OTC Swaps Regulatory Recap

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Introduction

The OTC derivatives regulatory landscape is always changing, and there have been several noteworthy developments recently. Specifically, shifts in supervisory approach, substantive rule changes, and cross-border coordination efforts all warrant attention. This paper gives derivatives market participants a practical overview of the most consequential recent developments. We focus on six key areas:

(1) regulatory withdrawals and supervisory tone;
(2) the "U.S. person" definition and related no-action relief;
(3) CFTC business conduct and swap documentation rule revisions;
(4) SEC/CFTC harmonization initiatives;
(5) EMIR 3 and cross-border developments; and
(6) the role of artificial intelligence in derivatives compliance.

I. Regulatory Withdrawals and Shifting Supervisory Approaches

On February 25, 2025, the CFTC's Division of Enforcement issued an advisory on how the Division will evaluate a company's or individual's self-reporting, cooperation, and remediation when recommending enforcement actions to the CFTC and establishes the factors the Division will consider. The advisory provides fair notice to the public and guidance that is designed to ensure due process in the Division's investigations and enforcement actions.

Market participants have also observed changes in the tone and conduct of examinations. Supervisory exams have become more collaborative. Regulators have shown increased willingness to engage constructively on practical implementation challenges. These developments represent what many view as "low-hanging fruit." They are welcome, but primarily behavioral rather than structural.[1] The CFTC has highlighted its emphasis and self-reporting, cooperation & remediation, and a mitigation credit for civil monetary penalties. The mitigation credit introduces a novel "Mitigation Credit Matrix".

II. U.S. Person Definition and Cross-Border No-Action Relief[2]

Changes to the CFTC's guidance on the "U.S. person" definition and cross-border no-action relief are among the more impactful recent developments. The "U.S. person" definition determines when CFTC swap dealer regulations apply to cross-border transactions. It also determines when foreign entities must register as swap dealers based on their U.S. activity.

Background on the U.S. Person Framework. Under the Commodity Exchange Act, the CFTC's jurisdiction extends to swaps involving U.S. persons. The definition of "U.S. person" therefore controls the scope of regulatory obligations for foreign market participants. It affects registration requirements, business conduct standards, reporting obligations, and clearing mandates. Prior guidance created

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[1] See CFTC Press Release 9054-25: https://www.cftc.gov/PressRoom/PressReleases/9054-25; Division of Enforcement Advisory, available here:https://www.cftc.gov/media/11821/EnfAdv_Resolutions022525/download.
[2] See e.g., CFTC Press Release 9149-25: https://www.cftc.gov/PressRoom/PressReleases/9149-25; CFTC No-Action Letter 25-42: https://www.cftc.gov/csl/25-42/download; CFTC Letters 25-18 and 25-14 (addressing cross-border clearing matters)

complexity around the treatment of foreign branches, guaranteed affiliates, and conduit affiliates of U.S. entities.

Recent No-Action Relief. CFTC No-Action Letter 25-42 provides targeted relief from certain cross-border requirements. The relief addresses situations where strict application of the U.S. person framework would impose disproportionate compliance burdens without corresponding regulatory benefit. CFTC Letters 25-18 and 25-14 address cross-border clearing matters specifically. These letters clarify when foreign counterparties must clear swaps through U.S.-registered derivatives clearing organizations.

Practical Impact on Market Participants. These changes have direct implications for how institutions structure cross-border transactions. For some market participants, the changes have materially affected booking decisions. Institutions may now route certain transactions through different legal entities based on the revised guidance. Trading strategies for firms with global operations may also require adjustment.

Documentation Implications. Market participants must evaluate documentation requirements for both new and existing client relationships. Updated representations regarding U.S. person status may be necessary, and certain Swap Dealers have updated their onboarding forms accordingly. Compliance certifications and counterparty classification protocols should be reviewed. Institutions should assess the scope of available relief and determine whether existing arrangements remain within regulatory safe harbors. ISDA protocols and relationship documentation may require amendment to reflect the revised framework.

III. CFTC Business Conduct and Swap Documentation Rule Revisions

The CFTC has finalized significant revisions to its business conduct standards and swap documentation requirements. Published in the Federal Register in late 2025, these amendments are commonly referred to as the External Business Conduct Standards ("EBCS") and Swap Trading Relationship Documentation ("STRD") rule changes.

