

Brussels, 30 September 2014

Mr Timothy MASSAD
Chairman
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington DC 20581
United States of America

Subject: CROSS-BORDER OTC DERIVATIVES REFORM - substituted compliance and recognition of EU rules

Dear Chairman Massad,

We are very pleased to congratulate you on your appointment as Chairman of the Commodity Futures Trading Commission (CFTC). Over many years, the European Banking Federationⁱ (EBF) has been in constructive discussions with the CFTC, and we look forward to continue this cooperative relationship.

The EBF supports the aim of legislators and regulators in the EU, the U.S. and elsewhere to regulate derivatives markets in order to contain systemic risk and increase transparency in line with the commitment of G20 leaders. In this context, we commend the CFTC for its huge effort to put a corresponding regulatory framework in place for an important part of the global derivatives markets as mandated under Title VII of the Dodd-Frank Act. Furthermore, the EBF and its members very much welcome the ongoing efforts made by both U.S. and EU authorities aiming to enhance trans-Atlantic regulatory coordination.

Recent data-based research indicates that regulatory divergence and inconsistent implementation cause significant market fragmentation and liquidity problems¹ for market participants. We would ask you to continue working with your EU and international counterparts to increase the consistency of the regulation of global derivatives markets, both bilaterally and at the international level through IOSCO, FSB, and BCBS. We would ask that this is treated as a priority so as to realise the goals which were set by the international community and recognised in the U.S. and Europe.

In the wake of the recent financial crisis, global leaders pledged to act together in order to repair the financial system and to strengthen financial regulation. Aware of the high level of interconnectedness of the markets they called for the consistent implementation of the global standards *'in a way that ensures a level playing field and avoids fragmentation of markets, protectionism, and regulatory arbitrage'*. In the U.S., where these high-level principles have been implemented through the 2010 Dodd-Frank Act, Congress requires the relevant U.S. agencies, including the CFTC and the SEC, to

ⁱ Launched in 1960, the European Banking Federation is the voice of the European banking sector from the European Union and European Free Trade Association countries. The EBF represents the interests of some 4,500 banks, large and small, wholesale and retail, local and cross-border financial institutions. Together, these banks account for over 80% of the total assets and deposits and some 80% of all bank loans in the EU alone.

'consult and coordinate with foreign regulatory authorities on the establishment of consistent international standards' for derivatives regulation.

In June 2013, the EU Commission and the CFTC agreed in their *'Common path forward'* statement to implement rules and regulations in a manner that *'will address conflicts, inconsistencies, and uncertainty to the greatest extent possible and consistent with international legal principles.'* The EBF welcomed this step which came at a critical juncture.²

Despite all these calls, it is our view that we are still some way off from achieving a co-ordinated implementation of cross-border derivatives rules by the EU and the U.S. agencies. For instance, the existing U.S. rules,³ as currently applied, only allow to a rather limited extent non-U.S. Swap Dealers (SDs) and Major Swap Participants (MSPs) to substitute U.S. rules with comparable and comprehensive foreign jurisdiction rules. Moreover, narrowing already restrictive approach to substituted compliance of its July 2013 cross-border guidance even further, the CFTC staff in November 2013 issued an interpretation which requires a non-U.S. SDs or a non-U.S. MSPs transacting with a non-U.S. customer to comply with the CFTC's transaction-level requirements if the dealer's U.S. office assists in the transaction.⁴ This leads to duplicative requirements and additional compliance costs, even though such transactions do not pose any risk to the U.S. financial system.

The markets need clarity and a consistent approach to regulation in order to thrive. While we welcome the increased use of No-Action Letters by the CFTC,⁵ we hope that this move towards a reliable approach to US recognition of third country derivatives rules will continue and will be reflected on a more permanent and comprehensive basis. Moreover, we want to underline that recognition of equivalency of the regulatory frameworks on both side of the Atlantic is of utmost importance. In particular, positive equivalence/substitutive compliance decisions regarding CCPs and TRs, and margining requirements for non-cleared derivatives are key for all financial firms (and non-financial users of derivatives) operating on a cross-border basis, in order to avoid further market and regulatory fragmentation.

