August 21, 2013

Comments on Commodity Futures Trading Commission`s **"**Exemptive Order Regarding Compliance with Certain Swap Regulations**"** and **"**Interpretive Guidance and Policy Statement Regarding Compliance with Certain Swap Regulations**"**

Japanese Bankers Association

We, the Japanese Bankers Association ("JBA"), would like to express our gratitude for this opportunity to comment on the "Exemptive Order Regarding Compliance with Certain Swap Regulations" （"Exemptive Order"）proposed in 12 July 2013 by the Commodity Futures Trading Commission.

We hope that our comments below will be fully taken into consideration as you work towards finalizing the rules proposed by the CFTC.

<General Comments>

Expiration of the Exemptive Order

The Exemptive Order provides time-limited relief from certain requirements under the *Interpretive Guidance and Policy Statement Regarding Compliance with Certain Swap Regulations* ("Interpretive Guidance") which was contemporaneously published by the CFTC. For example, the application of some requirements may be delayed "until 75 days after the Guidance is published in the Federal Register," or "until the earlier of December 21, 2013 or 30 days following the issuance of a substituted compliance determination for the relevant regulatory requirements of the jurisdiction in which the non-U.S. SD or non-U.S. MSP is established." We highly appreciate that the CFTC has given due regard to comments provided by governments and market participants including the JBA in relation to the CFTC's Further Proposed Guidance published in January 2013.

However, since the discussion on the cross-border application issue among relevant authorities which is expected to make further progress is still underway, applying the Interpretive Guidance ahead of completing this discussion process is likely to impose a considerable compliance burden on market participants (including non-financial companies) within and outside the United States and may have an adverse impact on the smooth operation in the market. It is therefore respectfully requested that the CFTC finalizes the effective date of the Interpretive Guidance when the cross-border application issue is fully discussed among relevant authorities across jurisdictions as well as when financial institutions are well-prepared for compliance.

<Specific Comments>

This section describes our concerns regarding certain requirements set forth under the Exemptive Order and Interpretive Guidance, and provides our comments that would hopefully be of help to address such concerns.

1. Definition of "U.S. Person" and its Effective Date

(1) Definition of "U.S. Person"

The Interpretive Guidance recently published newly adds the (vi) and (vii) to the definition of the term "U.S. person."[1] We understand that these two prongs added indicate that even a fund established outside the United States is deemed to be a U.S. person if its investors are a U.S. person and its investments are not limited to a non-U.S. person.

According to this interpretation, a non-U.S. person needs to assess, for the purpose of calculating de minimis threshold for the swap dealer ("SD") registration determination, whether the fund, its counterparty, is a U.S. person by looking through to the U.S. / Non-U.S. person status of the fund's investors. It, however, will require a considerable amount of workload for a non-U.S. person to confirm the nationality, principal place of business, the level of substantial control by a U.S. person, the nature of transactions and other necessary information of the fund i.e. its counterparty. Particularly, it will be extremely difficult when such a fund further invests in multiple hedge funds. Given this, the CFTC is respectfully requested to place the burden on the funds to advise their counterparties of U.S. person status, or to disclose information which would enable their counterparties to easily assess the U.S. / Non-U.S. person status of the funds. Approaching each and every fund to determine the status is problematical.

Under the scheme of trust funds such as investment trusts that are publicly offered and traded in Japan, an investment trust distributor generally engages in the offering activities. Therefore, a significant burden and cost will be incurred on a trust bank (i.e. the trustee) to research whether any of ultimate beneficiaries of investment trusts are U.S. persons, and hence such research may be extremely difficult. Although trust funds such as investment trusts that are publicly offered and traded in Japan do not necessarily prohibit offering to U.S. persons under terms and conditions defined in a contract, it is considered that no investment trust is majority-owned by a U.S. person(s) because they are publicly offered inside Japan. In addition to such publicly-offered investment trusts, in the case of corporate pension funds, etc., it is also considered that no fund is majority-owned by a U.S. person(s) because such pension funds are established for the employees of those companies

[1] Interpretive Guidance Ⅳ.A.4.(ⅵ)(ⅶ) (Federal Register45317)

located in Japan. In view of this, it is unreasonable to invest significant effort and cost for the assessment of the U.S. / Non-U.S. person status of ultimate beneficiaries in order to prove this. If trust funds launched in Japan are construed as being a "collective investment vehicle" defined under the Interpretive Guidance, it is respectfully requested that the CFTC takes into account varied market conditions/practices across jurisdictions and establish a procedure that allows Non-U.S. person to determine whether collective investment vehicle or non-U.S. company pension fund are majority owned by U.S. person.

