



**Americans for Financial Reform**  
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March 10, 2014

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Secretary of the Commission  
Commodity Futures Trading Commission  
Three Lafayette Center  
1155 21<sup>st</sup> Street NW  
Washington, DC 20581

Re: Request for Comment on Application of Commission Regulations to Swaps Between Non-U.S. Swap Dealers and Non-U.S. Counterparties Involving Personnel or Agents of the Non-U.S. Swap Dealers Located in the United States

Americans for Financial Reform (“AFR”) appreciates this opportunity to respond to the Commodity Futures Trading Commission’s (“CFTC”, or “Commission”) Request for Comment on Application of Commission Regulations to Swaps Between Non-U.S. Swap Dealers and Non-U.S. Counterparties Involving Personnel or Agents of The Non-U.S. Swap Dealers Located in the United States (the “Request for Comment”). AFR is a coalition of more than 200 national, state, and local groups who have come together to advocate for reform of the financial industry. Members of AFR include consumer, civil rights, investor, retiree, community, labor, faith based, and business groups.

In multiple previous comments, statements, and letters AFR has described the critical importance of cross-border jurisdiction and enforcement to the effectiveness of derivatives regulation.<sup>1</sup> Uniting these previous comments is a concern for the potential impact on the U.S. financial system and U.S. taxpayers if derivatives transactions by nominally foreign entities which in fact have a significant connection to the U.S. economy escape effective derivatives oversight. This is of course the same concern that motivated the clear statement in 7 USC 2(i), added by Section 722(d) of the Dodd Frank Act, that the CFTC has jurisdiction over transactions outside the United States when such activities “have a direct and significant connection with activities in, or effect on, commerce of the United States”.

In our previous comments, we urged the CFTC to interpret its jurisdiction to include all derivatives transactions undertaken by foreign subsidiaries of U.S. entities, as subsidiaries are generally dependent on explicit or implicit guarantees from the parent U.S. entity. Furthermore, the line between parent and subsidiary transactions is not always clear, as cash and transactions

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<sup>1</sup> See e.g. Americans for Financial Reform, “[AFR Letter to CFTC on Cross Border Issues](#)”, July 3, 2013; Americans for Financial Reform, “[AFR Comment to CFTC On Cross Border Applications of Certain Provisions of the Commodity Exchange Act, RIN 3038-AD 57](#)”, August 27, 2012.

are easily shifted between the parent entity and the global network of branches and subsidiaries.<sup>2</sup> The CFTC did not take this advice, and has instead laid out a cross-border regulatory framework in which substituted compliance is available for derivatives transactions between foreign subsidiaries of U.S. entities. Transactions between guaranteed foreign subsidiaries of U.S. entities and foreign entities not tied to a U.S. parent are completely exempted from Dodd-Frank (unless such foreign entities are registered swap dealers). Finally, transactions involving foreign subsidiaries of U.S. entities that are not explicitly guaranteed by the parent are also broadly exempted from Dodd-Frank in cases where such subsidiaries are neither conduits nor swap dealers.

A danger in this approach is the possibility that major U.S. financial firms will be able to move most of their derivatives transactions into nominally overseas subsidiaries, giving them a choice between substituted compliance regimes or in some cases permitting them to avoid oversight altogether.

If industry succeeds in exempting transactions by nominally foreign subsidiaries that are actually physically conducted within the United States from Dodd-Frank oversight then this danger will be well on its way to being realized. If the CFTC alters its November staff advisory to permit such an outcome, then major U.S. and global banks conducting transactions on the U.S. market will effectively have their choice of rules under which to operate. This could open the door to a damaging ‘race to the bottom’ in global derivatives oversight, or even to the emergence of regulatory havens where there is little oversight at all. This possibility is underlined by reports from market participants that major U.S. banks are seeking ways to remove the explicit guarantee from key foreign subsidiaries. This would permit such nominally foreign subsidiaries broad exemptions from Dodd-Frank while still allowing them to benefit from an implicit connection to a U.S. parent that is well understood by counterparties.

