IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

INVESTMENT COMPANY INSTITUTE and CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA, Plaintiffs, v. UNITED STATES COMMODITY FUTURES TRADING COMMISSION, Defendant.	Civil Action No. 1:12-cv-00612 (BAH)

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 respectfully submits this brief in support of Defendant Commodity Futures Trading Commission's ("CFTC") Cross-Motion for Summary Judgment, Opposition to Plaintiffs' Motion for Summary Judgment, and Motion to Dismiss in Part.

Better Markets is a non-profit organization founded to promote the public interest in the securities and commodities markets. It advocates for greater transparency, accountability, and oversight in the financial system through a variety of activities, including comment letters on proposed agency rules, public advocacy, litigation, and independent research. Better Markets has an interest in this case because the Court's disposition of the issues presented will profoundly affect three important goals that Better Markets seeks to advance:

(1) enhanced investor protection and market oversight through a registration and reporting regime that is necessary to enable the CFTC to manage systemic risk in the commodity markets and to protect millions of investors from the perils that arise when investment companies trade commodity interests—including **swaps**, the very instruments that were at the heart of the financial crisis of 2008;

(2) the application by regulators and reviewing courts of an economic impact test that accurately reflects the controlling statutory language and Congress's policy choices, rather than a rigid, quantitative, and imprecise cost-benefit analysis, which places undue emphasis on the costs of regulation, and which Congress did not in fact require; and

(3) the successful implementation of comprehensive regulatory reform in accordance with the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (July 21, 2010) ("Dodd-Frank Act") through the adoption of rules, including the rule at issue in this case, that are collectively essential for preventing another financial crisis.

The Plaintiffs are challenging the CFTC's rule, Commodity Pool Operators and Commodity Trading Advisors: Compliance Obligations, 77 Fed. Reg. 11,252 (Feb. 24, 2012) ("Rule"), on multiple grounds, but of greatest concern to Better Markets is their claim that the CFTC failed to conduct an adequate cost-benefit analysis when it promulgated the Rule. A decision invalidating the Rule on this basis would undermine all of the foregoing interests of Better Markets. Such a holding would (1) eliminate the investor protection and market oversight tools that the Rule provides; (2) perpetuate and strengthen the inaccurate view that, under Section 15(a) of the Commodity Exchange Act ("CEA"), 7 U.S.C. § 19(a), Congress intended to burden the CFTC with the costly, time-consuming, and ultimately counter-productive duty to conduct an extensive cost-benefit analysis for each of its rules; and (3) pose a grave threat to the overarching policy objective of financial reform, as a duty to conduct cost-benefit analysis could cripple the agency's ability to finalize its regulatory reforms and to defend its already-implemented rules against court challenges. In this brief, therefore, Better Markets focuses its defense of the Rule on cost-benefit grounds.

SUMMARY OF ARGUMENT

The CFTC fulfilled its duty to consider the costs and benefits of the Rule for the following reasons. First, Section 15(a) of the CEA imposes a limited obligation on the CFTC to **consider** the costs and benefits of its rules in light of five specific factors, **all of which focus on protecting the public interest**. Congress's careful choice of words in Section 15(a), and the case law construing similar provisions, make clear that the CFTC has broad discretion in discharging this duty. The CFTC has no obligation to quantify costs or benefits, weigh them against each other, or find that a rule will confer a net benefit before promulgating it. The rationale for this flexible obligation in the law is clear: requiring the CFTC to conduct a

resource-intensive, time consuming, and inevitably imprecise cost-benefit analysis as a precondition to rulemaking would significantly impair the agency's ability to implement Congress's crucial regulatory objectives in the financial markets.

Second, as the CFTC and any reviewing court considers the costs and benefits of rules implementing financial reform after the devastating 2008 financial crisis, it must give proper weight to Congress's overriding objective embodied in the Dodd-Frank Act. That fundamental objective is to institute a comprehensive set of reforms to prevent another financial collapse and economic crisis, including the enormous financial losses and human suffering they would cause. Therefore, as the CFTC assessed the costs and benefits of the Rule under Section 15(a), it was obligated to consider, above all, the benefits of the entire collection of reforms of which the Rule is an integral part and, consequently, give greater weight to the unquestionable benefit of preventing another crisis. Against the backdrop of the worst financial and economic crisis since the Great Depression, it is inconceivable that the implementation of those essential reforms should hinge on the outcome of a rule-by-rule cost benefit analysis that ignores the overriding purpose of the new regulatory framework—and that gives controlling weight to cost concerns from the very industry responsible for the crisis.

