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OTC Derivatives Regulation and Extraterritoriality III

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Comprehensive EU and US measures to regulate over the counter ("OTC") derivatives are progressing closer to full implementation. EMIR[1] entered into force in the EU on 16 August 2012, with the clearing obligation expected to take effect in 2013. In the US, the Dodd-Frank Act requirements are being implemented, with dealer registration commencing as of year-end 2012 and mandatory clearing to begin in March 2013. Both measures by their terms have some degree of extraterritorial application. The CFTC has proposed guidance on the Dodd-Frank Act's extraterritorial scope and granted temporary exemptive relief from the application of some requirements to non-US persons. In the absence of agreement between the US and EU regulators, however, extraterritoriality has the potential to cause intractable and irreconcilable conflicts for the derivatives industry. This note sets out certain situations in which extraterritoriality is likely to result in such conflicts.

[1] Regulation 648/2012.

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Introduction

In the wake of the financial crisis, G20 leaders committed to the clearing of all standardized OTC derivatives contracts by the end of 2012, among other derivatives reforms. In the US, Title VII of the Dodd Frank Wall Street Reform and Consumer Protection Act ("**Dodd-Frank**") and in the EU, the EU Regulation on OTC derivatives, central counterparties and trade repositories ("**EMIR**") both seek to implement certain of these commitments. Some requirements and new CFTC regulations have already taken effect or are expected to take effect in the first quarter of 2013. US regulators have yet to adopt final rules and regulations in a number of areas, however. EMIR entered into force on 16 August 2012.[2] On 19 December 2012, the European Commission adopted six regulatory technical standards (the "**regulatory technical standards**") relating to various provisions of EMIR, and three implementing technical standards (the "**implementing technical standards**," together with the regulatory technical standards, the "**adopted technical standards**"). The draft technical standards submitted by the European Securities and Markets Authority ("**ESMA**") and the European Banking Authority were accepted without modification.[3] The adopted technical standards could start to apply in mid-February 2013 (although in practice the application of the adopted technical standards is dependent upon a number of factors, including the entry into effect of the clearing obligation and authorization of central counterparties ("**CCPs**") and trade repositories).[4] The implementing technical standards[5] were published in the EU's Official Journal on 21 December 2012 and will enter into force on 10 January 2013. However, since their

[2] This note discusses current versions of certain rule proposals under Dodd-Frank and technical standards under EMIR. The final, definitive versions of the Dodd-Frank rules and EMIR technical standards, which will affect how the regimes eventually operate, may differ from the versions discussed in this note.

[3] ESMA, Final Report, Draft technical standards under the Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC Derivatives, CCPs and Trade Repositories, 27 September 2012.

[4] The European Parliament and the Council now have one month from the adoption of the regulatory technical standards to object (which may be extended by another month at their discretion). The regulatory technical standards are expected to be published in the EU's Official Journal around 10 days after the expiry of the objection period and will enter into force on the twentieth day following publication.

[5] (1) Commission Implementing Regulation (1247/2012) of 19 December 2012 laying down implementing technical standards with regard to the format and frequency of trade reports to trade repositories according to Regulation (EU) No 648/2012 of the European Parliament and of the Council on OTC derivatives, central counterparties and trade repositories; (2) Commission Implementing Regulation (1248/2012) of 19 December 2012 laying down implementing technical standards with regard to the format of applications for registration of trade repositories according to Regulation (EU) No 648/2012 of the European Parliament and of the Council on OTC derivatives, central counterparties and trade repositories; (3) Commission Implementing Regulation (1249/2012) of 19 December 2012 laying down implementing technical standards with regard to the format of the records to be maintained by central counterparties according to Regulation (EU) No 648/2012 of the European Parliament and of the Council on OTC derivatives, central counterparties and trade repositories.

provisions complement those contained in the regulatory technical standards, they will not take effect until the associated regulatory technical standards enter into force.