A choice to exempt transactions conducted in the United States from full Dodd-Frank oversight would also clash directly with the statutory language of 7 USC 2(i), which specifies that:

“The provisions of this Act relating to swaps that were enacted by the Wall Street Transparency and Accountability Act of 2010 (including any rule prescribed or regulation promulgated under that Act), shall not apply to activities **outside** the United States” [Emphasis added]

This clearly sets the statutory jurisdiction of CFTC rules to include all activities conducted inside the United States.

Commenters from U.S. and foreign banks have raised the possibility that transactions conducted outside the United States may have some minor, entirely incidental connection to the U.S. which would inappropriately trigger Dodd-Frank oversight. However, the November staff advisory specified that only the regular use of personnel or agents located in the U.S. to arrange, negotiate,

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<sup>2</sup> For descriptions of how such transfers functioned in the case of Lehman Brothers International and other complex global banks, see Herring, Richard and Jacopo Carmassi, "The Corporate Structure of International Financial Conglomerates: Complexity and Its Implications for Safety and Soundness," in The Oxford handbook of Banking, ed. by Allen Berger, 2010.

or execute a swap would trigger Dodd-Frank oversight. The advisory also characterized the type of activities that would trigger full U.S. regulatory coverage as “core, front-office activities of that SD’s dealing business”.<sup>3</sup> This would seem to rule out minor, entirely incidental, and occasional interaction with a U.S. office as triggering U.S. oversight.

Given the types of activities specified in the November staff advisory, any weakening of that advisory would open the door to regular and significant levels of swaps activities being performed within the U.S. by nominally foreign entities under foreign rules, or in some cases no rules at all. This is entirely at odds with the language of the Dodd-Frank Act and with the CFTC’s multi-year efforts to regulate the U.S. derivatives markets. It could mean that U.S. firms operating in the U.S. would face different rules for the same transactions as compared to competitor firms also operating in the very same market and location, perhaps literally next door, who had arranged to route transactions through a nominally foreign subsidiary.

Furthermore, it could have profound effects for other areas of CFTC jurisdiction as well. Such a decision would imply that the CEA generally may not apply to business performed in the U.S. by agents for a foreign entity. CFTC oversight of commodity futures trading generally could be threatened if foreign entities try to use this precedent to perform agency trades in U.S. commodity futures markets without complying with CFTC rules.

We thus urge the CFTC to avoid any weakening of the November staff advisory. Below, we respond to specific questions in the Request for Comment.

1. *The Commission invites comment on whether the Commission should adopt the Staff Advisory as Commission policy, in whole or in part.*

For the reasons laid out above, we urge the Commission to adopt the entire November Staff Advisory as Commission policy.

2. *The Commission invites commenters to provide their views on whether transactional requirements should apply to Covered Transactions with non-U.S. persons who are not guaranteed or conduit affiliates of U.S. persons.*

As AFR has stated in previous comments and letters, we are concerned that the complete exemption of transactions with non-U.S. persons who are not guaranteed or conduit affiliates of U.S. persons could undermine the application of Dodd-Frank requirements to the full range of transactions that have a direct and significant connection with commerce of the United States. This could occur for two reasons.

First, transactions between guaranteed foreign subsidiaries of U.S. banks and truly foreign entities (who are not affiliated with any U.S. entity) do pose credit risks to the U.S. bank guaranteeing one side of the transaction. This argues for the application of at least clearing requirements to such transactions.

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<sup>3</sup> Commodity Futures Trading Commission, Division of Swap Dealer and Intermediary Oversight, “[CFTC Staff Advisory No. 13-69](#)”, November 14, 2013.

Second, U.S. entities can set up foreign subsidiaries that are not explicitly guaranteed and do not rise to the level of being a regular conduit, but nevertheless are seen by the market as having an implicit guarantee from the parent. This occurred multiple times during the financial crisis.<sup>4</sup> As stated above, we have heard informal discussion from market participants of attempts by U.S. banks to set up such subsidiaries today. In previous comments we have urged the CFTC to address this issue by imposing a rebuttable presumption that foreign subsidiaries of U.S. entities are guaranteed by the parent. This presumption could be rebutted by documented evidence that market terms for transactions with the subsidiary reflected the resources of the subsidiary and not the parent. In any case, the presence of a guarantee should be determined by examining the market terms available to the subsidiary for transactions, rather than simply the presence of a written guarantee.

