

CLIENT UPDATE

CFTC COMPARABILITY DETERMINATIONS AND NO-ACTION RELIEF FOR CERTAIN FOREIGN SWAP DEALERS AND MAJOR SWAP PARTICIPANTS

NEW YORK

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On December 20, 2013, the Commodity Futures Trading Commission (the “CFTC”) approved a series of broad comparability determinations permitting substituted compliance for non-U.S. swap dealers (“SDs”) and major swap participants (“MSPs”) in the following regulatory regimes: Australia, Canada, the European Union, Hong Kong, Japan and Switzerland (the “Enumerated Jurisdictions”). Substituted compliance refers to the circumstances under which the CFTC will permit such non-U.S. SDs and MSPs to comply with “comparable and comprehensive” regulatory requirements of their home jurisdiction with respect to certain of their swaps and swap-related activities in lieu of complying with the Commodity Exchange Act (the “CEA”) and the CFTC Regulations.¹

Also on December 20, 2013, the CFTC issued a no-action letter (the “SDR Reporting Rules Letter”). The SDR Reporting Rules Letter granted temporary no-action relief from certain swap data reporting rules set forth in Parts 45 and 46 of the CFTC Regulations (collectively, the “SDR Reporting Rules”) for SDs and MSPs that are non-U.S. persons (as defined in the CFTC’s Cross-Border Guidance,

¹ See our client memorandum, “CFTC Cross-Border Guidance, Temporary Exemptive Order and No-Action Letters,” dated July 24, 2013, available at <http://www.debevoise.com/newseventspubs/publications/detail.aspx?id=e39c6856-07fa-4600-867d-ed23701a1ef0>

dated July 26, 2013)² established under the laws of the Enumerated Jurisdictions (other than Hong Kong) and that are not part of an affiliated group in which the ultimate parent entity is a U.S. SD, U.S. MSP, U.S. bank, U.S. financial holding company or U.S. bank holding company.

Finally, on December 20, 2013, the CFTC issued another no-action letter (the “Internal Business Conduct Rules Letter”) granting temporary no-action relief from certain entity-level internal business conduct requirements which were not covered by the CFTC’s comparability determinations for SDs and MSPs established under the laws of the Enumerated Jurisdictions (other than Hong Kong) in order to provide such SDs and MSPs with an opportunity to prepare for compliance with such Regulations.

COMPARABILITY DETERMINATIONS

The comparability determinations permit substituted compliance for a broad range of “entity-level” business conduct requirements (set forth in the attached Table I) for SDs and MSPs in the Enumerated Jurisdictions based on a finding that the relevant regulatory requirements imposed by such jurisdictions are comparable to and as comprehensive as the corresponding requirements in the CEA and the CFTC Regulations.

In addition to the comparability determinations for certain entity-level requirements covering the six Enumerated Jurisdictions, the CFTC also approved substituted compliance for certain “transaction-level” requirements for SDs and MSPs in the European Union (the “EU”) and Japan. For the EU, the CFTC issued comparability determinations for transaction-level requirements under Regulations 23.501 (trade confirmation), 23.502 (portfolio reconciliation), 23.503 (portfolio compression) and certain provisions of Regulations 23.202 (daily trading records)³ and 23.504 (swap trading relationship documentation).⁴ For Japan, the CFTC issued comparability determinations for transaction-level requirements under Regulation 23.202 and certain provisions of Regulation 23.504.⁵

² See our client memorandum referred to in footnote 1 above.

³ The EU comparability determination for Regulation 23.202 applies to all requirements under that section other than the requirements of subsections (a)(1) and (b)(1) (requiring that SDs and MSPs keep records of all oral and written communications concerning quotes, solicitations, bids, offers, instructions, trading and prices, that lead to the execution of a swap or a related cash or forward transaction).

⁴ The EU comparability determination for Regulation 23.504 applies only to subsections (b)(2) (requiring that the swap trading relationship documentation include all confirmations of swap transactions) and (b)(4) (requiring that such documentation include a swap valuation process and a process for resolving valuation disputes).