For example, in the case of a trust fund which is launched by a Japan - domiciled trustor (investor) and publicly offered by the trustor or through Japan – domiciled distributors, etc., it is obvious that such a fund is not targeted to U.S. investors unless otherwise stipulated in the contract or prospectus. In light of this, the following treatment should be permitted: "a fund that is launched by a non-U.S. person and sold/offered outside the United States by a non-U.S. person is not deemed as a U.S. person unless the contract/prospectus, etc. stipulates that the fund is offered to U.S. investors."

Further, in the case of trust funds in Japan, determination of their "principal place of business" should be based on the location of investors to funds (i.e. the trustor of the fund) or that of a trust bank (i.e. the trustee and nominee of the fund, having the right to manage and dispose of the fund), and should not be based on the location of investment advisors and/or managers who have no right to manage the trust and only have the right to give investment instructions.

(2) Effective date of the definition of "U.S. Person"

As the definition of the term "U.S. person" under the Interpretive Guidance is extremely complicated, it will require a considerable amount of time to collect and analyze necessary information for the purpose of assessing all counterparties to determine whether they meet the revised definition of the term "U.S. person" or to obtain a representation of U.S. / Non-U.S. person status from counterparties. Given this, it is requested that the Exemptive Order allows market participants to apply the revised definition of the term "U.S. person" under the Interpretive Guidance at least from December 21, 2013 at earliest, instead of from "75 days after the Guidance is published in the Federal Register."

2. Areas Needed to be Confirmed and Areas of Request Concerning De Minimis Calculation

(1) "A non-U.S. person guaranteed by a U.S. person"

We would like to confirm whether the following understanding is correct: if a counterparty is deemed "a non-U.S. person guaranteed by a U.S. person," swap transactions with this counterparty need to be included in the de minimis calculation only when (a) this "non-U.S. person guaranteed by a U.S. person" is not an SD nor affiliated with an SD and (b) this U.S. guarantor is a Financial Entity.

Further, please confirm whether the scope of such a “guaranty” is limited to those guarantees associated with derivatives. If the term “guaranty” encompasses those transactions unrelated to derivatives, such a treatment contravenes the objectives of derivatives regulation. Thus, we believe that the scope of “guaranty” should be limited to those guaranties associated with derivatives.

We also would like to confirm whether the new requirement to include in the de minimis calculation those swap dealing activities with “a non-U.S. person guaranteed by a U.S. person” will be applied only to swaps entered into after the effective date of the Interpretive Guidance. As this requirement was not set forth under the Proposed Guidance, this requirement should not be applied retroactively, but rather be applied to swap entered into after the date when the Interpretive Guidance is put into effect.

Pursuant to the Interpretative Guidance, a Japanese bank may exclude from its de minimis calculation any dealing transaction with a counterparty that is guaranteed by a U.S. person and affiliated with a swap dealer. The CFTC did not define the term “affiliate” in this context. We would like to apply ” affiliate under common control” stipulated in note 268 of Federal Register P.45320 and ask the CFTC for confirmation on this point.

(2) Monitoring of de minimis threshold calculation with respect to joint ventures

There may be a case where a joint venture entered into by multiple financial institutions which are unaffiliated with each other is deemed an affiliate of any financial institution in the group. In such a case, swap dealing transactions by the joint venture would be included in the de minimis calculation of each financial institution group while the joint venture itself includes swap dealing transactions by each financial institution member for its own de minimis calculation. However, double-counting of the same transaction or requiring aggregation of a transaction with multiple financial institution groups for the de minimis calculation purpose should be avoided. Therefore, where a joint venture is entered into by multiple financial institutions, it should be made clear that its swap dealing activity shall be subject to the de minimis calculation and monitored only by the one financial institution member which owns a majority of the voting rights of the joint venture and controls its operation in substance.