Today, the EBF welcomes and joins the G20 Finance Ministers calls to *'encourage jurisdictions to defer to each other when it is justified, in line with the St Petersburg Declaration.'*⁶ Our plea for a more comprehensive, permanent and reliable approach to U.S. recognition of EU derivatives rules is also justified by the fact that the EU has a rich and dip supervisory structure which creates an effective framework, exactly as the U.S. regulatory structure, directed at making markets safer and more resilient. Its effects can already be grasped across the EU.

The EBF agrees with the CFTC that the recognition of equivalence/substituted compliance should be based on an outcomes-based approach and that *'comparable does not necessarily mean identical'*. We agree that regulators should defer to each other when the rules developed in pursuance of the same international principles achieve the same regulatory objectives. In this regard, we support the recent EU Commission call for the alignment of international rules to avoid market fragmentation and arbitrage opportunities and we welcome your commitment to work with foreign supervisors to develop workable deference rules.

In light of the ongoing EU implementation of derivatives reform we therefore respectfully suggest that the CFTC offers further and more comprehensive, permanent and reliable recognition of equivalence/substituted compliance of EU rules in order to resolve outstanding issues in a practical way whilst minimising future legal uncertainty.

Additionally, as the issue of extraterritoriality is not limited to the EU and U.S. but goes far beyond, and given that the derivatives market is global in nature, we hope that the CFTC under your leadership will continue to pursue greater consistency of derivatives regulation also with other jurisdictions and

on a global basis through enhanced dialogue and the development of cooperation channels, such as OTC Derivatives Regulators Group (ODRG) and the IOSCO Cross-Border Taskforce.

Finally, we realise that this is not a one-sided issue and that U.S. regulators remain concerned about the EU position on equivalence and reciprocity, especially with regard to recognition of third country CCPs and of third country rules relating to risk mitigation for non-cleared derivatives. The EBF remains engaged in discussion with the EU Commission on these important issues.

Yours sincerely,



Wim Mijs
Chief Executive
European Banking Federation

cc to: Mr Michel Barnier, Vice-President of the European Commission, responsible for internal market and services (Michel.Barnier@ec.europa.eu).

¹ ISDA Revisiting Cross-Border Fragmentation of Global OTC Derivatives: Mid-year 2014 Update, 24 July 2014 (available at: <http://www2.isda.org/functional-areas/research/research-notes/>).

² EBF, Statement, EBF welcomes EU/US agreement on derivatives, Brussels, 23 July 2013 (available at: http://www.ebf-fbe.eu/uploads/EBF_003482%20-%20Press%20statement%20-%20EBF%20welcomes%20EU-US%20agreement%20on%20derivatives.pdf).

³ CFTC, Interpretive Guidance and Policy Statement Regarding Compliance With Certain Swap Regulations, 78 FR 45292, 26.07.2013, as well as the CFTC's 20 December 2013 substituted compliance determination concerning EU firms and various CFTC no-action letters and staff advisories, including those cited below.

⁴ CFTC Staff Advisory No. 13-69, Applicability of Transaction-Level Requirements to Activity in the United States, 14 November 2013 (available at: <http://www.cftc.gov/ucm/groups/public/@lrllettergeneral/documents/letter/13-69.pdf>).

⁵ The CFTC No-Action Letter (NAL) No. 14-89 of 27 June 2014 providing temporary relief for reporting requirements which conflict with local bank secrecy laws (available at: <http://www.cftc.gov/ucm/groups/public/@lrllettergeneral/documents/letter/14-89.pdf>), the CFTC NAL No. 13-45 of 11 July 2013 providing conditional recognition of EMIR risk-mitigation rules (available at <http://www.cftc.gov/ucm/groups/public/@lrllettergeneral/documents/letter/13-45.pdf>), the CFTC NAL No. 13-75 of 20 December 2013 providing for the temporary relief from certain requirements of Part 45 and Part 46 of the CFTC's Regulations (SDR Reporting) (available at: <http://www.cftc.gov/ucm/groups/public/@lrllettergeneral/documents/letter/13-75.pdf>) and CFTC NAL No. 14-46 of 9 April 2014 providing for no-action for EU-regulated trading platforms (available at: <http://www.cftc.gov/ucm/groups/public/@lrllettergeneral/documents/letter/14-46.pdf>).

⁶ Communiqué, Meeting of G20 Finance Ministers and Central Bank Governors, Cairns, 20-21 September 2014 (available at: https://www.g20.org/sites/default/files/g20_resources/library/Communique%20G20%20Finance%20Ministers%20and%20Central%20Bank%20Governors%20Cairns.pdf).