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CFTC Proposes Cross-Border Guidance and Exemptive Order

On June 29, the CFTC released proposed interpretive guidance regarding the cross-border impact of the swap-related provisions of Title VII of the Dodd-Frank Act.[1] The CFTC also released a proposed exemptive order that would provide non-U.S. registered swap dealers ("**SDs**") and major swap participants ("**MSPs**") with temporary conditional exemptions from many swap-related Title VII requirements for one year, and permit SDs and MSPs that are U.S. persons (as defined below) to defer compliance with some requirements until January 2013.[2] Comments on the proposed interpretive guidance are due 45 days after it is published in the Federal Register and comments on the proposed exemptive order are due 30 days after it is published in the Federal Register, both of which are expected shortly.

The Proposed Guidance

The proposed guidance interprets the cross-border reach of Title VII's swap provisions. The main impacts would be as follows:

- **U.S. persons** that are registered SDs and MSPs would be subject to all "entity-level" requirements (such as capital, internal business conduct, chief compliance officer and reporting to swap data repositories) and "transaction-level" requirements (such as margin, clearing and external business conduct).
- **Non-U.S. persons**:
  - would not be required to count swaps with non-U.S. persons or non-U.S. branches of U.S. SDs when determining whether they must register with the CFTC as an SD (unless the dealer's obligations under those swaps are guaranteed by a U.S. person).
  - need not count the swap dealing transactions of their U.S. affiliates when determining whether the *de minimis* threshold for SD registration is met. However, they would be required to aggregate their swap dealing activity with the U.S.-facing swap dealing activity of their non-U.S. affiliates under common control. Moreover, *all* swap dealing activity of non-U.S. affiliates under common control would be counted if such affiliates' obligations are guaranteed by a U.S. person.
  - that are SDs or MSPs would not be required to comply with the CFTC's transaction-level requirements when dealing with non-U.S. persons, except where there is a guarantee by a U.S. person or where a swap counterparty is a non-U.S. conduit affiliate of a U.S. person.
  - that are SDs or MSPs would be permitted to substitute non-U.S. rules for the CFTC's entity-level requirements, with substituted compliance for SDR reporting allowed only if the CFTC is provided direct access to swap data.
  - that are SDs or MSPs may comply with home-country law under the "substituted compliance" regime for those swaps with non-US persons guaranteed by U.S. persons and non-U.S. conduit affiliates.

[1] CFTC Proposed Interpretive Guidance and Policy Statement Regarding Cross-Border Application of Certain Swaps Provisions of the Commodity Exchange Act, available **here.**

[2] CFTC Proposed Exemptive Order Regarding Compliance with Certain Swap Regulations, available **here**.

- **Non-U.S. branches** of registered SDs and MSPs that are U.S. persons generally would be subject to the same requirements as the U.S. head office. However, with respect to non-U.S. counterparties, such branches would not need to comply with external business conduct rules, and may apply to substitute non-U.S. rules for other transaction-level requirements. Branches may even comply with non-U.S. rules that are not determined to be comparable to U.S. rules if their activity is below a *de minimis* level.
- **Non-SDs and non-MSPs** must generally comply with reporting, recordkeeping, clearing and execution requirements when at least one counterparty is a U.S. person, and may comply with non-U.S. rules, instead of U.S. rules, regarding swap data repository ("**SDR**") reporting and swap data recordkeeping so long as the CFTC has direct access to the data stored at the non-U.S. trade repository. Transactions between non-U.S. persons that are not SDs or MSPs would be exempt from Title VII requirements other than large trader reporting.

The Proposed Order

The proposed exemptive order would provide market participants with conditional temporary relief from certain Title VII requirements applicable to CFTC-regulated swaps and registered entities. In particular, the proposed order would allow:

- **U.S. persons** that are registered SDs and MSPs to delay, until January 1, 2013, compliance with entity-level requirements other than swap data recordkeeping, SDR reporting and large trader reporting;
- **Non-U.S. persons** that are registered SDs and MSPs to delay, for one year from the publication of the proposed order in the Federal Register, compliance with entity-level requirements, subject to exceptions relating to the SDR reporting and large trader reporting requirements; and
- **Non-U.S. persons** that are registered SDs and MSPs, as well as non-U.S. branches of registered SDs and MSPs that are U.S. persons, to delay compliance with Title VII transaction-level requirements with non-U.S. counterparties, subject to compliance with non-U.S. regulation.

In order to benefit from the exemptive order, SDs and MSPs would be required to file an application for registration with the National Futures Association by the date on which registration is required. Registered SDs and MSPs that are not U.S. persons and non-U.S. branches of U.S. persons that are SDs or MSPs must submit a "compliance plan" to the CFTC within 60 days of applying for registration as an SD or MSP.

"U.S. Person" Defined

For the purposes of both the proposed guidance and the proposed order, "U.S. person" is defined as:

- Any natural person who is a resident of the U.S.;
- Any corporation, partnership, LLC, business or other trust, association, joint-stock company, fund, or any form of enterprise similar to any of the forgoing that is either: (i) organized or incorporated under the laws of the U.S. or has its principal place of business in the U.S., or (ii) in which the direct or indirect owners thereof are responsible for the liabilities of such entity and one or more of such owners is a U.S. person;
- Any individual account (discretionary or not) where the beneficial owner is a U.S. person;
- Any commodity pool, pooled account, or collective investment vehicle (whether or not it is organized or incorporated in the U.S.) of which a majority ownership is held, directly or indirectly, by a U.S. person(s);
- Any commodity pool, pooled account, or collective investment vehicle the operator of which would be required to register as a commodity pool operator under the Commodity Exchange Act;

- A pension plan for the employees, officers, or principals of a legal entity with its principal place of business inside the United States; and
- An estate or trust, the income of which is subject to U.S. income tax, regardless of source.

Uncertainties Remain

While the proposed guidance and order provide increased certainty and relief to many swap market participants and help address many short-run compliance issues, the complexity of the proposals raises a number of interpretive questions.

If you have any questions regarding the matters covered in this publication, please contact any of the lawyers listed below or your regular Davis Polk contact.

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