Unlike in the US, many aspects of OTC derivatives trading, advice and dealing are already regulated in Europe, so the focus of EMIR is on clearing. Certain EU reforms in relation to OTC derivatives, including an exchange trading requirement for standardized OTC derivatives, will be implemented though amendments to the Markets in Financial Instruments Directive (Directive 2004/39/EC, "**MiFID**"), generally referred to as MiFID II, including a new regulation made under MiFID.[6]

Both Dodd-Frank and EMIR have some extraterritorial effect, as well as different approaches in certain other key areas which have the potential to give rise to conflicts.

Dodd-Frank

The Dodd-Frank requirements relating to swaps regulated by the Commodity Futures Trading Commission ("**CFTC**") will apply to activities outside the United States which either: (a) have a direct and significant connection with activities in, or effect on, commerce in the United States; or (b) contravene CFTC rules intended to prevent evasion of US requirements.[7] Similarly, the requirements relating to security based swaps regulated by the Securities and Exchange Commission ("**SEC**") will apply to security-based swaps entered into outside the US where these contravene SEC rules intended to prevent the evasion of US requirements.[8] On 29 June 2012, the CFTC issued proposed interpretive guidance regarding the cross border application of key requirements under Title VII of Dodd-Frank.[9] Under the CFTC's proposed approach, non US institutions engaged in derivatives transactions with US persons (or in certain cases non-US persons guaranteed by US persons) would be subject to US registration and regulatory requirements, although, in some cases, the CFTC would permit "substituted compliance" with home country requirements in lieu of compliance with US rules.[10] The CFTC's guidance has been the subject of substantial comment from non-US and international institutions and governments. The SEC has not yet issued any further guidance as to the extraterritorial application of the security-based swap requirements under Dodd-Frank.

Although the CFTC has not finalized the proposed interpretive guidance, on December 21, 2012, the CFTC issued an exemptive order addressing certain extraterritorial effects for the period until July 13, 2013 (the "**Cross-Border**

[6] The MiFID II legislative proposals were published on 20 October 2011. If you wish to review further information on MiFID II, our prior client publication is available at http://www.shearman.com/files/Publication/120c86fd-417f-4045-92a8-b071e80931a0/Presentation/PublicationAttachment/49b7a19e-4a4e-4c95-8507-6f757e3565f2/FIA-102011-A-Changing-Landscape-The-MiFID-II-Legislative-Proposal.pdf.

[7] Dodd-Frank, section 722(d); Commodity Exchange Act ("CEA") Section 2(i).

[8] Dodd-Frank, section 772(b); Securities Exchange Act of 1934 ("Exchange Act") Section 30(c).

[9] Cross Border Application of Certain Swaps Provisions of the Commodity Exchange Act, 77 Fed. Reg. 41214 (July 12, 2012). If you wish to review further information on the cross-border application of key Dodd-Frank requirements, you may refer to our prior publication available at http://www.shearman.com/files/Publication/eb0a65a3-e73e-4ef2-badb-a1941b0484d7/Presentation/PublicationAttachment/6ed47d5c-4fc5-493e-8ce3-0449f18c4c19/Cross-Border-Application-of-Swaps-Provisions-of-the-Dodd-Frank-Act-DR-071812.pdf.

[10] As part of the interpretive guidance as proposed to be modified in the Cross-Border Exemptive Order, the CFTC has proposed a broad definition of US person that would include some investment vehicles organized outside the United States that are majority owned (directly or indirectly) by US persons.

Exemptive Order").[11] Among other matters, the Cross-Border Exemptive Order adopts a temporary, more limited definition of US person, clarifies certain aspects of the *de minimis* exception from swap dealer and major swap participant registration as it applies to non-US persons, delays implementation of so-called "entity-level requirements" for registered non-US swap dealers and MSPs and allows non-US dealers and non-US branches of US dealers to comply with local transaction-specific requirements for trades with non-US persons instead of CFTC transaction-level requirements. In adopting this temporary relief, the CFTC indicated it is continuing to review cross-border implementation issues, including through discussions with other regulators, and expects to provide further guidance in the future.

