IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION, INTERNATIONAL SWAPS AND DERIVATIVES ASSOCIATION, INSTITUTE OF INTERNATIONAL BANKERS, Plaintiffs, v. UNITED STATES COMMODITY FUTURES TRADING COMMISSION, Defendant.	Civil Action No. 13-cv-1916 (ESH)

BRIEF OF BETTER MARKETS, INC. AS *AMICUS CURIAE* IN SUPPORT OF DEFENDANT COMMODITY FUTURES TRADING COMMISSION

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IDENTITY AND INTEREST OF BETTER MARKETS

Better Markets, Inc. ("Better Markets") respectfully submits this brief in support of Defendant Commodity Futures Trading Commission ("CFTC"). Better Markets is a non-profit organization that promotes the public interest in the financial markets. It has submitted over 150 comment letters to the CFTC, the Securities and Exchange Commission ("SEC"), and other financial regulators advocating for strong and swift implementation of the comprehensive reforms Congress established in the Dodd-Frank Act to prevent another financial crisis and recession—calamities brought on by some of the very institutions that the Plaintiffs represent in this case. As part of that advocacy, Better Markets has argued extensively for the adoption of appropriately strong rules governing the derivatives markets under Title VII of the Dodd-Frank Act, and for broad application of those rules to international or "cross-border" transactions.[1]

Better Markets has also defended the rules of the CFTC and the SEC in court against relentless legal challenges from some sectors in the financial industry. Those attacks are intended not only to invalidate specific rules, but to delay, weaken, and ultimately derail the entire process of financial reform. The principal tactic is to raise the specter of alarming but unsubstantiated costs and burdens that will allegedly flow from regulation, and to insist that the rule-writing agencies catalogue, quantify, and weigh all of those costs before issuing their rules.

That is certainly the Plaintiffs' strategy here. They have alleged that cross-border application of the Title VII Rules will impose heavy compliance costs and cause damaging disruptions in the derivatives markets, but they offer little concrete support for such predictions. Moreover, throughout the history of financial regulation, such dire forecasts about the impact of

[1] *See, e.g.,* letters *available at* https://www.bettermarkets.com/sites/default/files/cross%20border%20comment%20letters.pdf.

regulation have proven groundless. *See* CFTC Opp'n to Mot. to Expedite at 5-6 (describing industry scarce tactics in recent lawsuits); BETTER MARKETS, SETTING THE RECORD STRAIGHT ON COST-BENEFIT ANALYSIS AND FINANCIAL REFORM AT THE SEC, at 44-48 (July 30, 2012).[2]

What is beyond dispute, however, is that just six years ago, Wall Street's unregulated, reckless, and often illegal conduct triggered the worst financial crisis and economic recession since the Great Depression. Yet nowhere do the Plaintiffs discuss or even acknowledge this historic financial crisis, which necessitated the passage of a comprehensive financial reform law, including Title VII and its cross-border application. Nor do the Plaintiffs acknowledge the role of their own members in causing the crisis, the enormous bailouts some of those members received,[3] or the irony in their demand for relief from the very reforms their conduct necessitated. And the Plaintiffs appear blind to the fact that nothing will cause more damage and disruption in the derivatives markets than another financial crisis.

Here, the threat to financial reform is enormous. The Plaintiffs are attacking not only the Cross-Border Guidance, but also the international application of 14 major rules governing almost every facet of the swaps marketplace. If successful, this assault will gut the new framework for derivatives regulation since U.S. banks will easily evade domestic requirements by engaging in their derivatives activities through a network of foreign branches and affiliates no longer subject to CFTC oversight. The result will be a perpetuation of the deregulatory environment that incubated the financial crisis of 2008: The too-big-to-fail banks will take mammoth risks in

[2] *Available at* http://bettermarkets.com/sites/default/files/CBA%20Report.pdf ("CBA Report").

