July 3, 2013

The Honorable Gary Gensler
Chairman
Commodity Futures Trading Commission
1155 21st Street, N.W.
Washington, D.C. 20581

The Honorable Mary Jo White
Chair
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

Re: June 27, 2013 Letter from 35 Members of Congress urging delay in cross-border regulation

Dear Chairman Gensler and Chair White:

We are writing to express our concerns regarding a letter sent to you on June 27, 2013 by 35 members of the U.S. House of Representatives regarding the cross-border regulation of derivatives ("Letter"). As explained below, the Letter fails to note a number of material facts essential to a full and accurate understanding of the issues.

OVERVIEW

With respect to harmony among U.S. regulators, there are compelling reasons why the recently proposed rule of the Securities and Exchange Commission ("SEC") is inapplicable as a model for the Commodities Futures Trading Commission ("CFTC"). First, as a legal matter, the CFTC and the SEC are subject to fundamentally different statutory mandates. Second, the CFTC has jurisdiction over more than 96.5 percent of the derivatives markets, while the SEC oversees less than 3.5 percent. Third, the CFTC has been considering cross-border regulation for more than 2 ½ years, has received and reviewed more than 322 comment letters, and proposed its guidance a year ago, whereas the SEC only recently proposed its 650 page rule in May and will require a substantial amount of time to finalize its approach.

With respect to harmony between U.S. and foreign regulators, the Letter ignores several key points. First, the Dodd-Frank Act **requires** the CFTC to apply Title VII provisions to cross-border transactions, subject to the jurisdictional limitations set forth in the law. Second, both the CFTC and the SEC have already sought to promote harmony in international regulation by adopting the concept of "substituted compliance." Third, there are in fact no existing conflicts between U.S. derivatives regulation and foreign rules.

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Finally, any delay in finalizing the CFTC's guidance (or the SEC's proposed rule) on cross-border regulation will only expose U.S. taxpayers to unjustifiable risks, potentially for years to come.

In short, the CFTC should delay no more and the SEC should follow its process as appropriate. Neither should be held hostage to the other, or to the international regulatory process.

Five years ago now, the American people suffered the worst financial crash since 1929 and are still suffering from the worst economy since the Great Depression. The human and monetary costs inflicted on the American people have been enormous, ultimately totaling more than $12.8 trillion. Given that much of this was caused by cross-border derivatives trading and investments, it is already past time for the CFTC to protect the American people by finalizing its guidance.

The SEC's proposed rule on cross-border regulation is no justification for the CFTC to weaken or delay its own approach

The SEC's proposed rule is based on fundamentally different legal authority

In Title VII of the Dodd-Frank Act, the SEC was given very limited statutory authority, relating solely to anti-evasion, and no affirmative mandate regarding cross-border jurisdiction. In stark and clear contrast, the CFTC was given the same anti-evasion authority **plus** an affirmative statutory mandate to regulate cross-border derivatives activities that "have a direct and significant connection with activities in, or effect on, commerce of the United States." (*Compare* DFA Section 772 (b) [SEC] *with* Section 722(d) [CFTC], attached as Exhibits 1 and 2).

Thus, the SEC's proposed rule has no bearing on the CFTC's statutory mandate to regulate the risks from cross-border derivatives trading and related activities (as distinguished from their shared desire to prevent evasion).

The SEC oversees an extremely small segment of the derivatives market

The CFTC's broader statutory mandate makes sense because the CFTC has decades of experience in regulating derivatives, and it has jurisdiction over virtually the entire derivatives market. In fact, the CFTC has jurisdiction over more than 96.5 percent of the combined swaps and security-backed-swaps markets.[1] In contrast, the SEC has jurisdiction over no more than 3.5 percent of those markets (see attached Exhibit 3).

