



To:

Michel Barnier,
Commissioner for the Internal Market and Services,
The European Commission,
BERL 10/034,
B-1049 Brussels,
Belgium

The Honorable Timothy Geithner,
Secretary,
The Department of the Treasury,
1500 Pennsylvania Avenue, NW,
Washington, D.C. 20220,
United States

5 July 2011

Dear Commissioner Barnier,
Dear Secretary Geithner,

Extra-territorial effects in EU and US regulation of derivatives

In September 2009, leaders of the G20 undertook to strengthen the international financial regulatory system. Shared G20 commitments included measures to ensure stricter rules on transparency, capital, counterparty risk (through clearing and other operational commitments) and trading of derivatives contracts. Considerable progress has been made on these commitments by G20 members, and it is clear that G20 leaders will successfully deliver them.

Importantly, understanding the global nature of today's financial markets, the G20 also undertook to 'take action at the national and international level to raise standards together so that our national authorities implement global standards consistently in a way that ensures a level playing field and avoids fragmentation of markets, protectionism, and regulatory arbitrage.'

The associations signing this letter are concerned that regulation in different G20 jurisdictions may be creating conditions which will lead to the above-mentioned harmful outcomes, ultimately decreasing the ability of global regulators to effectively regulate an increasingly global capital marketplace.

Extra-territorial application of one nation's laws to another nation's markets and firms is a fundamental concern in a global market like derivatives, where it is common for counterparties based in different parts of the world to transact with each other.

Specifically, in the United States and Europe, we believe that both sets of rules, as proposed in the United States and as currently being debated in the EU, leave the global derivatives business with ambiguity and problematic extra-territorial challenges and issues of legal uncertainty and misunderstanding which might give rise to material risk.

We are also concerned that recent public commentary by EU and US decision-makers on issues deriving from extra-territorial aspects of financial legislation may be giving a misleading impression as to the proven commitment of decision-makers in these (and other) jurisdictions to problem-solving and avoidance of conflicts and unnecessary burdens.

The G-20's goal of addressing key systemic risk issues cannot be met without international coordination on market infrastructure, regulatory transparency, and counterparty credit risk. Examples of extra-territorial concerns that have arisen due partly to insufficient coordination are included below:

Licensing, authorisation or registration rules: Rules for licensing entities that are significant participants in the swap market should be coordinated so that those entities do not face duplicative regulatory regimes. We urge global legislators and regulators to work together towards a sensible and mutually acceptable solution that reflects the legitimate interest in regulatory oversight of entities active in a jurisdiction in a manner that gives due recognition to the rules that are applicable to an entity in its home jurisdiction.

Potential overlap and conflict in regulation of derivatives market participants in foreign jurisdictions: It is important that global regulators agree to a coherent and complementary approach to the regulation of activities of financial institutions such as banks, broker dealers and asset managers in foreign jurisdictions, ensuring both a sufficiently stringent regulatory standard and an avoidance of conflict and overlap in regulation. An example of the difficulties that can be caused in this context is the extra-territorial application of margin requirements to non-US subsidiaries, branches or affiliates of US financial services institutions, meaning that these subsidiaries, branches and affiliates will face dual (and possibly, conflicting) regulatory requirements (as opposed to local competitors who will have to comply only with the local regulatory regime). Similarly, non-US firms have concerns about their US subsidiaries, branches or affiliates facing dual (and possibly, conflicting) requirements in the US and in their home jurisdiction. We also urge global regulators to enter into mutual recognition arrangements where each would limit the extra-territorial reach of their regulation so long as a firm complies with their home country regulations.

Discrimination in dealing with sovereigns: We urge global regulators to avoid or revisit regulatory approaches which apply discriminatory rules to locally-regulated financial institutions' dealing with entities from other jurisdictions, particularly sovereigns from those jurisdictions (both recent EMIR drafts and recent US draft prudential regulations propose that sovereigns outside their jurisdiction should have to post margin with the firms regulated under each set of regulations).