Key Changes Include:[3]

Removal of Pre-Trade Mid-Market Mark (PTMM) and Scenario Analysis Requirements. The revised rules eliminate certain pre-trade disclosure obligations that imposed substantial operational burdens. The removal of the PTMM requirement simplifies the pre-execution process while maintaining core counterparty protection principles.

[3] See • Federal Register Publication (December 30, 2025): https://www.federalregister.gov/documents/2025/12/30/2025-23953/revisions-to-business-conduct-and-swap-documentation-requirements-for-swap-dealers-and-major-swap; CFTC Press Release 9157-25: https://www.cftc.gov/PressRoom/PressReleases/9157-25.

Introduction of the "Intended-to-be-Cleared" (ITBC) Concept. The rules formally introduce the ITBC framework. This provides greater clarity around the regulatory treatment of swaps intended for clearing at execution. The formalization affects how market participants document and process transactions.

Prime Brokerage and Client Trading Implications. The rule changes carry specific ramifications for prime brokerage arrangements. Participants engaged in prime brokerage must evaluate how the revised requirements affect client onboarding, trading permissions, and compliance monitoring.

Legal Documentation Impacts. Swap dealers and counterparties should anticipate the need to amend existing trading documentation. This includes ISDA Master Agreements and related protocols. Documentation counsel should review existing arrangements to identify provisions requiring updates.

IV. SEC/CFTC Harmonization Initiative[4]

The perennial goal of harmonizing SEC and CFTC regulatory requirements has reemerged as an area of active focus. On March 11, 2026, the agencies signed a Memorandum of Understanding Regarding Harmonization in Areas of Common Regulatory Interest. This MOU supersedes the prior 2018 coordination agreement and reflects a more ambitious commitment to regulatory alignment.

The MOU recognizes that financial markets are evolving rapidly and becoming more interconnected. New trading models, digital infrastructure, and automated systems increasingly blur traditional jurisdictional lines. The agencies acknowledge that market participants operate across platforms and asset classes. Risks can propagate quickly across markets. The MOU aims to provide regulatory clarity, reduce uncertainty, and help ensure U.S. markets remain globally competitive.

The MOU applies to firms of common regulatory interest. These include firms registered as both Investment Advisers and Commodity Pool Operators or Commodity Trading Advisors. They also include firms registered as both Broker-Dealers and Futures Commission Merchants or Introducing Brokers. Entities registered as both Clearing Agencies and Derivatives Clearing Organizations are covered. So are firms registered as both Swap Execution Facilities and Security-Based Swap Execution Facilities, both Swap Data Repositories and Security-Based Swap Data Repositories, and both Swap Dealers and Security-Based Swap Dealers.

The MOU identifies six primary areas for coordination:

1. Clarifying product definitions through joint interpretations and rulemakings.
2. Modernizing clearing, margin, and collateral frameworks.
3. Reducing frictions for dually registered exchanges, trading venues, and intermediaries.
4. Providing a fit-for-purpose regulatory framework for crypto assets and other emerging technologies.
5. Streamlining regulatory reporting for trade data, funds, and intermediaries.
6. Coordinating cross-market examinations, economic analyses, risk monitoring, surveillance, and enforcement.

[4] See CFTC Harmonization Initiative: https://www.cftc.gov/harmonization; CFTC Press Release 9192-26: https://www.cftc.gov/PressRoom/PressReleases/9192-26; Memorandum of Understanding, https://www.sec.gov/files/mou-sec-cftc-2026.pdf .

Examination Coordination. The agencies commit to conduct coordinated exam planning and joint or aligned examinations where appropriate. They will share exam findings and supervisory insights. Where a Covered Firm appears on both agencies' examination plans, the agencies will consider how to minimize burden. This may include conducting coordinated examinations. The agencies will exchange regulatory information including examination letters, reports, registration data, and risk assessment data.

Enforcement Coordination. The MOU establishes procedures for consultation on enforcement investigations involving potential overlapping jurisdiction. The agencies will confer on areas of mutual interest and identify jurisdictional overlap prior to issuing Wells notices. Where parallel enforcement actions are appropriate, they will coordinate on potential charges, relief, sequencing, litigation strategy, and public communications.

Information Sharing. The agencies agree to share data regarding matters of common regulatory interest. They will work to access swap and security-based swap data directly from the respective data repositories. Each agency will share analysis of reported data and related analytical and monitoring capabilities.