Finally, the CFTC fully satisfied its obligations under Section 15(a), as correctly interpreted. The CFTC amply **considered** the costs and benefits of the Rule. More important, throughout the rulemaking process the agency was guided by an understanding of the need to establish transparency, accountability, and controls on systemic risk throughout our financial system to achieve the ultimate benefit of avoiding another financial and economic crisis—and possible second Great Depression. The CFTC's consideration of the costs and benefits of the Rule was appropriate and should be upheld.

ARGUMENT

I. SECTION 15(A) REQUIRES THE CFTC TO CONSIDER THE COSTS AND BENEFITS OF ITS RULES IN LIGHT OF THE PUBLIC INTEREST, NOT TO CONDUCT A COMPARATIVE OR QUANTITATIVE COST-BENEFIT ANALYSIS.

The CFTC has only a narrow statutory duty to **consider** the costs and benefits of its rules, given the plain wording of Section 15(a) and the absence of any language requiring an exhaustive cost-benefit analysis. It has no obligation to quantify or net the costs and benefits, and it must be guided by the dictates of the public interest, not the burdens of regulation on industry. Congress did not intend to subject the implementation of its regulatory objectives in the commodity markets to the impediments of rigid, quantitative, and ultimately imprecise cost-benefit analysis—a methodology that emphasizes the costs rather than the benefits of regulation.

A. The obligation to "consider" certain factors in the rulemaking process is a statutorily limited duty that confers broad discretion on the CFTC.

The CFTC's obligation to assess the economic impact of its rules is determined first and foremost by what Congress actually required of the agency. Section 15(a) simply directs the CFTC to "consider the costs and benefits of the action of the Commission," and "evaluate" those considerations in light of:

> (A) considerations of protection of market participants and the public; (B) considerations of the efficiency, competitiveness, and financial integrity of futures markets; (C) considerations of price discovery; (D) considerations of sound risk management practices; and (E) other public interest considerations

The language of this provision and the case law construing similar wording make clear that Congress intended the CFTC to have wide discretion in the way it fulfilled this obligation. Where a statute mandates certain considerations without specifying how to evaluate those considerations or the weight they deserve, such as here, courts are to respect an agency's views. In fact, 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 (1950). In *Secretary of Agriculture v. Central Roig Refining Co.,* the Court addressed a statute requiring the Secretary of Agriculture to take three factors "into consideration" when setting import quotas. Even though the Secretary had given "no weight" to one of the factors, the Court had no difficulty upholding his judgment. *Id.* at 610. As the Court explained:

> By way of guiding the Secretary in formulating a fair distribution of individual allotments, **Congress directed him to exercise his discretion "by taking into consideration" three factors**: past marketings, ability to market, and processings to which proportionate shares pertained. Plainly these are not mechanical or self-defining standards. They in turn imply wide areas of judgment and therefore of discretion. . . . Moreover, he is under a duty merely to take "into consideration" the particularized factors. The Secretary cannot be heedless of these factors in the sense, for instance, of refusing to hear relevant evidence bearing on them. But Congress did not think it was feasible to bind the Secretary as to the part his "consideration" of these three factors should play in his final judgment—what weight each should be given, or whether in a particular situation all three factors must play a quantitative share in his computation.

Id. at 611-12; *see also Cent. Ariz. Water Conservation Dist. v. EPA,* 990 F.2d 1531, 1542 n.10 (9th Cir. 1993) (language in 42 U.S.C. § 7491(g)(1) requiring "consideration" does not require a cost-benefit analysis).

The D.C. Circuit Court of Appeals has followed this approach. *See, e.g.*, *Brady v. FERC*, 416 F.3d 1, 6 (D.C. Cir. 2005); *New York v. Reilly,* 969 F.2d 1147, 1150 (D.C. Cir. 1992). As explained by the court in *New York v. Reilly,* 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." 969 F.2d at 1150. Indeed, in the D.C. Circuit, when Congress requires an agency to "consider" certain factors in its rulemaking, a court's role in reviewing the agency's discharge of that duty is extremely limited. Courts are not to find a rule arbitrary and capricious within the meaning of the Administrative Procedure Act, 5 U.S.C. § 706(2)(A), unless the agency has

"wholly failed" to comply with the statutory requirement, or if there is a "complete absence of any discussion of a statutorily mandated factor" in the agency's reasoning. *Pub. Citizen v. Fed. Motor Carrier Safety Admin.,* 374 F.3d 1209, 1216 (D.C. Cir. 2004) (citing *United Mine Workers v. Dole*, 870 F.2d 662, 673 (D.C. Cir. 1989)).[1] Thus, Congress's decision to frame Section 15(a) in terms of a duty to "consider" certain broad factors clearly establishes that the CFTC has wide discretion in how it evaluates the impact of its rules. The Plaintiffs' argument that the CFTC must conduct an exhaustive, comparative, and quantitative cost-benefit analysis in its rulemaking process conflicts with this statutory language and the foregoing case law.