All of the risks above would of course be multiplied greatly if the Commission allowed transactions involving a subsidiary of a U.S. bank to be performed from U.S. soil without applying any transactional requirements. Such a decision would make it far more convenient for U.S. banks or foreign banks with a major role in the U.S. markets to structure transactions that avoid Dodd-Frank transactional requirements.

3. *The Commission invites comment on whether there should be any differentiation in treatment of swaps with non-U.S. counterparties depending on the nature of the SD (i.e. whether it is a guaranteed affiliate or a conduit affiliate of a U.S. person).*

As we have made clear throughout this comment, we generally urge the application of Dodd-Frank requirements to swaps conducted in the U.S. that involve non-U.S. counterparties. However, if any differentiation is made it is obviously critical to ensure that swap dealers who are nominally foreign subsidiaries of U.S. entities are fully covered by Dodd-Frank rules. These would generally be the swap dealers directly connected to major U.S. banks and other systemically important financial institutions, many of whom received public support during the financial crisis. To exempt such swap dealers from Dodd-Frank derivatives regulation would run completely counter to public and Congressional expectations and intentions in instituting regulation of the U.S. swaps markets.

4. *To the extent that a non-U.S. SD must comply with the transactional requirements when entering a Covered Transaction, should the non-U.S. SD be able to rely on a substituted compliance program for purposes of complying with the relevant transactional requirements?*

In previous comments, AFR has underlined the importance of ensuring that permission for substituted compliance is granted only to rule sets that are fully and completely equivalent to U.S. rules, both in their terms and their enforcement. While we are encouraged by some commitments the CFTC has made in this area, the ability to ensure true equivalence for

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<sup>4</sup> One example of such implicit guarantees was Bear Stearns' support for two subprime credit hedge funds incorporated in the Cayman Islands in summer 2007. Bear Stearns took this step for reputational reasons, despite the lack of any formal or explicit guarantee. Another example was the large-scale support provided by major banks during 2008 for various special purpose vehicles, also made necessary for reputational reasons in the absence of any explicit guarantee.

substituted compliance has not yet been demonstrated by any market experience even for firms operating in foreign countries. The Commission has also stated that foreign rules need not be identical to U.S. rules to qualify for substituted compliance, and indeed it is unlikely that they will be so. Permitting substituted compliance for transactions conducted in the U.S. thus implies that firms will be operating under different rules within the United States, within the same markets, and possibly within the same building. This could create issues for enforcement and oversight that can easily be avoided simply through the common-sense requirement that all firms performing derivatives transactions in the United States operate under the same rules. We would thus oppose any substituted compliance for Covered Transactions at this time.

To the extent that any substituted compliance is granted, we would favor limiting such substituted compliance to U.S. subsidiaries of foreign parent banks operating in the United States. It should not be available for nominally foreign subsidiaries of U.S. banks operating in the U.S. The potential for U.S. taxpayer exposure to credit risks taken by a U.S. bank (including through a foreign subsidiary guaranteed explicitly or implicitly) would be greater than the risk for a U.S. subsidiary of a foreign bank. However, such exposure is not completely absent in the case of foreign banking organizations, as demonstrated by the Federal Reserve requirement that an intermediate holding company structure be created for such foreign banking organizations in order to protect the U.S. financial system.<sup>5</sup>

5. *The Commission invites comment on the meaning of “regularly” in the phrase “persons regularly arranging, negotiating or executing swaps for or on behalf of an SD” and whether such persons are performing core, front-office activities of that SD’s swap dealing businesses.*

AFR believes that arranging, negotiating, or executing swaps are core front office activities of swap dealing. These activities would appear to be involved in structuring the swaps product to be sold, actually selling the product, and in trading swaps. These are all activities which are economically central to the business of swaps dealing. The specification of ‘arranging, negotiating, or executing’ would appear to exclude purely clerical and incidental functions such as notating or recording the sale of a swap for consolidated risk management or bookkeeping purposes.

We would favor tying the definition of ‘regularly’ to an expectation by employees of the swap dealer that personnel located in the U.S. are available on request to engage in the core front office activities of arranging, negotiating, and executing swaps, or to a corresponding expectation by U.S. personnel that they can regularly draw on employees of the nominally foreign swap dealer to conduct core front office transactions for a swap that U.S. employees intend to arrange, negotiate, or execute.