[3] For example, numerous Plaintiff-member banks, which held tens of billions of dollars' worth of unregulated derivatives with AIG as counterparty, received massive payments, directly or indirectly, from various AIG bailout funding mechanisms, as follows (in billions): Goldman Sachs, $10.4; Deutsche Bank, $9.2; Société Générale, $7.8; Barclays, $7; Merrill Lynch, $5; Bank of America, $5. *See* Better Markets' comment letter to SEC Re: Cross-Border Security-Based Swap Activities, at Figure 1 (Aug. 21, 2013), *available at* https://www.bettermarkets.com/sites/default/files/130-SEC-%20CL-%20Cross-Border%20Regulation-%208-21-13.pdf.

search of huge revenues, while counting on U.S. taxpayers to clean up the mess and bail them out when their wagers fail. As an organization dedicated to strong and expeditious financial reform, Better Markets has an interest in helping to ensure that the Plaintiffs' arguments and tactics are rejected and that, through the uninterrupted application of the Title VII Rules in accordance with the Guidance, the chances of another financial crisis are minimized.

ARGUMENT

Without appropriately broad cross-border application of the Title VII Rules, the new framework for regulating the derivatives markets and preventing another financial crisis will become largely meaningless, as banks will easily shift their trading activities offshore to evade U.S. regulation. The arguments the Plaintiffs are advancing to achieve this deregulatory objective are meritless. The CFTC's obligation under Section 15(a) of the Commodity Exchange Act ("CEA"), 7 U.S.C. § 19(a), to consider costs and benefits does not apply, since Congress has already determined that the Title VII Rules should be extended to cross-border activities in accordance with Section 2(i) of the CEA, 7 U.S.C. § 2(i). The CFTC has no authority to second-guess this judgment. Even if it did apply, Section 15(a) would not require cost-benefit analysis, but a far more limited consideration of factors in light of the public interest. Among those key factors would be the collective benefit of the Title VII Rules, applied under the Guidance, in preventing another financial crisis and the trillions of dollars in damage it would inflict.

I. The Plaintiffs' claims threaten to abolish meaningful regulation of derivatives under Title VII.

All parties agree that the derivatives markets are fundamentally international in character, transcending national borders. As stated by the Plaintiffs, that is why the appropriate regulation of cross-border derivatives transactions has such "immense implications" for market participants both in the U.S. and abroad. Pls.' Mot. at 1. The Plaintiffs' declarations confirm the point by repeatedly acknowledging that, as part of their "global swaps business," banks regularly "transact with swap counterparties across the globe, including other U.S. banks, foreign affiliates and branches of U.S. banks, and other foreign banks." *See, e.g.,* Don Thompson Decl. at ¶ 2.

It is equally clear that international derivatives activities pose risks that "can threaten the financial stability of the entire U.S. financial system." Guidance, 78 Fed. Reg. at 45,294. The Guidance describes numerous examples, spanning more than a decade, where international derivatives activities by U.S. banks and their affiliates resulted in massive losses, systemic instability, or both—in some cases helping to precipitate the financial crisis and resulting in huge taxpayer bailouts. Guidance at 45,293-95 (highlighting enormous losses incurred by AIG's London affiliate, the JP Morgan Chase "London Whale" debacle, and other examples).

The Plaintiffs' declarations provide further compelling evidence that all of the branches, affiliates, and other units of a large, international bank are interconnected in terms of costs, and therefore interconnected in terms of risk as well. The declarations repeatedly allege that, under the 14 challenged rules, the banks' foreign branches and guaranteed affiliates will be subject to expensive new regulation. They provide no concrete details regarding these claimed costs, but they do contain a telling admission: Whatever those costs may be, they ultimately will be "**borne by [the parent bank] itself, because all are part of the same corporate group.**" *See, e.g.,* Don Thompson Decl. at ¶ 6 (emphasis added). This inevitable transmission of risk to the parent entity is precisely why the Title VII Rules must be applied not only to transactions in the U.S., but to all global derivatives activities that pose risks to U.S. entities, as the Guidance reflects.

Congress recognized the uniquely dangerous threat that cross-border derivatives activities pose to our financial system and our economy. It therefore chose to override any presumption against the extraterritorial application of U.S. law by enacting Section 2(i) of the CEA. As evidence of Congress's firm resolve to appropriately capture cross-border transactions within the mandate of Title VII, Section 2(i) gives the CFTC multiple broad grounds for asserting its jurisdiction extraterritorially. First, the standard is framed in terms of "commerce," an extraordinarily broad concept. Second, the standard is triggered not only where there are "direct and significant **effects**" on commerce, but also more generally where there is simply a "direct and significant **connection**" with activities in commerce. Finally, the standard authorizes regulation of extraterritorial activities under Title VII wherever it is "necessary or appropriate" to prevent evasion of **any** CEA provisions enacted by the Dodd-Frank Act. Congress plainly recognized that without cross-border application, the Title VII framework would be ineffective, as banks would relocate their transactions around the globe with little more than a keystroke.