EMIR

The EMIR clearing obligation applies generally to transactions to which two EU entities are party. The clearing obligation also apples to transactions between a financial counterparty (or a non-financial counterparty exceeding the clearing threshold) and a non-EU entity that would be subject to the clearing obligation if the counterparty were established in the EU. Finally, for transactions between two non-EU entities, the clearing obligations will apply "*provided that the contract has a direct, substantial and foreseeable effect within the EU or where such an obligation is necessary or appropriate to prevent the evasion of any provisions of*" EMIR.[12] The technical standards specifying the contracts that have a direct, substantial and foreseeable effect within the EU are also still under review.[13] The impact of the potentially wide scope of this definition is mitigated to some extent by a provision of EMIR intended to avoid duplicative or conflicting rules. Where one party to the transaction is established outside the EU and is subject to a regime declared "equivalent" to that under EMIR, the party will be deemed to comply with the EMIR clearing and reporting obligations.[14] This is conditional upon the European Commission adopting an implementing act on the equivalence of the non-EU regime. To date, no such implementing acts have been adopted. In addition, there is a mechanism for recognizing third-country CCPs for purposes of satisfying the clearing obligation. The adopted technical standards set out aspects of the recognition regime for third country CCPs,[15] including the information to be provided to ESMA in applications for recognition of a CCP in a third country.

Whether branches of third country entities would be considered to be "established" in the EU is key to defining the scope of the clearing obligation. The provisions of EMIR applicable to CCPs are silent as to territorial scope, but key to how new legislation affects all market participants given that the clearing obligation may only be satisfied through use of an

[11] Final Exemptive Order Regarding Compliance with Certain Swap Regulations; Further Proposed Guidance, 78 Fed. Reg. 858 (Jan. 7, 2013). If you wish to review further information on the Cross-Border Exemptive Order, you may refer to our prior publications, available at http://www.shearman.com/files/Publication/3e12a8c1-d987-47ae-aee1-514c809cef1c/Presentation/PublicationAttachment/3b2c9b49-5269-43f5-8fb8-1c5061ea9ce4/CFTC-Issues-Order-Temporarily-Limiting-Cross-Border-Application-of-Swaps-Provisions-of-Dod.pdf and http://www.shearman.com/files/Publication/71555774-9d1b-41e1-9a7b-008dd84f1516/Presentation/PublicationAttachment/4798f2a5-4454-435d-8e8e-14ca3a3e1ac3/CFTC-Defers-Compliance-Dates-for-Business-Conduct-and-Documentation-Requirements-until-Mid.pdf.

[12] EMIR, Article 4(a)(iv) and (v).

[13] European Commission, EMIR: Frequently Asked Questions published on 14 November 2012.

[14] EMIR, Article 13.

[15] EMIR, Article 25.

approved CCP. Non-EU CCPs are prohibited from providing clearing services to entities established in the EU unless they are recognized by ESMA. Third-country branches of EU clearing members are considered to be established in the EU for these purposes, and therefore the relevant third-country CCPs must be recognized under EMIR in order to provide services to those branches.[16] By contrast, third-country CCPs do not need to be recognized under EMIR in order to provide services to subsidiaries of EU firms incorporated in such third country.[17] There is some limited grandfathering for national regimes in EMIR, such as the UK's recognized overseas clearing house ("**ROCH**") regime. We also understand from the FSA that both UK and EU regulators consider that the UK "overseas persons" exclusion regime also comprises a form of authorization or recognition for the purposes of grandfathering CCPs. It is to be hoped that the designation of acceptable non EU-CCPs can be swift given the present market uncertainties.

The adopted technical standards now provide some clarity on the initial level at which the EMIR clearing threshold for non financial counterparties will be set, with a view to tailoring this further as more data becomes available. The current thresholds are based on different notional amounts per asset class, with broadly defined asset classes: credit derivatives (EUR 1 billion), equity derivatives (EUR 1 billion), interest rate (EUR 3 billion), foreign exchange (EUR 3 billion) and commodity and other OTC derivatives not falling within any other category (EUR 3 billion). When one threshold is reached, the non-financial counterparty will become subject to the clearing obligation in respect of all asset classes.