Plaintiffs attach undue significance to the word "evaluate" in Section 15(a). Resorting to the dictionary, they argue that "evaluate" places a "stringent" duty on the CFTC to "determine or set the value of or to determine the significance, worth, or condition of a thing." Pfs' Mem. at 21-22.[2] However, the Plaintiffs ignore the language and structure of the statute. As a threshold matter, "evaluate," both as commonly understood and as defined in the dictionary cited by the Plaintiffs, hardly necessitates a quantitative or comparative analysis. In any event, the alleged nuances of the word are trumped by the structure of Section 15(a) and its repeated reliance on the concept of "considerations"—a term the courts have interpreted specifically in the context of

[1] The court in *Public Citizen*, 374 F.3d 1209, expressed its view that the agency had a duty to "weigh" certain costs and benefits even though the applicable statute simply required the agency to "consider" costs and benefits. However, the court's discussion of cost-benefit analysis was pure dicta. The court made very clear that its holding was based solely on the agency's "dispositive" failure "to consider a statutorily mandated factor—the impact of the rule on the health of drivers." *Id.* at 1216. Further, the court read the cost-benefit obligation in tandem with a separate statutory provision, which required the agency not only to consider costs and benefits, but also to "deal with" a long list of specific issues relating to commercial motor vehicle safety. *Id.* at 1221.

[2] References to "Pfs' Mem." are to Plaintiffs' Memorandum of Points & Authorities in Support of Motion for Summary Judgment filed May 18, 2012. (Doc. # 8.); references to "Df's Mem." are to Defendant's Memorandum in Support of its Cross-Motion for Summary Judgment, in Opposition to Plaintiffs' Motion for Summary Judgment, and in Support of its Motion to Dismiss in Part filed June 18, 2012 (Doc. # 15).

cost-benefit analysis, as discussed above.[3] The core obligation in Section 15(a) is framed simply in terms of the duty to "consider the costs and benefits." Moreover, each of the five factors that bear on the CFTC's analysis is framed as a "consideration." Finally, the Plaintiffs' interpretation of Section 15(a) is also conceptually untenable: as explained below, all five enumerated considerations concern broad public interests, are not amenable to a quantitative analysis, and do not focus on industry costs associated with rulemaking. Thus, the single use of the word "evaluate" as a synonym to create more readable legislative text cannot be used to defeat Congress's explicit, deliberate, and repeated reliance on the longstanding judicially interpreted concept of "consider." Accordingly, under the precedents cited above, the CFTC's statutory duty is limited in scope, and it has enormous discretion in determining how to comply with that duty.

B. The nature of the five factors in Section 15(a) demonstrates that Congress's primary goal is to protect the public interest, not limit the costs of regulation imposed on industry.

The nature of the five considerations in Section 15(a) reflects Congress's primary concern with the need to fashion regulations that serve the public interest and accomplish the agency's mission, not with a need to spare industry the inevitable and routine costs of regulation. Without exception, each factor relates to a public benefit that arises from a robustly regulated marketplace, including preventing abuse, promoting competition, enhancing transparency, and limiting systemic risk. 7 U.S.C. § 19(a)(2).[4] None of the factors mentions any industry-focused

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[3] Under longstanding rules of statutory construction, Congress is presumed to have known these precedents and the interpretation of the words it chooses to use in laws.

