March 9, 2020

Mr. Christopher Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street NW
Washington, DC 20581

Comments on Cross-Border Application of the Registration Thresholds and Certain Requirements Applicable to Swap Dealers and Major Swap Participants - RIN3038−AE84

Dear Mr. Kirkpatrick:

We, the Japanese Bankers Association (JBA), would like to express our gratitude for this opportunity to comment on "Cross-Border Application of the Registration Thresholds and Certain Requirements Applicable to Swap Dealers and Major Swap Participants" ("Proposed Rule") issued by the Commodity Futures Trading Commission (CFTC) on January 8, 2020. We respectfully expect that the following comments will contribute to your further discussion.

[General comments]

We generally support the overall proposals in the Proposed Rule, which reflects our request for clarification in our comment letter submitted in 2018[1] and that CFTC give due consideration to avoid the duplicative and overlapping requirements and market fragmentation.

We, however, still have some concern over the following issues and would like to request the CFTC to further consider them.

1. Clarification of the cross-border application of requirements to non-U.S. persons

The Proposed Rule still does not address how other various requirements[2] would be applied to non-U.S. persons. In order to develop an optimal regulatory regime as a whole, we request the CFTC to clarify as soon as possible the cross-border application of such requirements, and to consider harmonizing the timing of application of such requirements with the Proposed Rule so that all requirements would be applied simultaneously.

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[1] https://www.zenginkyo.or.jp/fileadmin/res/abstract/opinion/opinion300843.pdf

[2] These includes central clearing obligations, trade execution requirements, swap data repository reporting requirements (entity-level requirements), real-time public reporting requirements (transaction-level requirements) and Group A requirements (some entity-level requirements: chief compliance officer, risk management, swap data recordkeeping, antitrust considerations).

2. Review of the definition of a significant risk subsidiary ("SRS")

The CFTC currently applies the swap requirements extraterritorially, if the activities have a "direct and significant connection with activities in, or effect on, commerce of the United States" (CEA Section 2(i)). With respect to the concept of the SRS, which is newly introduced in the Proposed Rule, a bailout of the SRS by the parent company is not legal obligation unlike a guarantee that clearly imposes economic burden on the guarantor. Therefore, the degree of effects on the U.S. commerce is not necessarily clear. Despite such uncertainty, applying the swap rules extraterritorially to SRSs may unduly expand the scope of the rules. This would not satisfy "Guiding Principles for Regulating Foreign Activities[3]" issued by Chairman Tarbert and thus would contradict the objective of the rules.

Furthermore, swap market participants have already completed their assessment to determine the attribute of covered swap entities under U.S. rules based on the "Interpretive Guidance and Policy Statement Regarding Compliance With Certain Swap Regulations (2013 Guidance)"[4] published in July 2013. In a situation where practice has already been established based on the current approach, the introduction of the newly-introduced SRS category will require them to re-assess the attribute of the counterparty, imposing significant burdens on them. In view of this point, we request the CFTC to maintain the 2013 Guidance framework, considering a cost-effectiveness.

3. Clarification of how the Proposed Rule is applied to a "non-U.S. person" that is not registered as a swap dealer (SD) or major swap participant (MSP)

The 2013 Guidance provided specific guidance in section "X. Appendix F" on how certain swap rules would be applied to a "non-U.S. person" that is not registered as an SD or MSP. The Proposed Rule, however, does not address a non-U.S. person that is not registered as an SD or MSP while it sets out how the group B requirements and the group C requirements will be applied to a "non-U.S. swap entity" that is a registered SD or MSP.

As such, we request the CFTC to clarify how regulatory requirements will be applied to a non-U.S. person that is not registered as an SD or MSP when its counterparty is a U.S. person or SRS. We understand that relevant rules will directly be applied to SDs or MSPs or U.S. persons and thus assume that they will only be applied indirectly to non-U.S. persons that are not registered as SDs or MSPs (that is, these rules will be applied to non-U.S. persons that are not registered as SDs or MSPs only when it is necessary to do so for the SDs or MSPs or the U.S. persons to comply with such rules). Please inform us whether our understanding is correct. If it is correct, we request the CFTC to clarify the details of the regulatory requirements that are

[3] The "Guiding Principles for Regulating Foreign Activities" set forth in the "Statement of Chairman Heath P. Tarbert in Support of the Cross-Border Swaps Proposal" include, but not limited to: "(1) Protect the National Interest".

[4] https://www.govinfo.gov/content/pkg/FR-2013-07-26/pdf/2013-17958.pdf

indirectly applied to non-U.S. persons, in a manner consistent with “X. Appendix F” in 2013 Guidance.

4. Ensuring symmetric application with respect to entities exempted from the requirements

CFTC should review the Proposed Rule from the perspective of ensuring symmetric application of requirements between U.S. swap entities and non-U.S. swap entities. Specifically, in Table C in the section “IV. Presumable Summary Tables", an exception consistent with the Foreign Branch Group B Exception should be applicable to the non-U.S. swap entities even when their counterparty is a foreign branch of a U.S. person.