Guiding Principles. The MOU articulates several guiding principles. These include respect for statutory mandates, regulatory efficiency, good faith collaboration, regulatory clarity and consistency, and functional and risk-based regulation. The agencies commit to reject a "turf war" mentality and to provide fair notice to market participants. They recognize the foundational importance of not regulating through enforcement.

Alternative Compliance. The MOU reflects a commitment to a "minimum effective dose" regulatory strategy. The agencies will seek to facilitate alternative compliance frameworks. This includes enabling a path for appropriately tailored "super-apps" where such approaches can achieve regulatory objectives more efficiently.

The MOU does not create legally binding obligations. Whether regulatory harmonization in this nation is achievable is an open question. Watch this space.

V. EMIR 3 and Cross-Border Regulatory Developments[5]

European regulators have finalized EMIR 3, the latest revision to the European Market Infrastructure Regulation. The changes affect both European market participants and their global counterparties. The revisions have particular implications for classification requirements, clearing thresholds, and the taxonomy applicable to non-financial counterparties (NFCs).

Classification and Clearing Threshold Changes. EMIR 3 modifies the framework for determining clearing obligations and margin requirements based on counterparty classification. Participants must evaluate their status under the revised taxonomy and assess whether applicable thresholds have changed.

[5] See Directive (EU) 2024/2994: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=OJ:L_202402994; Regulation (EU) 2024/2987: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=OJ:L_202402987.

Phase-In and Phase-Out Provisions. The regulation includes transitional provisions governing compliance timing. Careful attention to these schedules is essential to avoid gaps in compliance coverage.

Cross-Border Alignment. EMIR 3 represents an effort to improve alignment between EU, UK, and U.S. regulatory frameworks. Significant divergences remain. Participants operating across jurisdictions must continue to navigate a complex web of potentially overlapping requirements.

SIMM Model Approvals and Asset Class Clearing Thresholds. The revisions also address the Standard Initial Margin Model (SIMM) approval process and clearing thresholds for specific asset classes. These technical provisions warrant attention from risk and operations teams.

VI. Artificial Intelligence in Derivatives Compliance: Promise and Peril

The complexity of the global derivatives regulatory environment has prompted growing interest in applying artificial intelligence to compliance functions. Cross-border rule mapping alone requires tracking requirements across multiple jurisdictions, each with distinct registration thresholds, reporting formats, clearing mandates, and margin rules. AI tools offer potential benefits in managing this complexity. They can assist with regulatory analysis, gap identification, and ongoing compliance monitoring.

Market participants and CLE Paper authors report a notable increase in AI usage.. Business colleagues increasingly submit AI-generated analyses of regulatory requirements to compliance teams for review. Sometimes they do so without adequately understanding the tools' limitations. Large language models can produce confident but inaccurate interpretations of complex regulatory text. Compliance professionals must therefore exercise caution before relying on AI-generated legal analysis.

The risks are not hypothetical. AI systems may misinterpret defined terms, overlook cross-references, or fail to account for no-action relief that modifies otherwise applicable requirements. They may conflate SEC and CFTC requirements or misapply cross-border guidance. In derivatives compliance, such errors can have significant consequences. Incorrect counterparty classification, missed reporting deadlines, or improper margin calculations can trigger regulatory violations.

Despite these concerns, AI offers genuine benefits when deployed appropriately. It can accelerate the initial review of lengthy regulatory texts. It can flag potential inconsistencies between existing compliance procedures and new rule requirements. It can assist in "translating" complex regulatory language into operational tasks that business and technology teams can implement. For cross-border compliance, AI can help map equivalent requirements across jurisdictions and identify divergences that require attention.

Governance is key. Firms should have clear protocols for AI use in compliance contexts. These should specify which tasks are appropriate for AI assistance and which require unassisted human judgment. Output validation procedures are essential. Compliance professionals should verify AI-generated analysis against primary sources before acting on it. The goal is to leverage AI's capabilities while maintaining human oversight of consequential compliance decisions. Regulators will likely expect firms to demonstrate that AI tools are subject to appropriate controls and do not substitute for professional judgment on material compliance matters.

Conclusion

The OTC derivatives regulatory landscape continues to evolve rapidly. The developments addressed in this alert require ongoing attention from compliance, legal, and business teams. Market participants should assess the impact of these changes on existing compliance frameworks. They should engage proactively with counsel to address documentation and operational implications. We will continue to monitor these developments and provide updates as warranted.