Thus, enjoining the cross-border application of Title VII Rules would conflict with the letter and intent of the Dodd-Frank Act. As a profoundly damaging consequence, it would "debilitate Congress's and the CFTC's four years of efforts to create order in these financial markets and to protect U.S. taxpayers from the prospect of further bailouts and future crises." CFTC Mot. to Hold in Abeyance, at 2.

II. Section 15(a) only requires the CFTC to consider "action[s] of the Commission;" it does not authorize, let alone require, the CFTC to second-guess the actions of Congress.

Contrary to the Plaintiffs' assertion, the CFTC was under no obligation to apply Section 15(a) to the cross-border application of any of the 14 challenged rules. On its face, Section 15(a) only requires that the CFTC "consider the costs and benefits of **the action of the Commission**." 7 U.S.C. § 19(a)(1) (emphasis added). Yet the decision to extend the protections set forth in those rules to international derivatives activities **was made by Congress** when it adopted Section 2(i). Accordingly, the Section 15(a) requirements do not apply to the cross-border aspects of those rules.

The basis for this limitation in Section 15(a) is clear. Agencies cannot be asked to second-guess the judgments of Congress, in the guise of demands for "cost-benefit analysis." This case perfectly illustrates the point. As Section 2(i) reflects, Congress determined that the application of the Title VII derivatives regime to cross-border activities was appropriate and necessary to help protect the public, our financial markets, and ultimately our economy from another financial crisis. It did so fully aware that applying the new regulatory regime to cross-border transactions would impose costs on the banks and other market participants who engage in international derivatives. The Plaintiffs insist that the CFTC should have re-considered that congressional determination, but such an exercise would be inappropriate, since it would entail re-evaluating and potentially overturning policy choices about costs and benefits that Congress has already made.

III. Even when Section 15(a) does apply, it only requires a consideration of various factors in light of the public interest, something far different from a cost-benefit analysis.

Even if Section 15(a) were somehow deemed applicable to the Title VII Rules or the Guidance—and it is not—the Plaintiffs' insistence that the CFTC conduct a "cost-benefit analysis" goes far beyond what the CEA actually requires.

A. The obligation to "consider" certain factors is a statutorily-limited duty conferring broad discretion on the CFTC.

Section 15(a) directs the CFTC to "consider the costs and benefits of [its] action" and "evaluate" those considerations in light of five enumerated "considerations." The Supreme Court has long recognized that when statutorily-mandated considerations are not "mechanical or self-defining standards," they "imply wide areas of judgment and therefore of discretion." *Sec'y of Agric. v. Cent. Roig Ref. Co.*, 338 U.S. 604, 611-12 (1950). According to this Circuit, where

"Congress did not assign the specific weight the [agency] should accord each of these factors, [it] is free to exercise [its] discretion in this area." *N.Y. v. Reilly*, 969 F.2d 1147, 1150 (D.C. Cir. 1992); *see also Brady v. FERC*, 416 F.3d 1, 6 (D.C. Cir. 2005). Indeed, when an agency must "consider" certain factors during rulemaking, a reviewing court's role is limited. Courts are not to find a rule arbitrary and capricious under the APA, 5 U.S.C. § 706(2)(A), unless the agency "wholly failed" to consider an enumerated factor. *Pub. Citizen v. Fed. Motor Carrier Safety Admin.*, 374 F.3d 1209, 1216 (D.C. Cir. 2004).[4]

B. Section 15(a) contains no language requiring cost-benefit analysis.

In Section 15(a), Congress also **refrained** from using language that would require the CFTC to engage in cost-benefit analysis. The Supreme Court has declared that an agency's duty to conduct cost-benefit analysis is not to be inferred lightly or without a clear indication from Congress. *Am. Textile Mfrs. Inst., Inc. v. Donovan*, 452 U.S. 490, 510-512 & n. 30 (1981) ("Congress uses specific language when intending that an agency engage in cost-benefit analysis."). Therefore, when Congress intends cost-benefit analysis to apply, it explicitly refers to "costs" and "benefits" and specifies the nature of the analysis. *See id.* and statutes cited therein; *see also* 42 U.S.C. § 300g-1(b)(3).[5]

When Congress wants agencies to be free from cost-benefit constraints, it imposes a less burdensome requirement, thus giving overriding importance to particular statutory objectives.[6]

[4] *Public Citizen*, 374 F.3d at 1221, suggested that the agency had to "weigh" costs and benefits even though the statute simply required the agency to "consider" them. However, that suggestion was pure dicta, and it arose from prescriptive language in a separate provision of the applicable statute. *Id.* at 1216.