(3) Treatment of U.S. Affiliate and SD that may be excluded from aggregation for purpose of the de minimis calculation

The Exemptive Order sets out that a non-U.S. person that was engaged in swap dealing activities with U.S. persons as of December 21, 2012 is not required to include the aggregate gross notional amount of swap transactions of its U.S. affiliates under common control, its affiliates registered as SD, and its non-U.S. affiliates which were engaged in swap dealing activities with U.S. persons as of

December 21, 2012. However, we think that the definition of the "non-U.S. person that was engaged in swap dealing activities with U.S. persons as of December 21, 2012" is unclear. A non-U.S. person should be unconditionally allowed, to exclude in the aggregation for their group's de minimis calculation, the swap dealing activities of their U.S. affiliates under common control, their affiliates registered as a swap dealer, and their non-U.S. affiliates. Further, it should be made clear that such exclusion is applicable not only to transactions executed on or after December 21, 2012 but also to all transactions executed on or after October 12, 2012 when the aggregation for the de minimis threshold calculation had started.

Under the Interpretive Guidance, swap transactions by entities registered as swap dealers are not required to be included in the aggregation for the purpose of a group's de minimis threshold calculation. Similarly to the aforementioned request, it should be made clear that this exclusion is applicable not only to those transactions executed after the SD registration but also to those transactions executed before the SD registration retroactively to the point when the aggregation for the de minimis threshold calculation purpose had started. If such exclusion is not allowed, swap transactions by a registered SD entity within a group executed prior to the entity's SD registration could be improperly included in a group's de minimis threshold calculation.

(4) Difference between SD and MSP threshold calculations in exclusion of certain swap counterparties from such calculations

It is considered that swap transactions with (i) a non-US branch of a U.S. swap dealer, (ii) a guaranteed affiliate which is a swap dealer, (iii) a guaranteed affiliate which is not a swap dealer, which is a non-U.S. person, and which is guaranteed by a swap dealer (including an affiliate of a swap dealer) and (iv) non-U.S. entity guaranteed by a non-financial entity, need not to be counted for the swap dealer de minimis threshold calculation purpose. On the other hand, it is not stipulated that swap transactions with above (iii) and (iv) may be excluded from the MSP threshold calculation purposes. It is therefore respectfully requested that in a case where at least one party to a transaction is a financial institution that is a non-U.S. person, the same scope of aggregation relief for the SD threshold calculation should also be available to the MSP threshold calculation.

(5) Eligibility criteria for treating a swap as being with a foreign branch of a U.S. bank

The Interpretive Guidance sets forth the criteria (i) to (v) permitting swap transactions with a foreign branch of a U.S. bank which is SD to be excluded from the calculation of the de minimis threshold for the swap dealer registration determination, and explicitly indicates that such criteria are applied to the Exemptive Order as well. As the criteria (i) to (v) for swap transactions with the foreign branch of the U.S. bank with regard to the calculation of the de minimis threshold are newly defined in the Interpretive Guidance, the determination of whether such swap transactions fall within the criteria (i) to (v) requires a considerable period of time. As with the definition of a U.S. person, we respectfully request the CFTC to allow firms to comply only with the Exemptive Order during the period the Exemptive Order is effective, and also to exclude from the threshold calculation for the swap dealer registration determination swap transactions with the foreign branch of the U.S. bank which is SD without setting any conditions. On the other hand, it is difficult for a non-U.S. person to determine whether its swap transactions with a non-U.S. branch of U.S. banks meet the criteria (i) to (v), while its counterparty, a U.S. person, is not obliged to confirm whether the dealing activity meets the criteria. Given this, if conditions are set, it is requested to set forth more simplified rules, for example, that shift the burden of the non-U.S. branch of the U.S. swap dealer to advise the non-U.S. person that the transaction is not with the foreign branch.

In addition, a foreign branch of a U.S. bank which is a swap dealer is an integral part of the U.S. principal entity which is a swap dealer, and should assume the same obligations as swap dealers or comply with the same rules as U.S. rules. As such, a swap transaction with the foreign branch of the U.S. bank is fully monitored by the regulators and hence risks are considered to be mitigated. It is therefore requested that the Interpretive Guidance allows excluding any swap transactions with the foreign bank of the U.S. bank from the calculation of the de minimis threshold, without setting any conditions.