⁵ The Japan comparability determination for Regulation 23.504 applies only to subsections (a)(2) (requiring SDs and MSPs to maintain and follow policies and procedures designed to ensure that they execute written swap trading relationship documentation with their counterparties), (b)(1) (requiring that such documentation be in writing and

NO-ACTION RELIEF FROM SDR REPORTING RULES

Background

On July 22, 2013, the CFTC published in the Federal Register an order (the “Exemptive Order”) which, among other things, permits non-U.S. SDs and non-U.S. MSPs established in specified non-U.S. jurisdictions to delay, under certain circumstances and subject to certain conditions, compliance with the SDR Reporting Rules with respect to their swaps with non-U.S. counterparties.⁶ This exemptive relief expired on December 21, 2013.

No-Action Relief

The SDR Reporting Rules Letter states that, in light of the expiration of the Exemptive Order, the Division of Market Oversight of the CFTC will not recommend that the CFTC take an enforcement action against a non-U.S. SD or MSP in Australia, Canada, the EU, Japan or Switzerland, that is not a part of an affiliated group in which the ultimate parent entity is a U.S. SD, U.S. MSP, U.S. bank, U.S. financial holding company or U.S. bank holding company, for failure to comply with:

- the requirements of Part 45 and 46 with respect to its swaps with non-U.S. counterparties that are not guaranteed affiliates⁷ or conduit affiliates⁸ of a U.S. person, until the earlier of: (1) 30 days following the issuance of a comparability determination by the CFTC with respect to the SDR Reporting Rules for the jurisdiction in which the non-U.S. SD or MSP is established and (2) December 1, 2014;

include all terms governing the trading relationship), (b)(2) (requiring that such documentation include all confirmations of swap transactions), (b)(3) (requiring that such documentation include credit support arrangements), (b)(4) (requiring that such documentation include a swap valuation process and a process for resolving valuation disputes), (c) (requiring independent audits of the documentation policies and procedures of an SD or MSP) and (d) (recordkeeping requirements for such documentation).

⁶ See our client memorandum referred to in footnote 1 above.

⁷ A “guaranteed affiliate” is defined in the CFTC’s Cross-Border Guidance as a non-U.S. person that is an affiliate of a U.S. person and that is guaranteed by a U.S. person.

⁸ A “conduit affiliate” is defined in the CFTC’s Cross-Border Guidance as an entity that functions as a conduit or vehicle for U.S. persons conducting swaps with third parties. The following factors are relevant to determining whether a non-U.S. person is a conduit affiliate: (1) the non-U.S. person is a “majority-owned affiliate” (as defined in Regulation 1.3(ggg)(6)(i)) of a U.S. person; (2) the non-U.S. person is controlling, controlled by or under common control with the U.S. person; (3) the financial results of the non-U.S. person are included in the consolidated financial statements of the U.S. person and (4) the non-U.S. person, in the regular course of business, engages in swaps with non-U.S. third parties for the purpose of hedging or mitigating risks faced by, or to take positions on behalf of, its U.S. affiliates, and enters into offsetting swaps or other arrangements with its U.S. affiliates in order to transfer the risks and benefits of such third-party swaps to its U.S. affiliates. For more information on conduit affiliates, see our client memorandum referred to in footnote 1 above.

- the requirements of Part 45 with respect to its swaps with non-U.S. counterparties that are guaranteed affiliates, or conduit affiliates, of a U.S. person, until March 3, 2014; and
- the requirements of Part 46 with respect to its swaps with non-U.S. counterparties that are guaranteed affiliates, or conduit affiliates, of a U.S. person, until April 2, 2014.

NO-ACTION RELIEF FROM ENTITY-LEVEL BUSINESS CONDUCT RULES

Background

The same Exemptive Order, which expired on December 21, 2013, also permitted non-U.S. SDs and MSPs established in specified non-U.S. jurisdictions to delay compliance with certain entity-level requirements.

The CFTC excepted Regulation 23.600(c)(2) (periodic risk exposure reports) from its comparability determinations described above and declined to take up determinations for Regulation 23.608 (restrictions on counterparty clearing relationships) for any jurisdiction, or for Regulation 23.609 (clearing member risk management) for Hong Kong and Switzerland, each of which regulations were the subject of the compliance relief that expired on December 21, 2013.