[5] Legislative proposals seeking to impose a cost-benefit analysis obligation on the CFTC, *see, e.g.*, H.R. 1840, 112th Cong. (introduced May 11, 2011), also support a finding that the CEA does not already mandate cost-benefit analysis. *See Am. Textile Mfrs.*, 452 U.S. at 512 n.30.

[6] Congress is equally clear when it wants an agency to quantify the benefits of a rule. *See, e.g.* 42 U.S.C. § 300g-1(b)(3); *FMC Corp. v. Train*, 539 F.2d 973, 978-979 (4th Cir. 1976). Even

See Whitman v. Am. Trucking Ass'ns., Inc., 531 U.S. 457, 471 (2001) (§ 109(b) of the Clean Air Act "unambiguously bars cost considerations"); *Nat'l Ass'n of Home Builders v. EPA*, 682 F.3d 1032, 1039 (D.C. Cir. 2012) (statutes requiring agencies to "consider" the "economic consequences" or "costs" do not require cost-benefit analysis); *Cent. Ariz. Water Conservation Dist. v. EPA,* 990 F.2d 1531, 1542 n.10 (9th Cir. 1993) (42 U.S.C. § 7491(g)(1) requiring "consideration" does not require a cost-benefit analysis). Courts respect these congressional choices, and even when a statute refers to "costs" and "benefits," they refuse to impose a duty to conduct cost-benefit analysis absent language of comparison in the statute. *Am. Petroleum Inst. v. EPA*, 858 F.2d 261, 265 & n.5 (5th Cir. 1988); *Reynolds Metal Co. v. EPA*, 760 F.2d 549, 565 (4th Cir. 1985); *Weyerhaeuser Co. v. Costle*, 590 F.2d 1011, 1045 (D.C. Cir. 1978).

The D.C. Circuit recently confirmed these principles. In *Inv. Co. Inst. v. CFTC*, 720 F.3d 370, 379 (D.C. Cir. 2013), the court made clear that the CFTC's Section 15(a) duty simply to "consider" such factors is a limited one and does not require a cost-benefit analysis: "Where Congress has required 'rigorous, quantitative economic analysis,' it has made that requirement clear in the agency's statute, but it imposed no such requirement here." (Cited authorities omitted). Clearly, the CFTC is not required to balance or quantify the costs and benefits of its rules.[7]

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where an agency has a duty to conduct cost-benefit analysis, this Circuit has recognized that agency "predictions or conclusions" need not be "based on a rigorous, quantitative economic analysis." *Am. Fin. Services Ass'n. v. FTC*, 767 F.2d 957, 986 (D.C. Cir. 1985).

[7] Plaintiffs rely on three decisions from this Court that address the **SEC's** duty to assess the economic consequences of its rules. *Bus. Roundtable v. SEC*, 647 F.3d 1144 (D.C. Cir. 2011); *Am. Equity Life Ins. Co. v. SEC*, 613 F.3d 166 (D.C. Cir. 2010); *Chamber of Commerce v. SEC*, 412 F.3d 133 (D.C. Cir. 2005). *See, e.g.*, Pls.' Mot. at 20-21. However, those cases are distinguishable. First, the language and structure of the statutory provisions in the securities laws is different from Section 15(a). Second, those panels never expressly held the SEC had a duty to conduct "cost-benefit analysis." To the extent those decisions could be read as requiring such a duty, or any duty more onerous than what Congress actually imposed, that interpretation would

C. <u>The five factors in Section 15(a) further demonstrate Congress's primary concern with protecting the public, not limiting industry costs.</u>

All five factors in Section 15(a) relate to a public benefit arising from a robustly regulated marketplace, including preventing abuse, promoting competition, enhancing transparency, and limiting systemic risk. None mentions any industry-focused concerns, such as compliance costs or the feasibility of conforming to rule requirements. *Compare* 42 U.S.C. § 300g-1(b)(3)(C); 42 U.S.C. § 6295(d) (1976 ed., Supp. II). Removing any doubt, the fifth factor references "any other public interest considerations." 7 U.S.C. § 19(a)(2)(E). Under principles of statutory construction, each prior factor derives its meaning from this factor: the public interest. *See Neal v. Clark*, 95 U.S. 704, 708-09 (1877).[8]