3. Scope of Central Clearing Mandate for Yen Interest Rate Swap Transactions

JPY interest rate swaps are subject to central clearing mandate under the Financial Instruments and Exchange Act in Japan, while a non-U.S. person, a counterparty of such swap, executing a transaction with a U.S. bank needs to comply with central clearing mandate under the U.S. Dodd-Frank Act. In Japan, in relation to yen interest rate swaps, a mechanism of indirect clearing participation for eligible central counterparties (“CCPs”) has not yet been established, and eligible CCPs defined in the U.S. regulation is not yet authorized in Japan. As such, there is a concern that Japanese financial institutions may not satisfy the central clearing mandate under both applicable Japan and U.S. regulation, giving rise to a possibility of Japanese financial institutions not being able to execute a swap transaction. In order to facilitate swap transactions in the cross-border swap markets, such inconsistency should be eliminated at an earlier stage. In the process of mutual

recognition of CCPs across the jurisdictions which may be necessary for such elimination, inconsistencies should be flexibly addressed on a case-by-case basis, such as publishing a No-Action Letter that allows the application of a substituted compliance.

Furthermore, 6 countries, which are Australia, the European Union, Hong Kong, Switzerland, Canada and Japan, may delay complying with the clearing requirement until 75 days after the publication of the Guidance in the Federal Register, and are granted a period of time for Substituted Compliance Determination. However, in order to ensure sufficient determination period, alike the other requirements, the relief period should be set until December 21.

4. Substituted Compliance

(1) Comprehensive substituted compliance

The scope of the application of substituted compliance involving comparability determination was commented on by the Financial Services Agency in Japan ("JFSA") in August 2012. [2] As stated in this letter, the comparability determination should be carried out by each jurisdiction in a comprehensive manner in light of whether foreign regulations broadly harmonize with U.S. regulations and are consistent with the overall objectives of G20 commitment. It is therefore requested to make a substituted compliance determination in a comprehensive manner, rather than on a requirement-by- requirement basis.

(2) Application of substituted compliance to Transaction Level Requirements

As noted in the General Comments above, it is requested to give a due consideration in determining the timing of the cross-border application. With regards to the substituted compliance for Transaction Level Requirements, in order to set aside a reasonable preparation period, regardless of whether substituted compliance is possible or not, we respectfully request to delay compliance until 90 days, not 30 days currently provided, following the issuance of a Substituted Compliance Determination for the relevant Transaction-Level Requirement. Even, as a result, the compliance date is beyond December 21, such relief period should still be ensured.

(3) Substituted compliance for SDR Reporting

Substituted compliance for SDR Reporting is currently being discussed among financial regulators on issues such as a framework for mutual access. This, therefore, should be solved in this discussion process. Since a report on transactions with a U.S. person is made to the CFTC, a condition that the CFTC has direct access to swap data should not be required.

5. Treatment of a U.S. Branch of a non-U.S. SD

[2] See the JFSA's comment letter dated August 13, 2012 (http://www.fsa.go.jp/inter/etc/20120820-1/01.pdf)

Although a U.S. branch of a non-U.S. SD[3] is treated as a non-U.S. person, the Interpretive Guidance states that the CFTC takes the view that a U.S. branch of a non-U.S. swap dealer would be subject to Transaction-Level requirements, without substituted compliance available, and recognizes its strong supervisory interest in regulating the dealing activities that occur with the United States. Therefore, an impact of a transaction with a U.S. branch of a non-U.S. SD is considered to be unclear. As was previously the case, a transaction between a U.S. branch of a non-U.S. SD and a non-U.S. person should not be subject to the CFTC rules. If a transaction between a U.S. branch of a non-U.S. SD and a non-U.S. person is subject to the Dodd-Frank Act requirements, problems may occur in executing transactions within a home jurisdiction and outside U.S., causing a significant negative impact on the market.

[3] Interpretive Guidance Ⅳ.G.4.a.(Federal Register45350 fn513)