Areas of Conflict

Dodd-Frank and EMIR are not fully aligned and differ in various respects. The contracts subject to mandatory clearing, application of the clearing obligation to non-financial institutions, registration requirements for dealers, rules on margin and collateral, registration requirements for clearing houses, exchange trading and reporting requirements are areas of potentially significant difference. The clearing obligation may potentially emerge as less of a concern because the majority of European clearing houses are already registered in the US as DCOs. Also, a number of US clearing houses have ROCH status in the UK and will benefit from limited grandfathering under EMIR. There may, however, be implementation time differences in terms of the scope of the clearing obligation in different parts of the world, which could potentially lead to counterparties using legal entities in particular jurisdictions to avoid clearing, if there is some advantage from doing so in terms of compliance, documentation or cost. To ensure that CCPs active in the EU can continue to provide services in the transitional period between the entry into force of the adopted technical standards and the recognition of the relevant third-country CCP under EMIR, those CCPs will be permitted to operate subject to existing national regimes until they have been recognized under EMIR.[18] EMIR's provisions seeking to avoid duplicative or conflicting rules and the CFTC's proposal for "substituted compliance" are helpful, but regulators on both sides of the Atlantic still need to take formal steps to avoid market fragmentation.[19]

[16] See further ISDA letter dated 30 July 2012 on concerns regarding the application of Article 25(1) EMIR Prohibition against non-EU CCPs providing clearing services in the EU.

[17] See European Commission's Frequently Asked Questions, published on 14 November 2012.

[18] EMIR, Article 89(4); see also European Commission's Frequently Asked Questions, published on 14 November 2012.

[19] See Joint Press Statement of Leaders on Operating Principles and Areas of Exploration in the Regulation of the Cross-border OTC Derivatives Market, 4 December 2012.

This article is intended to identify certain practical issues that may arise from overlapping US and EU regulatory jurisdiction.

A glossary of terms not previously defined is set out on page 12 below.

SCENARIO	APPLICABLE DODD-FRANK REQUIREMENTS	APPLICABLE EUROPEAN REQUIREMENTS	ASSOCIATED ISSUES
A non-US bank with a branch in the US operates a global booking model (whereby all swaps or security-based swaps executed by the bank or its affiliates are entered into by the bank's home state entity).	The non-US bank may be required to register as a swap dealer or security-based swap dealer and thereby become subject to CFTC/SEC conduct of business regulation and prudential regulation, including capital and margin requirements. Under the CFTC's Cross-Border Exemptive Order, if registration is required, the non-US bank could defer compliance with certain Entity-Level Requirements (such as capital requirements).[20] For other, Transaction-Level Requirements, the US rules would apply to transactions with US persons. Under the Cross-Border Exemptive Order, the Transaction-Level Requirements would generally not apply to transactions with non-US persons, except as required under local law. Following the expiration of the Cross-Border Exemptive Order, under the CFTC's proposed guidance, substituted compliance with comparable home country rules may be permitted for Entity-Level Requirements and certain Transaction-Level Requirements for transactions with non-US persons guaranteed by US persons.	If the foreign bank is established in the EU, it is likely that it will be subject to licensing under the various EU financial services directives such as the MiFID or the Banking Consolidation Directive (Directive 2006/48/EC). These directives, together with the Capital Adequacy Directive (Directive 93/6/EEC, as amended by Directive 98/31/EEC), impose conduct of business and prudential rules and regulations on EU investment firms and banks. These rules will apply to the foreign bank's activities in the EU and may in some cases also apply to activities outside the EU (e.g. in the case of prudential rules).	If an EU bank has to register in the US, triggering US regulatory supervision over the foreign bank's activities in the EU, conflicts with EU competent authorities may arise. EU home state regulators are unlikely to defer to the assumption of jurisdiction by US regulators over activities to which conflicting local regulatory requirements apply. EU entities falling within the scope of Dodd-Frank capital requirements would also be subject to EU capital requirements. Duplicative calculation of capital could be required (unless reliance on home country capital requirements is allowed), even if the international standards agreed under Basel III are implemented in the EU (through CRD IV) and US. To avoid duplication of regulation, a non-US entity might cease or restrict dealing with US persons or create a separate US subsidiary to handle US-based activity. The use of a subsidiary would require repapering of client agreements and transactions and require an intra-group business transfer; it could also increase inefficiencies and systemic risk, as US customers of foreign banks may have a more thinly capitalized subsidiary as their counterparty. This would be a particular concern if separate subsidiaries