To argue that the CFTC should follow the SEC's recently proposed rule under such circumstances is to ignore this reality. It would be as if the SEC were called upon to defer to the CFTC to set the regulatory standards for all mutual funds simply because the CFTC required less than 1 percent of mutual funds to also register as a CPO. That would be

[1] BIS Annual derivatives market report, 2012. If either DTCC or CFTC-reported data were used, the SEC portion of the markets would decrease to less than 3 percent. *See, e.g.* http://dtcc.com/products/consent.php?id=tiwd/products/derivserv/data/index.php.

entirely inappropriate, of course, and it should not be permitted in connection with cross-border derivatives regulation.

The CFTC has fully considered its cross-border guidance for 2 ½ years, while the SEC is just beginning the process

It would be irresponsible for the CFTC to wait for the SEC, even as to its very limited anti-evasion provisions. As you know, the SEC just proposed a rule regarding the anti-evasion cross-border provisions on May 1, 2013. Comments are not due until August 21, 2013. Moreover, given the sprawling 650 page proposal, an extension substantially beyond that deadline is likely.

In contrast, the CFTC has had 2 ½ years of meetings, consideration, and deliberation regarding the guidance, as well as virtually unlimited input from industry and others. Indeed, the CFTC worked for 1½ years before proposing its initial guidance in June 2012 and then worked for another 6 months before issuing further guidance in December 2012. At the same time that it issued the further guidance in December 2012, the CFTC also issued an exemptive order, pushing back the effective date for yet another seven months, to July 12, 2013. The CFTC has received and considered at least 322 filed comment letters and had dozens of meetings.

Thus, the CFTC has thoroughly considered the cross-border guidance and has already delayed its effective date multiple times. The time for delay is over and the timing of the SEC's rule is irrelevant.

The Letter also ignores several key points regarding international harmony in cross-border regulation

The CFTC has a duty to apply Title VII to cross-border transactions

Like many who urge the CFTC and the SEC to weaken or delay the implementation of cross-border regulation to accommodate international regulatory standards, the Letter overlooks a number of important considerations.

First, the CFTC has a legal obligation under the Dodd-Frank Act to apply the Title VII reforms to cross-border activity whenever that activity has a "direct and significant connection with" or "effect on" U.S. commerce. The CFTC cannot ignore this plain duty at the behest of those who seek greater regulatory harmony.

The CFTC, as well as the SEC, have already sought to promote regulatory harmony through substituted compliance

Second, both the CFTC and the SEC have "consulted and coordinated" with foreign regulatory authorities, in accordance with the Dodd-Frank Act, and one consequence is the willingness of both agencies to adopt the concept of substituted compliance. Accordingly, both the CFTC and the SEC have already acted to promote regulatory harmony by allowing

compliance with foreign laws and regulations to satisfy U.S. requirements under certain circumstances.[2]

Asking the CFTC or the SEC to further weaken their regulation of cross-border activity in the name of harmony cannot be justified. No one should be comforted by anyone's claim that foreign regulators can and will protect American taxpayers. The crisis revealed that foreign regulators, and European regulators in particular, were unable to protect their own depositors, taxpayers, and treasuries. The banks that were nationalized in Europe, many exceeding the GDP of the entire country, have saddled their taxpayers with trillions of dollars in liabilities.

Moreover, foreign regulators have a conflict of interest in enforcing strong rules against U.S. derivatives dealers. If they adopt weaker rules, laws, or enforcement, then U.S. firms will move their business, jobs, and revenues overseas, while the bill for their recklessness will be sent back to the U.S., as it was in the cases of AIG, Lehman Brothers, Citigroup, Bear Stearns, and so many others. Hence, while a substituted compliance regime that incorporates strong comparability standards may be appropriate,[3] ceding any additional protections to foreign regulators would be hazardous and unacceptable.

There is in fact no current conflict between U.S. and foreign rules on derivatives regulation

Third, there is no current conflict with international laws regarding Title VII. That is largely because the United States in general and the CFTC in particular are years ahead of foreign governments and regulators in passing laws and regulations comprehensively governing derivatives.