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<sup>5</sup> Federal Reserve System, 12 CFR Part 252, “[Enhanced Prudential Standards for Bank Holding Companies and Foreign Banking Organizations](#)”, Final Rule, RIN 7100-AD86.

Thank you for the opportunity to comment on this Request for Comment. Should you have any questions, please contact Marcus Stanley, AFR's Policy Director, at 202-466-3672 or [marcus@ourfinancialsecurity.org](mailto:marcus@ourfinancialsecurity.org).

**Following are the partners of Americans for Financial Reform.**

*All the organizations support the overall principles of AFR and are working for an accountable, fair and secure financial system. Not all of these organizations work on all of the issues covered by the coalition or have signed on to every statement.*

- AARP
- A New Way Forward
- AFL-CIO
- AFSCME
- Alliance For Justice
- American Income Life Insurance
- American Sustainable Business Council
- Americans for Democratic Action, Inc
- Americans United for Change
- Campaign for America's Future
- Campaign Money
- Center for Digital Democracy
- Center for Economic and Policy Research
- Center for Economic Progress
- Center for Media and Democracy
- Center for Responsible Lending
- Center for Justice and Democracy
- Center of Concern
- Center for Effective Government
- Change to Win
- Clean Yield Asset Management
- Coastal Enterprises Inc.
- Color of Change
- Common Cause
- Communications Workers of America
- Community Development Transportation Lending Services
- Consumer Action
- Consumer Association Council
- Consumers for Auto Safety and Reliability
- Consumer Federation of America
- Consumer Watchdog
- Consumers Union
- Corporation for Enterprise Development
- CREDO Mobile
- CTW Investment Group
- Demos
- Economic Policy Institute
- Essential Action

- Green America
- Greenlining Institute
- Good Business International
- HNMA Funding Company
- Home Actions
- Housing Counseling Services
- Home Defender's League
- Information Press
- Institute for Agriculture and Trade Policy
- Institute for Global Communications
- Institute for Policy Studies: Global Economy Project
- International Brotherhood of Teamsters
- Institute of Women's Policy Research
- Krull & Company
- Laborers' International Union of North America
- Lawyers' Committee for Civil Rights Under Law
- Main Street Alliance
- Move On
- NAACP
- NASCAT
- National Association of Consumer Advocates
- National Association of Neighborhoods
- National Community Reinvestment Coalition
- National Consumer Law Center (on behalf of its low-income clients)
- National Consumers League
- National Council of La Raza
- National Council of Women's Organizations
- National Fair Housing Alliance
- National Federation of Community Development Credit Unions
- National Housing Resource Center
- National Housing Trust
- National Housing Trust Community Development Fund
- National NeighborWorks Association
- National Nurses United
- National People's Action
- National Urban League
- Next Step
- OpenTheGovernment.org
- Opportunity Finance Network
- Partners for the Common Good
- PICO National Network
- Progress Now Action
- Progressive States Network

- Poverty and Race Research Action Council
- Public Citizen
- Sargent Shriver Center on Poverty Law
- SEIU
- State Voices
- Taxpayer's for Common Sense
- The Association for Housing and Neighborhood Development
- The Fuel Savers Club
- The Leadership Conference on Civil and Human Rights
- The Seminal
- TICAS
- U.S. Public Interest Research Group
- UNITE HERE
- United Food and Commercial Workers
- United States Student Association
- USAction
- Veris Wealth Partners
- Western States Center
- We the People Now
- Woodstock Institute
- World Privacy Forum
- UNET
- Union Plus
- Unitarian Universalist for a Just Economic Community

***List of State and Local Partners***

- Alaska PIRG
- Arizona PIRG
- Arizona Advocacy Network
- Arizonans For Responsible Lending
- Association for Neighborhood and Housing Development NY
- Audubon Partnership for Economic Development LDC, New York NY
- BAC Funding Consortium Inc., Miami FL
- Beech Capital Venture Corporation, Philadelphia PA
- California PIRG
- California Reinvestment Coalition
- Century Housing Corporation, Culver City CA
- CHANGER NY
- Chautauqua Home Rehabilitation and Improvement Corporation (NY)
- Chicago Community Loan Fund, Chicago IL
- Chicago Community Ventures, Chicago IL
- Chicago Consumer Coalition
- Citizen Potawatomi CDC, Shawnee OK