D. <u>Any consideration of the costs and benefits of rules implementing financial reform must take into account the overriding goal of preventing another crisis.</u>

Whenever the CFTC even considers costs and benefits under Section 15(a), it must adopt a holistic approach that takes into account the enormous collective benefit that the Title VII rules will provide: helping to prevent another devastating financial crisis. This perspective is required under Section 15(a) **and** the Dodd-Frank Act. Section 15(a) includes a broad mandate that the CFTC shall consider "**any other public interest considerations**." 7 U.S.C. § 19(a)(2)(E) (emphasis added). Today, as our economy still struggles to recover from the financial crisis, the

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not be entitled to precedential weight. "Questions which merely lurk in the record, neither brought to the attention of the court nor ruled upon, are not to be considered as having been so decided as to constitute precedents." *Webster v. Fall*, 266 U.S. 507, 511 (1925); *Honeywell Int'l, Inc. v. EPA*, 374 F.3d 1363, 1374 (D.C. Cir. 2004). In **none of those cases** did the parties argue or the panels address the judicial precedents that interpret "consider" as imposing a limited duty, that require explicit statutory language before finding that cost-benefit analysis applies, and that recognize cost-benefit analysis can impede the achievement of regulatory objectives. *See* CBA Report, *supra* 3, at Appendix B.

[8] Even Executive Orders have carefully and expressly avoided imposing cost-benefit analysis on the independent regulatory agencies such as the CFTC. Executive Order 13,579, 76 Fed. Reg. 41,587 (July 14, 2011); Executive Order 13,563, 76 Fed. Reg. 3,821, § 7 (Jan. 21, 2011); Executive Order 12,866, 58 Fed. Reg. 51,735, § 3(b) (Oct. 4, 1993).

most compelling public interest is preventing another crisis.

The Dodd-Frank Act also calls for this perspective. The overriding objective of a law confers broad discretion on an agency as it considers the costs and benefits of a rule necessitated by that law. *See FMC Corp.*, 539 F.2d at 978-79; *see also Fla. Manufactured Hous. Ass'n v. Cisneros*, 53 F.3d 1565, 1578 (11th Cir. 1995). The objective of the Dodd-Frank Act is "[t]o promote the financial stability of the United States" to prevent another financial crisis. Dodd-Frank Act, Preamble. Congress's intent was unmistakable from the breadth and depth of the law: Fundamentally change the regulatory structure so our financial markets can never again generate the levels of risk, recklessness, and abusive conduct that triggered the financial crisis.

The benefits of avoiding another financial crisis are enormous. By conservative estimates, the ongoing crisis will cost **at least $12.8 trillion**. BETTER MARKETS, THE COST OF THE WALL STREET-CAUSED FINANCIAL COLLAPSE AND ONGOING ECONOMIC CRISIS IS MORE THAN $12.8 TRILLION (2012);[9] *see also* GAO, FINANCIAL REGULATORY REFORM: FINANCIAL CRISIS LOSSES AND POTENTIAL IMPACTS OF THE DODD-FRANK ACT, GAO-13-180, 17 (Jan. 2013).

The Title VII Rules and the Guidance are essential components of the new regulatory framework designed to prevent a recurrence of these staggering costs. Any actual burdens the Plaintiffs could possibly attribute to cross-border implementation of those rules would pale in comparison to the damage that will be done if the Plaintiffs succeed in this case and the banks are once again given free rein to do as they please in the derivatives markets.

CONCLUSION

For the foregoing reasons, Better Markets requests that the Court uphold the Guidance and the cross-border application of the Title VII Rules.

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[9] *Available at* http://bettermarkets.com/sites/default/files/Cost%20Of%20The%20Crisis.pdf.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of this *Brief of Better Markets, Inc. as Amicus Curiae in Support of Defendant Commodity Futures Trading Commission* was served this 19th day of March, 2014, upon counsel for the parties and counsel for the *Amicus Curiae* in support of Plaintiffs, via the Court's CM/ECF electronic filing system, as follows:

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