As we understand it, the CFTC's office of the general counsel performed a comprehensive review of derivatives laws in Europe and elsewhere ("Review"). That Review identified no conflicts with Title VII or CFTC regulations. We have been informed that the Review was shared with the European Commission (and presumably other foreign regulators), who confirmed the absence of any conflicts. In addition, we have learned that the Review (which we have not seen) was shared with several prominent Wall Street derivatives dealer banks and their expert representatives and that they too agreed with the Review's conclusion that there were no conflicts.

The fact that other jurisdictions have not yet passed laws or implemented regulations means that the field is open for the U.S. to continue to lead the way. Let others follow, ideally with equally strong or stronger rules. If there are conflicts later, then the

[2] We believe that the SEC has not done enough in its Proposed Rule to ensure that the test for allowing substituted compliance is sufficiently rigorous, and we will offer our views on that subject when we comment on the SEC's proposal.

[3] As we set forth in one of our comment letters to the CFTC: if there is to be substituted compliance, it must be on a rule by rule basis and be comparable in form, substance, enforcement and over time. *See* Better Markets Comment Letter "Proposed Interpretive Guidance and Policy Statement: Cross-Border Application of Certain Swaps Provisions of the Commodity Exchange Act" (August 27, 2013) *available at* http://bettermarkets.com/sites/default/files/CFTC-%20CL-%20Cross%20Border%20Application%20of%20swaps%20provisions%208-27-12.pdf, incorporated here as if fully set forth.

CFTC can address them later. All such claims of conflicts now are hypothetical and speculative, and they do not constitute a legitimate basis for policy making (or for any delay in making policy).

Waiting for foreign regulators to fully implement derivatives regulation will only expose U.S. taxpayers to years of unjustifiable risk

The development of derivatives regulation in Europe is lagging far behind the U.S. effort. While the European Markets and Infrastructure Regulation ("EMIR") has been passed, it has not yet been implemented. Furthermore, it addresses only a limited set of regulations, which deal only with clearing and data reporting. Comprehensive Dodd-Frank Title VII-like regulation in the European Union is still years away. MiFID2 and MiFIR, which govern execution, trading, position limits, and other issues, will not be finalized for years.

Europe has years to go and many hurdles to overcome in a convoluted process that has many parties pulling in many different directions.[4] It would be indefensible to condition the protection of the American people on those actions, which will only be final at some indeterminate time in the future.

Now is the time for the CFTC to finalize its cross-border guidance, triggering a regulatory race-to-the-top to protect the people of the United States and the globe from another derivatives-ignited financial disaster. The SEC too should proceed as quickly as possible to finalize a strong cross-border rule, so that all participants in the security-based swap market also benefit from the reforms mandated under the Dodd-Frank Act.[5]

The costs to the United States of the last financial crisis have been staggering and must be prevented from happening again

Too much of the financial reform discussion is antiseptic, academic, bloodless, and ahistorical. Too many critics focus on each regulation as if it were an end in itself. The purpose of a regulation, its connection to comprehensive reform, and the financial and economic crises giving rise to it are almost never mentioned, particularly by those importuning the regulators to write rules that protect or enhance their business lines and profits.

The financial crash of 2008 was the worst financial collapse since 1929 and it ushered in the worst economy since the Great Depression. The ongoing costs of those historic events to the people, communities, and government of the United States will be more than $12.8 trillion over ten years (not including the costs of the Fed's zero interest

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[4] *See*, *e.g.*, "Hard Bargaining starts on MiFID2," Financial Times, Philip Stafford, June 18, 2013, *available at* http://www.ft.com/intl/cms/s/0/9c774aee-d800-11e2-9495-00144feab7de.html#axzz2X5r5Nt2D .