[20] Notwithstanding the general exemption, requirements for reporting of trades to a swap data repository and large trader reporting requirements for transactions with US counterparties would apply.

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			were used across multiple jurisdictions. Extraterritorial laws often give rise to jurisdictional problems and spark responses from legislators elsewhere to prevent the extraterritorial application of those laws.[21] Given the global nature of financial sector businesses, it is possible that the EU could take measures in response to the extraterritoriality of US regulations (or *vice versa*), which could be counterproductive.
Non-US branch of a US entity engages in a swap or security-based swap with a non-US entity.	US entities may be required to register as swap dealers or security-based swap dealers for all swaps or security-based swaps activities, respectively, and may be subjected to US regulation regardless of where they are carried out. Under the CFTC's Cross-Border Exemptive Order, activities of foreign branches of US swap dealers with non-US persons would be subject to the Dodd-Frank Entity-Level Requirements but generally would only be subject to the Transaction Level Requirements to the extent required by local law (i.e. host country requirements will apply). After the expiration of the Cross-Border Exemptive Order, under the CFTC's proposed guidance, the Transaction-Level Requirements would apply (other than external business conduct rules), but substituted compliance with comparable host country regulation may be permitted.	Derivatives transactions between an EU person and a foreign branch of a US entity may be subject to EMIR. As noted above, the EU clearing obligation applies to a transaction between a financial counterparty (or a non-financial counterparty exceeding the clearing threshold) and a non-EU entity that would be subject to the clearing obligation if it were established in the EU. It also applies to transactions between two non-EU entities "*provided that the contract has a direct, substantial and foreseeable effect within the EU or where such an obligation is necessary or appropriate to prevent the evasion of any provisions of*" EMIR. Counterparties are permitted to comply with the clearing obligation through indirect clearing arrangements with a client of a clearing member of a CCP, provided that the client is an authorized EU credit institution or investment firm, or has equivalent authorization in a third country.	Foreign branches of US entities may be subject to local regulation in the EU as well as US regulation of the overall entity. Local competent authorities are unlikely to defer to US regulators' jurisdiction over the affairs of branches in the EU, especially as regards conduct of business matters. Under MiFID II, a mechanism for harmonizing access to EU markets for non-EU entities is proposed, subject to a strict equivalence regime. If a transaction is subject to both the EMIR mandatory clearing requirements and the Dodd-Frank clearing requirements (for example, if the US regime for CCPs was not declared equivalent to EMIR by the European Commission), it may be difficult for parties to comply with both sets of requirements. If a swap is required to be executed under Dodd-Frank on a swap execution facility and on an EU-regulated trading platform under EU legislation, the

[21] For example, the extraterritorial application of US sanctions against Cuba so that any entity, wherever organized, that is owned or controlled by a US person is subject to such sanctions led to the EU adopting Regulation 2271/96 prohibiting EU entities from complying with certain extraterritorial US laws. No such measures exist in the financial regulatory sector, though this is possible in the future.

