

## Securities Regulation Daily Wrap Up, DERIVATIVES—CFTC staff issues guidance on cross-border derivatives transactions, (Nov. 15, 2013)

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By Jim Hamilton, J.D., LL.M.

The CFTC staff issued guidance on cross-border derivatives transactions in response to inquiries from swap market participants. The Division of Swap Dealer and Intermediary Oversight said that substituted compliance should be available for the transaction-level requirements with respect to swaps between a non-U.S. swaps dealer and a non-U.S. person, or should not apply at all, depending on whether or not such non-U.S. person is a guaranteed affiliate or affiliate conduit of a U.S. person.

Under such circumstances, the staff guidance said that the Commission intended substituted compliance to be available, or transaction-level requirements to not apply, where the activities of the non-U.S. swaps dealer takes place outside the United States. In this regard, pursuant to the Dodd-Frank Act, the CFTC has a strong supervisory interest in swap dealing activities that occur within the United States, regardless of the status of the counterparties.

**Substituted compliance.** The heart of the CFTC's cross-border regulation of derivatives transactions is the doctrine of substituted compliance under which the CFTC will defer to comparable and comprehensive foreign regulations.

In the Division's view, persons regularly arranging, negotiating, or executing swaps for, or on behalf of, a swap dealer are performing core, front-office activities of that firm's dealing business. Thus, a non-U.S. swap dealer, whether an affiliate or not of a U.S. person, regularly using personnel or agents located in the U.S. to arrange, negotiate, or execute a swap with a non-U.S. person generally would be required to comply with the transaction-level requirements. For the avoidance of doubt, the Division's view would also apply to a swap between a non-U.S. swap dealer and a non-U.S. person booked in a non-U.S. branch of the non-U.S. swap dealer if the non-U.S. swap dealer is using personnel or agents located in the U.S. to arrange, negotiate, or execute such swap.

**Congressional reaction.** Rep. Jeb Hensarling (R-Tex.), Chair of the House Financial Services Committee said that the CFTC guidance injects a level of uncertainty into the cross-border regulation of derivatives. In a sudden and unexpected change, the CFTC staff decided that swaps transactions that had been permissible Thursday afternoon would not be permissible on Friday morning.

Similarly, Rep. Frank Lucas (R-Okla.), Chair of the Agriculture Committee, is concerned that the staff guidance has created confusion and is disrupting the U.S. swaps markets. Regulations that market participants thought were in place changed overnight without warning or consultation. Chairman Lucas urged the CFTC to immediately issue a public statement explaining to market participants when it will enforce its guidance. Regulating without regard for how markets function is irresponsible, said the Chair, and harms U.S. credibility with the international business community.

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