[5] The need for the SEC to put anti-evasion regulations in place and to police the securities based swaps market as fast as possible was reinforced by yet another global scandal of the big derivatives dealers rigging the CDS markets. *See* "EU Accuses 13 Banks of Hampering CDS Competition, Bloomberg, Ben Moshisnky, Abigal Moses, and Stephanie Bodoni, July 1, 2013, *available at* http://www.bloomberg.com/news/2013-07-01/eu-accuses-13-investment-banks-of-hampering-cds-competition.html.

rate policy and asset purchases, all of which have been necessitated by the massive damage done by the financial collapse).[6]

Of course, the dollar cost, almost unimaginably large, will still never capture the human suffering and economic wreckage inflicted on our country from coast to coast by the financial and economic crises. Financial reform in general and Title VII in particular were passed to prevent that from happening again. The regulation of cross-border derivatives trading and activities that have a direct and significant effect on the U.S. are an essential part of that framework.

CONCLUSION

After 2 ½ years of consideration, and massive and unlimited input from Wall Street and others, it is time for the CFTC to protect the American people now from high risk cross-border derivatives trading that has a direct and significant impact on the U.S. In addition, the SEC should proceed with its recently proposed rule, receive and review all comments, deliberate as to how best to regulate its share of the market, and finalize its rule as expeditiously as possible.

Better Markets appreciates your consideration of these facts.

Sincerely,

Dennis M. Kelleher
President and CEO

[6] *See* BETTER MARKETS, THE COST OF THE WALL STREET COLLAPSE AND ONGOING ECONOMIC CRISIS IS MORE THAN $12.8 TRILLION (Sept. 15, 2012), *available at* http://bettermarkets.com/sites/default/files/Cost%20Of%20The%20Crisis.pdf.

CC: The Honorable Scott D. O'Malia, Commissioner, Commodity Futures Trading Commission
The Honorable Jill Sommers, Commissioner, Commodity Futures Trading Commission
The Honorable Bart Chilton, Commissioner, Commodity Futures Trading Commission
The Honorable Mark Wetjen, Commissioner, Commodity Futures Trading Commission
The Honorable Elisse Walter, Commissioner, Securities and Exchange Commission
The Honorable Luis A. Aguilar, Commissioner, Securities and Exchange Commission
The Honorable Troy A. Paredes, Commissioner, Securities and Exchange Commission
The Honorable Daniel M. Gallagher, Commissioner, Securities and Exchange Commission
The Honorable Brad S. Schneider, U.S. House of Representatives
The Honorable John Carney, U.S. House of Representatives
The Honorable Jim Himes, U.S. House of Representatives
The Honorable Ron Kind, U.S. House of Representatives
The Honorable Suzan DelBene, U.S. House of Representatives
The Honorable John B. Larson, U.S. House of Representatives
The Honorable Bill Owens, U.S. House of Representatives
The Honorable Derek Kilmer, U.S. House of Representatives
The Honorable Dan Maffei, U.S. House of Representatives
The Honorable Patrick Murphy, U.S. House of Representatives
The Honorable Gerald E. Connolly, U.S. House of Representatives
The Honorable Sean Patrick Maloney, U.S. House of Representatives
The Honorable Denny Heck, U.S. House of Representatives
The Honorable Juan Vargas, U.S. House of Representatives
The Honorable Elizabeth Esty, U.S. House of Representatives
The Honorable Gary Peters, U.S. House of Representatives
The Honorable Mike Quigley, U.S. House of Representatives
The Honorable John Delaney, U.S. House of Representatives
The Honorable Terri Sewell, U.S. House of Representatives
The Honorable Rick Larsen, U.S. House of Representatives
The Honorable Pedro Pierluisi, U.S. House of Representatives
The Honorable John Barrow, U.S. House of Representatives
The Honorable Allyson Y. Schwartz , U.S. House of Representatives
The Honorable Jim Matheson, U.S. House of Representatives
The Honorable Kyrsten Sinema, U.S. House of Representatives
The Honorable Gregory W. Meeks, U.S. House of Representatives
The Honorable Grace Meng, U.S. House of Representatives
The Honorable Gwen Moore, U.S. House of Representatives
The Honorable Jared Polis, U.S. House of Representatives
The Honorable Mike McIntyre, U.S. House of Representatives
The Honorable David Scott, U.S. House of Representatives
The Honorable Steve Israel, U.S. House of Representatives
The Honorable Ann Kirkpatrick, U.S. House of Representatives
The Honorable Ann McLane Kuster, U.S. House of Representatives
The Honorable Bill Foster, U.S. House of Representatives