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	In terms of margin requirements, the proposed PR Rules provide that transactions between a foreign dealer or MSP and a foreign counterparty are exempt from the requirement to post margin. However, foreign branches, offices, or subsidiaries of US persons (and counterparties receiving a guarantee from US affiliates) would not fall within the exclusion. Margin requirements apply to transactions between US bank dealers/MSPs and their counterparties regardless of location. Under the proposed margin rules, initial margin would need to be segregated[22] with an independent third-party custodian based in a jurisdiction applying the same insolvency regime as the posting (under PR Rules) or receiving (under CFTC Rules) swap participant. For example, initial margin posted by a US swap participant to a swap dealer must be segregated with a US custodian.	Where one party to the transaction is established outside the EU and is subject to a regime declared equivalent to EMIR, it will be deemed to comply with the EMIR clearing and reporting obligations. The MiFID II proposal for a mandatory exchange-trading requirement for clearing-eligible and sufficiently liquid derivatives may also apply to contracts with non-EU persons where they are subject to the EMIR clearing obligation. The EMIR risk mitigation provisions for OTC transactions not cleared by a CCP include a requirement for financial counterparties (or non-financial counterparties meeting the clearing threshold) to "*require the timely, accurate and appropriately segregated exchange of collateral with respect to OTC derivatives contracts*". Detailed requirements will be set out in further technical standards. These requirements will apply to non-EU entities on the same basis as the clearing obligation described above. Outside the EU, other local requirements will apply. In Japan, for example, certain OTC derivatives transactions must be cleared by a licensed domestic CCP.	platform would likely have to be approved under both pieces of legislation. Similar issues with conflicting local requirements could also arise for non-US persons incorporated outside the EU. It is usually possible to comply with differing requirements in relation to levels and acceptable forms of margin, but it may be difficult or impracticable for non-US entities to comply with aspects of the Dodd-Frank margin requirements, particularly in relation to segregation and appropriate custodians. The US segregation requirement may conflict with the EU practice of title transfer collateral arrangements. The potential for the ESMA technical standards to impose conflicting requirements could make matters more problematic. Depending on the CFTC's final position on the requirements applicable to branches of US entities, non-US entities may avoid entering into transactions with such branches in order to avoid becoming subject to Dodd-Frank requirements.
Foreign branch of a US entity engages in a swap with a non-US sovereign.	The proposed margin rules classify non-US sovereigns as financial end-users, and therefore would be subject to the margin requirement. Since that time, the CFTC has taken the position that non-US sovereigns would not be subject to the mandatory clearing requirement	The EMIR requirements (including clearing and reporting requirements) will not apply to: (1) members of the European System of Central Banks (i.e. the Eurozone countries), other EU national bodies performing similar functions and other EU	Non-US sovereigns may be reluctant to enter into derivatives transactions with US banks if this obliges them to post collateral.

[22] Under the CFTC Rules this would be at the option of the counterparty.

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	(although this position would not apply to sovereign wealth funds, as opposed to the sovereign itself). Under the Cross-Border Exemptive Order, until July 2013, the non-US branch of a US registered swap dealer would not be required to comply with other Transaction-Level Requirements with a non-US sovereign, except to the extent required under local law.	public bodies charged with or intervening in the management of the public debt; and (2) the Bank for International Settlements. The EMIR requirements (save for the reporting requirement) will not apply to: (1) multilateral development banks; (2) public sector entities owned and expressly guaranteed by central governments; and (3) the European Financial Stability Facility and the European Stability Mechanism.	
Non-US entity deals in swaps with a US person.	The foreign entity may, depending on the scope of its activities, be subject to the Dodd-Frank requirements, either through the requirement to register as a swap dealer or security-based swap dealer, or classification as an MSP. Under the CFTC's Cross-Border Exemptive Order, if registration is required, compliance may be deferred for certain Entity-Level Requirements (such as capital requirements), and after expiration of the order, substituted compliance based on comparable home country regulation might be permitted under the CFTC's proposed interpretive guidance. For other, Transaction-Level Requirements, the US rules would apply to transactions with US persons. Under the CFTC's proposed interpretive guidance, even if registration is not required, the Dodd-Frank clearing, margin and reporting requirements would apply.	An EU financial counterparty is likely to be subject to regulation in its home state as a bank or investment firm.	There is a clear imbalance where foreign entities are subject to US registration requirements, but US persons may not be subject to equivalent requirements in the jurisdictions of those foreign entities. This is likely to impose onerous burdens on non-US entities and may deter them from transacting with US persons. The jurisdictions of those foreign entities may respond with retaliatory measures.
EU entity deals in swaps with US persons, or US entity transacts with an EU entity, in circumstances where the swap is subject to the	The swap may also be subject to the US mandatory clearing obligation as well as reporting requirements. The CFTC has not proposed to permit substituted	The EMIR mandatory clearing and reporting obligations apply to the transaction where the non-EU entity would be subject to the clearing obligation if	If the swap must be cleared both by a registered EU CCP and by a US clearing house, the CCP would need to be both registered with ESMA and have DCO

