participants in US markets and with respect to the treatment of US participants in foreign markets.

IV. Proposed Regulation 23.22—Requirements Applicable in the Case of an Associated Person of a Swap Dealer or Major Swap Participant

The Commission has requested comment as to whether it should by regulation restrict "associated persons" of Swaps Entities to "natural" persons.[12] ISDA believes that the Commission should restrict the "associated person" definition to natural persons on the same basis as such definition is restricted to natural persons for other classes of CFTC registrants. In particular, this restriction is consistent with the regulatory purpose of reaching individuals who work at point of "sale". Further, pursuant to the Dodd-Frank Act, the definitions of FCM, IB, CPO and CTA have directly or indirectly been amended to incorporate references to swaps. Thus, IB status will be just as available (and necessary) in the swaps market to both jural entities and natural persons (for the latter, as an alternative to associated person status) as it is in the futures market.[13] However, even when those FCMs, IBs, CPOs and CTAs are engaged in the swaps market, their "associated persons" remain limited to natural persons. It would be logically inconsistent to subject Swaps Entities, operating in the same market, to a broader definition of "associated person."

In addition, it has been established that the Commission's existing "associated person" definition is not limited to "direct" employees of Commission registrants.[14] Therefore, a jural entity that, for example, employs a salesperson whose activities are for the benefit of a Commission registrant[15] need not be an "associated person". However, the actual salesperson (and that sales person's supervisor, if any) within that jural entity *will* be an "associated person" of the Commission registrant. Given that the apparent policy goal is to prohibit persons who are subject to statutory disqualification from being associated with Swaps Entities, a definition of "associated person" that

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[12] Under the Dodd-Frank Act, persons subject to a statutory disqualification (*i.e.*, disqualification under Section 8a(2) or 8a(3) of the CEA) may not be associated persons of Swaps Entities. Under existing CFTC futures regulations, associated persons of existing CFTC registrants (*e.g.*, futures commission merchants ("**FCMs**"), retail foreign exchange dealers ("**RFEDs**"), commodity pool operators ("**CPOs**") or commodity trading advisors ("**CTAs**")) are required to be registered, unless they choose to register instead as "introducing brokers" ("**IBs**"). Current Commission regulations define "associated person" as any *natural person* associated with such entities. This language is mirrored in the statutory definition of "associated person of a swap dealer or major swap participant", with the notable exception that such definition is not limited to "natural" persons. See Section 721(a)(4) of the Dodd-Frank Act. The Dodd-Frank Act does not require registration of associated persons of Swap Entities themselves (unless the Swaps Entities are also FCMs, *etc.*), it simply prohibits such association by disqualified persons.

[13] We note that the definition of IB in the Dodd-Frank Act includes any person conducting the activities of an IB (including with respect to swaps) *except an individual who elects to be and is registered as an associated person of an FCM*. We query why such an election is available only to those who choose to be associated persons of FCMs.

[14] *See Stotler & Co. v. CFTC*, 855 F.2d 1288, 1293 (7th Cir. 1988) ("If a person acts as a salesman and solicits orders for a particular futures commission merchant, he may be an associated person with that merchant, even if he places some trades with others."). *See also Bogard v. Abraham-Reitz & Co.*, [1984–1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,273 at 29,393 (CFTC July 5, 1984) ("even if [one] were an independent contractor whose conduct in the performance of the services undertaken was not controlled by [the purported principal], that status would not itself preclude his being [an] agent"); *Lobb v. J.T. McKerr & Co.*, [1987–1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,568 at 36,441 n. 13 (CFTC Dec. 14, 1989).

[15] The Commission states that "associated person" has typically referred to a salesperson of a Commission registrant.

is limited to natural persons need not be broadened because the persons at point of sale or supervising those at point of sale would in any event be "associated persons".[16]

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ISDA appreciates the opportunity to provide comments on the proposed rules and looks forward to working with the Commission as it continues the rulemaking process. Please feel free to contact me or my staff at your convenience.

Sincerely,

Robert Pickel
Executive Vice Chairman

[16] There is little value in the jural entity that directly employs the salesperson being an associated person because even if that entity is subject to statutory disqualification, there is little to stop the principals of that entity forming another "clean" jural entity. It is altogether more difficult for natural persons to evade statutory disqualification.