An example of the above is a swap between the Seoul branch of the U.S. bank (i.e. a U.S. swap foreign branch) registered as an SD and the Tokyo HQ of the Japanese bank (i.e. a non-U.S. swap entity) registered as an SD. In this case, as referred to in the footnote 2 of Table C, the former may be allowed to rely on the Foreign Branch Group B Exception, up to five percent of all its swaps in any calendar quarter on the basis of aggregate gross notional amounts, whereas such an exception is not available for the latter. Such treatment results in asymmetric application of requirements and the rationale of such asymmetric application is unclear.

5. Expansion of the scope of the proposed exclusion of cleared swaps from Other Non-U.S. Person’s de minimis threshold calculation

In §23.23(d), the Proposed Rule allows an Other Non-U.S. Person to exclude from its de minimis threshold calculation any swaps entered into anonymously on a designated contract market (“DCM”), a registered or exempt swap execution facility (“SEF”), or a foreign board of trade (“FBOT”) if such swap is also cleared through a registered or exempt derivatives clearing organization (“DCO”). With respect to the level of risks posed to the U.S commerce, we generally support this proposal. We also would like to propose to expand the scope of this exclusion to allow an Other Non-U.S. Person to exclude from its de minimis threshold calculation all swaps that are cleared through a registered or exempt DCO regardless of whether they are anonymously entered into on a DCM, a registered or exempt SEF, or an FBOT. The inclusion of all swaps, which meet the conditions specified above, in the calculation is excessive. Since once a swap is cleared through these facilities, the swap is no longer exposed to counterparty risk, therefore a significant systemic risk posed to the U.S. commerce would be limited. Moreover, expanding the scope of this exclusion would encourage market participants to use clearing organizations and promote the liquidity of global swap markets. From these viewpoints, we believe that expanding the scope of the proposed exclusion will benefit both U.S. persons and non-U.S. persons.

6. Consideration of the treatment of a U.S. branch of a non-U.S. swap entity

Regulatory requirements that are not to be addressed at a branch level should not be applied

differently between a non-U.S. person's U.S. branch and other categories of a non-U.S. person. Consistent with the current 2013 Guidance, we request that transactions between non-U.S. persons (excluding cases where a counterparty apparently has a connection with the U.S. commerce, such as a Guaranteed Entity) are treated as "Do Not Apply," regardless of the location of a branch.

Taking Table C as an example, it is proposed to apply certain Group B requirements to a non-U.S. person's U.S. branch only. Portfolio reconciliation and swap trading documentation, however, are required to be performed not only by the U.S. branch but also firm-wide including its HQ. The impact of transactions between non-U.S. persons on the U.S. commerce is generally limited. Therefore, we request the CFTC to carefully consider how to apply these requirements.

[Comments to the Questions]

II. Key Definitions

A. U.S. Person, Non-U.S. Person, and United States

(2) Is it appropriate, as proposed, that commodity pools, pooled accounts, investment funds, or other CIVs that are majority-owned by U.S. persons not be included in the proposed definition of "U.S. person"? Would a majority of such funds or CIVs be subject to margin requirements of foreign jurisdictions? Is it accurate to assume that the exposure of investors to losses in CIVs is generally capped at their investment amount? Does tracking a CIV's beneficial ownership pose challenges in certain circumstances?

(Comment)

We consider it appropriate <u>not</u> to include commodity pools, pooled accounts, investment funds, or other CIVs ("investment funds, etc.") that are majority-owned by U.S. persons in the definition of "U.S. person."

(Rationale)

It is not realistic to include investment funds, etc. that are majority-owned by U.S. persons in the definition of "U.S. person" since significant practical burdens would arise from identifying and tracking the beneficial ownership of investment funds, etc. on a real time basis. There is a concern that non-U.S. persons may ultimately make a judgment not to engage in any transactions related to investment funds, etc. in which U.S. persons are involved so as to avoid such practical burdens and excessive cost arising from the registration threshold calculations. This may disrupt sound and active marketplace.

(5) Should the "U.S. person" definition include a catch-all provision? What types of entities would be expected to fall under such a provision?

(Comment)

We consider that the "U.S. person" definition should not include a catch-all provision.

(Rationale)
The inclusion of the catch-all provision may lead to instances where a non-U.S. person cannot clearly make a judgment whether an entity meets the conditions of the "U.S. person" or where a uniform conclusion cannot be reached based on the applicable provisions. In that case, a non-U.S. person may be compelled to take conservative actions in practice (i.e., the non-U.S. person will deem this entity to be a "U.S. person" and avoid or limit engaging in a transaction with this entity, or take regulatory actions that are unnecessary under normal conditions). We believe that such situation may drive further bifurcation of the global swaps markets into separate U.S. person and non-U.S. person marketplaces, which will contradict the objective of the rules.

III. Cross-Border Application of the Swap Dealer Registration Threshold
B. Non-U.S. Persons

(19) Should a non-U.S. person be permitted to exclude from its de minimis threshold calculation swap dealing transactions conducted through a foreign branch of a registered SD?

(Comment)
We think that such transactions should be permitted to be excluded from the de minimis threshold calculation.