SCENARIO	APPLICABLE DODD-FRANK REQUIREMENTS	APPLICABLE EUROPEAN REQUIREMENTS	ASSOCIATED ISSUES
EMIR clearing obligation.	compliance for the clearing, trade-execution and real-time public reporting requirements, or for the large trader reporting requirements otherwise applicable to non-US persons transacting with US persons. However, the CFTC has proposed to allow substituted compliance with respect to swap data repository reporting and recordkeeping requirements for transactions subject to them, provided that the CFTC has direct access to the swap data for these transactions that is stored at the foreign trade repository.	incorporated in the EU (subject to equivalence determination). EMIR contains an exemption for intra-group transactions. The definition of "intra-group" differs for financial versus non-financial counterparties, but in both cases a transaction will only be intra-group if the counterparty is established either in the EU or in a jurisdiction declared equivalent by the European Commission.	and/or SEC clearing agency status (or an exemption from registration). However, where one party to the transaction is established outside the EU and is subject to a regime declared equivalent to EMIR, it will be deemed to comply with the EMIR clearing and reporting obligations. If a swap is required to be executed under Dodd-Frank at a swap execution facility and on an EU-regulated trading platform under EU legislation, dual regulation for the execution venue would likely be required. EMIR contains mechanisms for recognizing third-country CCPs (e.g. US CCPs) and for grandfathering existing UK recognized overseas clearing houses pending the outcome of applications to ESMA for authorisation. CCPs and platforms are presently facing considerable challenges in complying with conflicting US and EU regulatory requirements and supervisory processes. Under EMIR, a swap must be reported to an ESMA-registered trade repository, and under Dodd-Frank to a registered swap data repository, with certain exceptions where substituted compliance may be acceptable. The parties may therefore need to report separately, leading to duplicative data submissions. Some repositories may consider providing a "one-stop shop" for reporting and holding data through different legal entities in both jurisdictions.
Foreign dealer deals in swaps with a non-US person, but the transaction has some US connection.	A transaction will be subject to US jurisdiction if it has a "direct and significant connection with activities in, or effect on," commerce of the United States. Under the CFTC's proposed cross-border guidance and Cross-Border Exemptive Order, in general US requirements	If the swap is transacted between EU entities, it is likely to be subject to EMIR and MiFID II requirements.	See the conflicts noted above in relation to complying with both regimes. Applying the requirements of Dodd-Frank to US persons involved in ancillary activities related to a swap could result in entities moving back-office or other operations away from the US or no longer

SCENARIO	APPLICABLE DODD-FRANK REQUIREMENTS	APPLICABLE EUROPEAN REQUIREMENTS	ASSOCIATED ISSUES
	would not apply to transactions entered into between two non-US persons outside the United States where neither person is a swap dealer or MSP. However, the final definition of US person is still uncertain, and questions as to the possible application of Dodd-Frank requirements may arise in a variety of cross-border situations, including where: a) US persons are involved in activity related to a swap (potentially including sales, marketing, operations, back-office or similar functions) even if the party to the swap is not a US person; or b) A non-US person contacts a US-domiciled professional fiduciary that acts for a counterparty located outside the US. Where such a connection is identified, the Dodd-Frank registration, mandatory clearing/execution, and trade reporting requirements could apply. In the context of a non-US branch of a US swap dealer, the CFTC takes the position in the Cross-Border Exemptive Order that a swap will be treated as being with the branch, rather than the home entity (and therefore exempt from certain Transaction-Level Requirements), where (i) the personnel negotiating and agreeing to the terms of the swap are located in the jurisdiction of the foreign branch, (ii) the documentation of the swap specifies that the counterparty or office is the foreign branch and (iii) the swap is entered into by the foreign branch in its normal course of business.		locating administrative or support personnel in the US. Similarly, US professional fiduciaries may be placed at a competitive disadvantage if the requirements were applied in the circumstances outlined in column 1 point (b).