EXHIBITS ATTACHED BELOW

Exhibit 1: SEC Statute:

"(c) Rule of construction. No provision of this title [15 USCS §§ 78a et seq,] that was added by the Wall Street Transparency and Accountability Act of 2010, or any rule or regulation thereunder, **shall apply** to any person insofar as such person transacts a business in security-based swaps **without the jurisdiction of the United States, unless** such person transacts such business in contravention of such rules and regulations as the Commission may prescribe as **necessary or appropriate to prevent the evasion of any provision of this title** [15 USCS §§ 78a et seq,] that was added by the Wall Street Transparency and Accountability Act of 2010…."

Section 772(b) of the DFA

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Exhibit 2: CFTC Statute:

"(i) Applicability. The provisions of this Act relating to swaps that were enacted by the Wall Street Transparency and Accountability Act of 2010 (including any rule prescribed or regulation promulgated under that Act), **shall not apply to activities outside the United States unless** those activities—

(1) have a direct and significant connection with activities in, or effect on, commerce of the United States; or

(2) contravene such rules or regulations as the Commission may prescribe or promulgate as are **necessary or appropriate to prevent the evasion of any provision of this Act** that was enacted by the Wall Street Transparency and Accountability Act of 2010."

Section 722(d) of the DFA

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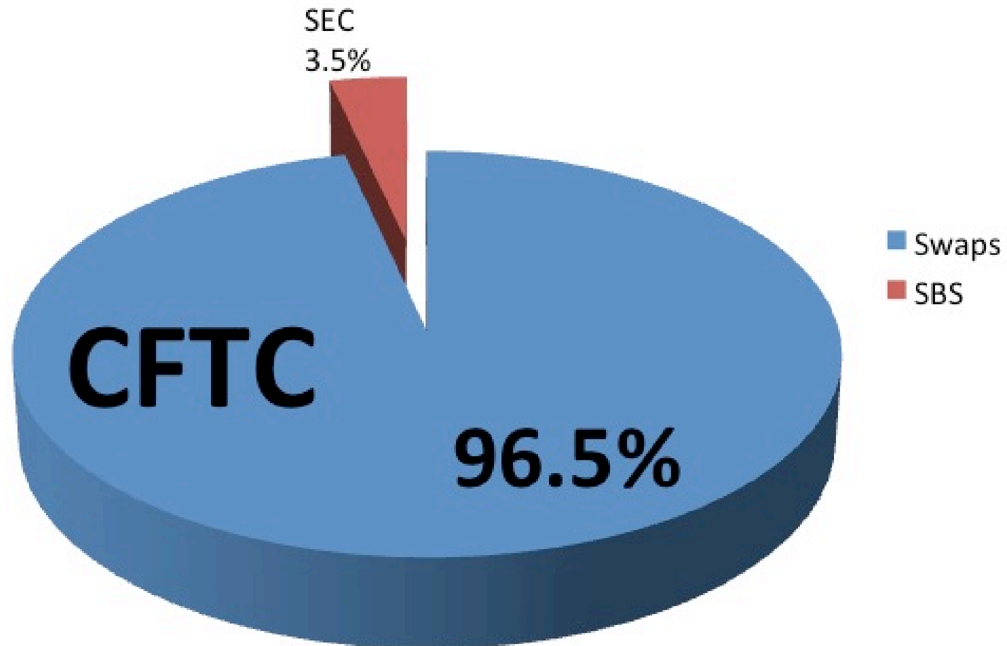
Relative Proportions of Swaps and Security Based Swaps



Source: BIS Annual derivatives market report, 2012. Note, if either DTCC data or CFTC-reported data were used, the SEC portion of the market would be under 3%. Thus, 3.5% is the maximum.

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