- Colorado PIRG
- Coalition on Homeless Housing in Ohio
- Community Capital Fund, Bridgeport CT
- Community Capital of Maryland, Baltimore MD
- Community Development Financial Institution of the Tohono O'odham Nation, Sells AZ
- Community Redevelopment Loan and Investment Fund, Atlanta GA
- Community Reinvestment Association of North Carolina
- Community Resource Group, Fayetteville A
- Connecticut PIRG
- Consumer Assistance Council
- Cooper Square Committee (NYC)
- Cooperative Fund of New England, Wilmington NC
- Corporacion de Desarrollo Economico de Ceiba, Ceiba PR
- Delta Foundation, Inc., Greenville MS
- Economic Opportunity Fund (EOF), Philadelphia PA
- Empire Justice Center NY
- Empowering and Strengthening Ohio's People (ESOP), Cleveland OH
- Enterprises, Inc., Berea KY
- Fair Housing Contact Service OH
- Federation of Appalachian Housing
- Fitness and Praise Youth Development, Inc., Baton Rouge LA
- Florida Consumer Action Network
- Florida PIRG
- Funding Partners for Housing Solutions, Ft. Collins CO
- Georgia PIRG
- Grow Iowa Foundation, Greenfield IA
- Homewise, Inc., Santa Fe NM
- Idaho Nevada CDFI, Pocatello ID
- Idaho Chapter, National Association of Social Workers
- Illinois PIRG
- Impact Capital, Seattle WA
- Indiana PIRG
- Iowa PIRG
- Iowa Citizens for Community Improvement
- JobStart Chautauqua, Inc., Mayville NY
- La Casa Federal Credit Union, Newark NJ
- Low Income Investment Fund, San Francisco CA
- Long Island Housing Services NY
- MaineStream Finance, Bangor ME
- Maryland PIRG
- Massachusetts Consumers' Coalition
- MASSPIRG
- Massachusetts Fair Housing Center

- Michigan PIRG
- Midland Community Development Corporation, Midland TX
- Midwest Minnesota Community Development Corporation, Detroit Lakes MN
- Mile High Community Loan Fund, Denver CO
- Missouri PIRG
- Mortgage Recovery Service Center of L.A.
- Montana Community Development Corporation, Missoula MT
- Montana PIRG
- Neighborhood Economic Development Advocacy Project
- New Hampshire PIRG
- New Jersey Community Capital, Trenton NJ
- New Jersey Citizen Action
- New Jersey PIRG
- New Mexico PIRG
- New York PIRG
- New York City Aids Housing Network
- New Yorkers for Responsible Lending
- NOAH Community Development Fund, Inc., Boston MA
- Nonprofit Finance Fund, New York NY
- Nonprofits Assistance Fund, Minneapolis M
- North Carolina PIRG
- Northside Community Development Fund, Pittsburgh PA
- Ohio Capital Corporation for Housing, Columbus OH
- Ohio PIRG
- OligarchyUSA
- Oregon State PIRG
- Our Oregon
- PennPIRG
- Piedmont Housing Alliance, Charlottesville VA
- Michigan PIRG
- Rocky Mountain Peace and Justice Center, CO
- Rhode Island PIRG
- Rural Community Assistance Corporation, West Sacramento CA
- Rural Organizing Project OR
- San Francisco Municipal Transportation Authority
- Seattle Economic Development Fund
- Community Capital Development
- TexPIRG
- The Fair Housing Council of Central New York
- The Loan Fund, Albuquerque NM
- Third Reconstruction Institute NC
- Vermont PIRG
- Village Capital Corporation, Cleveland OH

- Virginia Citizens Consumer Council
- Virginia Poverty Law Center
- War on Poverty - Florida
- WashPIRG
- Westchester Residential Opportunities Inc.
- Wigamig Owners Loan Fund, Inc., Lac du Flambeau WI
- WISPIRG

***Small Businesses***

- Blu
- Bowden-Gill Environmental
- Community MedPAC
- Diversified Environmental Planning
- Hayden & Craig, PLLC
- Mid City Animal Hospital, Pheonix AZ
- UNET