[4] The primary focus of Section 15(a) is also evident from its close parallel to the overall public interest objectives of the CEA. According to the findings and purposes section of the CEA, transactions in the commodities markets "are affected with a national public interest." 7 U.S.C. § 5(a). To promote this public interest, the purposes of the CEA include "to protect all market participants," to promote "fair competition," to "prevent price manipulation," and to avoid "systemic risk," 7 U.S.C. § 5 (b). All of these purposes are reflected in Section 15(a). *See also Motor Vehicle*

concerns, such as compliance costs or the feasibility of conforming to rule requirements—factors Congress readily incorporates into statutes when it seeks to strike a different regulatory balance. *Cf.* 42 U.S.C. § 300g-1(b)(3)(C) (requiring analysis of certain costs of safe drinking water regulations including costs that "are likely to occur solely as a result of compliance with the maximum contaminant level, including monitoring, treatment, and other costs"); 42 U.S.C. § 6295(d) (1976 ed., Supp. II) (requiring a weighing of the economic impact on manufacturers and the savings in operating costs as "compared to any increase in the price of, or in the initial charges for, or maintenance expenses of, the covered products which are likely to result").

Removing any doubt, the fifth and final factor requires the CFTC to consider generally "any **other** public interest considerations." 7 U.S.C. § 19(a)(2)(E) (emphasis added). Consequently, in accordance with traditional canons of statutory construction, each of the four prior factors derives their meaning from this fifth factor, the public interest. *See, e.g.*, *Neal v. Clark*, 95 U.S. 704, 708-09 (1877) (relying on the context and proximity of words in a statute to understand their meaning).

Thus, rather than incorporating a list of considerations reflecting the costs and burdens facing industry, or even a balanced mix of industry and public interest factors, Section 15(a) focuses **exclusively** on public interest considerations. The CFTC's own interpretation of its duty under Section 15(a) recognizes the dispositive role of the public interest. In the Proposing Release for the Rule, the CFTC confirmed that "[t]he Commission may in its discretion give greater weight to any one of the five enumerated areas and could in its discretion determine that,

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Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co., 463 U.S. 29, 54-55 (1983) ("Congress intended safety to be the pre-eminent factor under the [National Traffic and Motor Vehicle Safety Act of 1966] and "each standard must be related thereto.").

The Rule at issue in this case is also tied to the public interest through the CFTC's exemptive authority, which is subject to a public interest test. The CFTC exercises its discretionary authority to include or exclude a person from the definition of a CPO only "if the Commission determines that the rule or regulation will effectuate the purposes of the [CEA]." 7 U.S.C. §1(a)(11)(B).

notwithstanding the costs, a particular rule . . . is necessary or appropriate to protect the public interest or to effectuate any of the provisions or accomplish any of the purposes of the CEA." 76 Fed. Reg. at 7,988.

The dominant emphasis in Section 15(a) on the public interest is further evidence that Congress did not intend the CFTC to engage in a mechanical weighing of industry costs and public benefits as if the two elements were of equal importance. In fact, one of the few constraints on the CFTC under Section 15(a) is that it must place the public interest first among its regulatory objectives, and above concerns regarding the costs of regulation.

C. The absence of language in Section 15(a) requiring a comparative or quantitative cost-benefit analysis conclusively refutes any attempt to impose such an onerous burden on the CFTC.

The CFTC's obligation under Section 15(a) is also determined by the conspicuous **absence** of the language Congress uses when it wants an agency to conduct a rigid cost-benefit analysis. Nowhere in Section 15(a) did Congress incorporate language requiring the CFTC to employ a specific methodology, to quantify costs and benefits, or to weigh them against each other as a precondition for promulgating a rule. As decades of congressional action makes clear, Congress carefully chooses economic impact standards. When it wants agencies to apply cost-benefit analysis involving quantification, a specific type of comparative weighing, or net benefit findings, it makes its intention clear.

The absence of such language in Section 15(a) reflects the congressional determination that financial market regulation is a legislative imperative that must not hinge on the outcome of an overly burdensome cost-benefit analysis applied to each implementing rule. Thus, rigorous cost-benefit analysis was never intended to apply to the CFTC and it cannot be established by implication.

Indeed, 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. *See Whitman v. Am. Trucking Assns., Inc.*, 531 U.S. 457, 468 (2001); *Am. Textile Mftrs. Institute, Inc., v. Donovan*, 452 U.S. 490, 510 (1981). That is because such an obligation can profoundly affect an agency's approach to regulation:

> Because benefits can be more accurately monetized in some industries than in others, Congress typically decides whether it is appropriate for an agency to use cost benefit analysis in crafting regulations. Indeed, this Court has recognized that "**[w]hen Congress has intended that an agency engage in cost benefit analysis, it has clearly indicated such intent on the face of the statute.**" *American Textile Mftrs. Institute, Inc., v. Donovan*, 452 U.S. 490, 510, 101 S. Ct. 2478, 69 L. Ed. 2d 185 (1981). Accordingly, we should not treat a provision's silence as an implicit source of cost benefit authority, particularly when such authority is elsewhere expressly granted and it has the potential to fundamentally alter an agency's approach to regulation. Congress, we have noted, "does not alter the fundamental details of a regulatory scheme in vague terms or ancillary provisions--it does not, one might say, hide elephants in mouseholes." *Whitman v. American Trucking Assns., Inc.*, 531 U.S. 457, 468 121 S. Ct. 903, 149 L. Ed. 2d 1 (2001).