No-Action Relief

The Internal Business Conduct Rules Letter states that, in order to provide non-U.S. SDs and MSPs established in Australia, Canada, the EU, Japan and Switzerland⁹ with an opportunity to prepare for compliance with Regulations 23.600(c)(2) and 23.608, and, in the case of a non-U.S. SD or MSP established in Switzerland, Regulation 23.609, the Division of Swap Dealer and Intermediary Oversight of the CFTC will not, prior to March 3, 2014, recommend that the CFTC take an enforcement action against:

- a non-U.S. SD or MSP established in Australia, Canada, the EU, Japan or Switzerland for failure to comply with Regulations 23.600(c)(2) or 23.608; or
- a non-U.S. SD or MSP established in Switzerland for failure to comply with Regulation 23.609.

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Please do not hesitate to contact us with any questions.

December 24, 2013

⁹ The CFTC notes in the Internal Business Conduct Rules Letter that, as of December 21, 2013, no non-U.S. SD or MSP established in Hong Kong would be required to comply with Regulations 23.600(c)(2), 23.608 or 23.609 and that, as a result, no relief for any such SD or MSP is necessary.

TABLE I

**BUSINESS CONDUCT RULES for SWAP DEALERS and MAJOR SWAP PARTICIPANTS
SUMMARY OF ENTITY-LEVEL COMPARABILITY DETERMINATIONS**

The following table presents, in summary form, the determinations of the Commodity Futures Trading Commission (“Commission”) that certain entity-level regulatory requirements in Australia, Canada, the European Union (“EU”), Hong Kong, Japan, and Switzerland are comparable to and as comprehensive as certain entity-level business conduct requirements for non-U.S. swap dealers and non-U.S. major swap participants under the Commodity Exchange Act and the Commission’s regulations.

COMPARABILITY DETERMINATION						
Commission Rule	<u>Australia</u>	<u>Canada</u>	<u>EU</u>	<u>Hong Kong</u>	<u>Japan</u>	<u>Switzerland</u>
Chief Compliance Officer § 3.3	Comparable (Notes 1, 2)	Comparable (Note 2)	Comparable (Note 2)	Comparable (Note 2)	Comparable (Note 2)	Comparable (Note 2)
Swap Data Recordkeeping §§ 23.201, 23.203	Comparable (Note 4)	Comparable (Note 4)	Comparable (Note 4)	Comparable (Note 4)	Comparable	Comparable (Note 4)
Risk Management Program § 23.600	Comparable (Note 3)	Comparable (Note 3)	Comparable (Note 3)	Comparable (Note 3)	Comparable (Note 3)	Comparable (Note 3)
Monitoring of Position Limits § 23.601	Comparable	Comparable	Comparable	Comparable	Comparable	Comparable
Diligent Supervision § 23.602	Comparable	Comparable	Comparable	Comparable	Comparable	Comparable
Business Continuity § 23.603	Comparable	Comparable	Comparable	Comparable	Comparable	Comparable
Research Conflicts § 23.605(c)	Comparable	Comparable	Comparable	Comparable	Comparable	Comparable

COMPARABILITY DETERMINATION						
<u>Commission Rule</u>	<u>Australia</u>	<u>Canada</u>	<u>EU</u>	<u>Hong Kong</u>	<u>Japan</u>	<u>Switzerland</u>
Clearing Conflicts § 23.605(d)	Comparable	Comparable	Comparable	Comparable	Comparable	Comparable
Undue Influence § 23.605(e)	Comparable	Comparable	Comparable	Comparable	Comparable	Comparable
Availability of Information for Disclosure § 23.606	Comparable (Note 4)	Comparable (Note 4)	Comparable (Note 4)	Comparable (Note 4)	Comparable	Comparable (Note 4)
Clearing Member Risk Management § 23.609	Comparable	Comparable	Comparable	No Determination	Comparable	No Determination

Note 1: Other than for § 3.3(e), which requires a swap dealer or MSP to produce an annual compliance report and stipulates the content thereof.

Note 2: Other than for § 3.3(f), which requires (i) the CEO or CCO of a swap dealer or MSP to certify that the annual compliance report is accurate and complete, and (ii) the annual compliance report to be furnished to the Commission.

Note 3: Other than for § 23.600(c)(2), which requires a swap dealer or MSP to produce quarterly risk exposure reports and provide such reports to its senior management, governing body, and the Commission.

Note 4: The Commission reserves the right to require a swap dealer or MSP to provide direct access to or produce records required to be maintained under the CEA and Commission regulations to Commission staff, the staff of an applicable U.S. prudential regulator, or the U.S. Department of Justice.