Rules for CCPs: Regulators should seek to agree on the standards for equivalence or recognition of CCPs in each others' jurisdictions – to avoid such ambiguity and to give CCPs and regulators the opportunity

to meet these standards (also giving market participants the opportunity to prepare for compliance and to transition to a cleared environment for their trading activities). Equivalence is critical for rules on clearing as conflicting clearing requirements would be impossible to comply with if the rules of each of two different jurisdictions require a trade to be cleared in its jurisdiction.

Trade Repositories: The Dodd-Frank Act's requirement that US-based Swap Data Repositories (SDRs) obtain indemnification from foreign regulators as a pre-condition to data sharing is, we understand, an area of discussion currently between global regulators. This statutory requirement is not only unnecessary (given international agreements on sharing of data and work such as that pursued in the OTC Derivatives Regulators Forum at international level) but also undermines the ability of trade repositories to provide coherent information on risk in the derivatives business to regulators throughout the world (the original goal of creating data repositories). Likewise, pre-conditions to recognition of third country repositories in EU regulation are best drafted in cooperation and understanding with regulators in those third countries. We support the continued dialogue among global regulators on these issues.

The above examples are not exhaustive, but indicative of the problems faced by regulators and industry alike in the current environment. The signatory associations would be happy to provide regulators with more detail on extra-territorial concerns if this would be helpful.

Failing to address problems such as these will have significant adverse consequences not only for financial and non-financial companies, but also for the global economy. Even if extra-territorial application of domestic rules and the associated erection of artificial barriers to the functioning of businesses with an international footprint is not the intention, in many instances, the economic effects often associated with protectionism will result. Application of one jurisdiction's rules to institutions operating in another jurisdiction makes it more costly to transact in markets subject to such rules, which in turn undermines the ability of firms to manage risk and makes for higher financing costs for the real economy. This in turn undermines investment and employment.

Of further concern is that extra-territorial application of rules will lead to a more fragmented view of activity in financial markets, making it more difficult for regulators to monitor, much less prevent a build-up of systemic risk.

We therefore urge policymakers to redouble their efforts to ensure that reform of the international financial regulatory system is based on consistency of approach and on mutual recognition. We believe that there remains considerable scope both in the Dodd-Frank Act and EU regulation to prevent, alleviate or limit the harmful effects of such overlapping, inconsistent and ambiguous rules. **We believe that regulators should seek to limit the damaging effects of divergence, either by consultation with international counterparts in preparation of legislation, or by resolving these differences in the course of implementation of legislation.** We encourage political leaders and regulators to give these issues the attention they merit, working *proactively* within the mechanisms available to them in each jurisdiction, and through *constructive and open* bilateral and multilateral dialogue. In this regard, we welcome the recent establishment of a Trans-Atlantic regulatory working group to address differences between the EU and US regulators on derivatives regulation and observe that the EU-US Financial Markets Regulatory Dialogue had been helpful in resolving issues such as these in the past. Furthermore, we believe that industry could add value to regulators' consideration of these extra-territorial effects and urge the participants in these groups to consider how they could take advantage of the relevant knowledge available from associations and market participants engaged in multiple jurisdictions.

Yours sincerely,



Conrad P. Voldstad, CEO, International Swaps and Derivatives Association (ISDA)



T. Timothy Ryan, Jr., President & CEO, Global Financial Markets Association (GFMA)



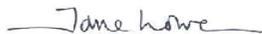
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Andrew Baker, Chief Executive Officer, Alternative Investment Management Association (AIMA)



Anthony Belchambers, CEO, Futures and Options Association (FOA)



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Cc

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Sharon Bowles MEP, Chairman, Economic and Monetary Affairs Committee, European Parliament

Werner Langen MEP

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George Osborne, Chancellor of the Exchequer, United Kingdom

Francois Baroin, Minister for the Economy, Finance and Industry, France

Wolfgang Schäuble, Federal Minister of Finance, Germany

Steven Maijoor, Chairman, European Securities Markets Authority

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