(Rationale)
A foreign branch of a registered SD is subject to regulation and supervision by the U.S. authorities as an SD, and hence the U.S. authorities are able to identify associated risks. We therefore consider it reasonable to exclude such transactions from the de minimis threshold calculation.

(20) As discussed in section II.F, under the Proposed Rule, the term "U.S. branch" would mean a branch or agency of a non-U.S. banking organization where such branch or agency: (1) is located in the United States; (2) maintains accounts independently of the home office and other U.S. branches, with the profit or loss accrued at each branch determined as a separate item for each U.S. branch; and (3) engages in the business of banking and is subject to substantive banking regulation in the state or district where located. Given that definition, would it be appropriate to require a U.S. branch to include in its SD de minimis threshold calculation all of its swap dealing transactions, as if they were swaps entered into by a U.S. person? Would it be appropriate to require an Other Non-U.S. Person to include in its SD de minimis threshold calculation dealing swaps conducted through a U.S. branch?

(Comment)

We do not consider it appropriate to require an Other Non-U.S. Person to include in its SD de minimis threshold calculation dealing swaps conducted by and/or through a "U.S. branch."

(Rationale)
We believe that the proposal provided in this question is inconsistent with the efforts being taken to solve the following issues recognized by the authorities for the current cross-border rules: "over-expansive," "insufficient deference to non-U.S. regulators," and "it has driven global market participants away from transacting with entities subject to CFTC swaps regulation (market fragmentation)." [5] Specifically, an Other Non-U.S. Person may be discouraged to conduct transaction activities of its U.S. branches in U.S. derivatives market, if swaps conducted by and/or through a U.S. branch were uniformly treated in the same manner as swaps conducted through a U.S. person and included in the Other Non-U.S. Person's SD de minimis threshold calculation, despite the fact that the risks of U.S. branches will eventually belong to their HQ, that is the Other Non-U.S. Person. Such situation may also prompt the fragmentation of the U.S. market and non-U.S. market.

(21) Under the Proposed Rule, an Other Non-U.S. Person would not be required to include its dealing swaps with an SRS or an Other Non-U.S. Person in its SD de minimis threshold. The Commission invites comment as to whether, and in what circumstances, a non-U.S. person should be required to include dealing swaps with a non-U.S. person in its SD de minimis threshold calculation if any of the risk of such swaps is transferred to an affiliated U.S. SD through one or more inter-affiliate swaps, and as to whether it would be too complex or costly to monitor and implement such a rule.

(Comment)
We believe that an Other Non-U.S. Person should not be required to include dealing swaps with a non-U.S. person in its SD de minimis threshold calculation in any circumstances.

(Rationale)
If this proposal was implemented, an Other Non-U.S. Person would need to assess whether a transaction with a non-U.S person should be included in its SD de minimis threshold calculation on an entity-by-entity basis. In addition to such operational burdens, the Other Non-U.S. Person would also need to assess whether a non-U.S. person counterparty will transfer any of the risk of the swaps to a U.S. SD on a transaction-by-transaction basis. We consider it unrealistic from a perspective of practical burden to mandate such assessment process to non-U.S. persons under the U.S. regulatory regime despite the fact that risks arising from the transactions between non-U.S. persons are very limited.

[5] CFTC "CROSS-BORDER SWAPS REGULATION VERSION 2.0"
https://www.cftc.gov/sites/default/files/2018-10/Whitepaper_CBSR100118.pdf

(22) With respect to proposed § 23.23(b)(2)(iii), should the Commission follow the SEC's approach, which does not require a non-U.S. person that is not a conduit affiliate nor guaranteed by a U.S. person to count dealing swaps with a non-U.S. person whose security-based swap transactions are guaranteed by a U.S. person. The SEC noted that "concerns regarding the risk posed to the United States by such security-based swaps, and regarding the potential use of such guaranteed affiliates to evade the Dodd-Frank Act . . . are addressed by the requirement that guaranteed affiliates count their own dealing activity against the de minimis thresholds when the counterparty has recourse to a U.S. person."

(Comment)

We believe that the CFTC should follow SEC's approach.

(Rationale)

Assessing whether the counterparty is a guaranteed affiliate imposes considerable burdens on non-U.S. persons for their entity-by-entity-basis assessment operations. Under such situation, assessing whether the counterparty is a Guaranteed Entity additionally imposes unrealistic and significant burdens on non-U.S. persons for their transaction-by-transaction-basis assessment operations.

Specifically, if swaps with a Guaranteed Entity conducted by an Other Non-U.S. person are required to be included in its SD registration threshold calculation, the Other Non-U.S. Persons are required to assess whether a transaction is guaranteed by a U.S. person for all counterparties whenever they enter into a transaction, even for non-financial enterprises which apparently have no connection with the U.S. Moreover, a U.S. person rarely offers a guarantee for such transactions, and hence the amount of associated risks is expected to be limited. Under these circumstances, imposing such practical burdens on non-U.S. persons is highly disproportionate to supervisory interest brought to the CFTC from the requirement.