Glossary

The following definitions are for ease of reference only and are not intended to provide a complete definition of the relevant concepts.

US	CFTC	Commodity Futures Trading Commission.
	CFTC Rules	Rules proposed by the CFTC under Dodd-Frank, including sections 731 and 764 (Margin Requirements for Non-bank Swap Dealers and Major Swap Participants).
	DCO	Derivatives Clearing Organization, as defined in the Commodity Exchange Act.
	Entity-Level Requirements	Apply to a swap dealer or MSP as a whole and encompass requirements as to capital, chief compliance officer, risk management, swap data recordkeeping and reporting and large trader reporting.
	Financial End-User	An end-user (as opposed to a dealer) that is a financial entity.
	Major Security-Based Swap Participant	A person other than a security-based swap dealer who maintains a substantial position in security-based swaps (as defined in Exchange Act Section 3(a)(67)).
	MSP	Major Swap Participant: a person other than a swap dealer who maintains a substantial position in swaps (as defined in CEA Section 1a(32) and CFTC Rule 1.3(hhh)).
	PR Rules	Margin rules proposed by the Prudential Regulators under Dodd-Frank, sections 731 and 764, applicable to swap dealers, security-based swap dealers, major swap participants and major security-based swap participants that are banks and bank holding companies (Margin and Capital Requirements for Covered Swap Entities, 12 April 2011).
	SEC	Securities and Exchange Commission.
	Security-Based Swap	A swap based on an index that is a narrow-based security index, a single security or loan or on the occurrence, non-occurrence or extent of the occurrence of an event relating to a single issuer of a security or the issuers of securities in a narrow-based security index (as defined in Exchange Act Section 3(a)(68)).
	Security-Based Swap Dealer	A person which holds itself out as a dealer in security-based swaps, makes a market in security-based swaps, regularly enters into security-based swaps with counterparties for its own account in the ordinary course of business or is commonly known as a dealer or market maker in security-based swaps (as defined in Exchange Act Section 3(a)(71)).
	Swap	A non-security based derivatives transaction (including interest rate, currency and commodity derivatives) as well as derivatives on broad-based security indices (such as index based credit default swaps) (as defined in CEA Section 1a(47) and CFTC Rule 1.3(xxx)).
	Swap Data Repository	A centralized recordkeeping facility for swaps (as defined in CEA Section 1a(48)).

	Swap Dealer	A person that holds itself out as a dealer in swaps, makes a market in swaps, regularly enters into swaps with counterparties for its own account in the ordinary course of business or is commonly known as a dealer or market maker in security-based swaps (as defined in CEA Section 1a(49) and CFTC Rule 1.3(ggg)).
	Swap Execution Facility	A trading system/platform that facilitates the execution of swaps (as defined in CEA Section 1a(50).
	Transaction-Level Requirements	Encompass mandatory clearing and swap processing, margin for uncleared swaps, trade execution requirements, relationship documentation, portfolio reconciliation and compression, real time public reporting, trade confirmation, daily trading records and external business conduct standards.
EU	ESMA	European Securities and Markets Authority.
	CRD IV	Capital Requirements Directive IV.
	Financial Counterparty	As defined in EMIR, article 2 (includes banks, investment firms, credit institutions, insurers, registered UCITS funds, pension funds and alternative investment fund managers).
	Non-Financial Counterparty	As defined in EMIR, article 2, an entity established in the EU other than a financial counterparty.
	Trade Repository	As defined in EMIR, article 2, a legal entity that centrally collects and maintains the records of OTC derivatives.
Miscellaneous	CCP	A central counterparty (also defined in EMIR, article 2).

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