Entergy Corp. v. Riverkeeper, Inc., 556 U.S. 208, 238-39 (2009) (emphasis added) (Stevens, J., dissenting).[5]

For decades, Congress has imposed a variety of distinct economic analysis obligations on regulatory agencies to achieve different legislative objectives. When Congress intends cost-benefit analysis to apply, it makes that duty explicit, often requiring a specific weighing or quantification. When Congress does not intend that result, it imposes a rulemaking requirement entirely free of cost-benefit analysis, given the overriding importance of the particular statutory objectives at stake. *See, e.g., Whitman v. Am. Trucking Ass'ns, Inc.*, 531 U.S. 457, 471 (2001) (holding that statute requiring EPA to set air quality standards at a level to protect the public health "unambiguously bars cost considerations"). And, when Congress wants to impose a

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[5] The majority in *Entergy* also recognized the continuing validity of the Court's analysis in *Whitman v. Am. Trucking Ass'ns., Inc.*, and *Am. Textile Mfrs. Institute, Inc. v. Donovan*. *Id.* at 222-23.

limited and flexible obligation on an agency to consider certain cost and benefit consequences of its rules in light of important goals that serve the public interest, such as in Section 15(a), it makes that intention clear, without requiring a comparative or quantitative cost-benefit analysis.

The statutes in which Congress mandates a **balancing** of costs and benefits stand in sharp contrast to Section 15(a). For example, the Flood Control Act, 33 U.S.C. § 701a, one of the earliest examples of a statute requiring cost-benefit analysis, explicitly requires a balancing of enumerated benefits against enumerated costs. Many federal statutes incorporate this same detailed and highly prescriptive language requiring agencies to balance specific costs and benefits. *See, e.g.*, 33 U.S.C. §§ 1312(b)(1)-(2), 1314(b)(1)(B); 33 U.S.C. § 1314(b)(4)(B) (1976 ed., Supp. III); 42 U.S.C. § 6295(c) and (d) (1976 ed., Supp. II); 42 U.S.C. § 7545(c)(2)(B) (1976 ed., Supp. III); 43 U.S.C. § 1347(b) (1976 ed., Supp. III).

Courts refuse to imply a duty to perform specific balancing of costs and benefits when a statute, like Section 15(a), does not explicitly mandate it. In so doing, courts readily distinguish between those statutes that require a balancing of costs and benefits, and those that do not. *See Am. Textile Mfrs. Inst. v. Donovan*, 452 U.S. 490, 512 n.30 (1981); *Reynolds Metal Co. v. EPA*, 760 F.2d 549, 565 (4th Cir. 1985). For example, the Federal Water Pollution Control Act of 1972, 33 U.S.C. § 1314(b)(2)(B), requires the agency to "take into account" direct and indirect costs and other "appropriate" factors in promulgating the best available technology levels. The court in *Weyerhaeuser Co. v. Costle,* 590 F.2d 1011, 1045 (D.C. Cir. 1978), found that this language does **not** require the agency "to use any specific structure such as a balancing test in assessing the . . . factors" nor "to give each . . . factor any specific weight." *See also Cent. Ariz. Water Conservation Dist. v. EPA,* 990 F.2d 1531, 1542, n.10 (9th Cir. 1993); *Am. Petroleum Inst. v. EPA,* 858 F.2d 261, 265 & n.5 (5th Cir. 1988) (contrasting different standards based on

specific statutory language). Thus, the case law confirms what is plain from the statute: Section 15(a) does not include language of comparison and this is conclusive evidence that Congress did not impose a duty to balance costs against benefits.

Similarly, statutes requiring a **quantification** of costs and benefits are worded very differently from Section 15(a). For example, the Safe Drinking Water Amendments of 1996, 42 U.S.C. § 300g-1(b)(3), impose a duty on the Environmental Protection Agency to use analysis of specific factors including the "[q]uantifiable and nonquantifiable health risk reduction benefits," the "[q]uantifiable and nonquantifiable costs" and "[t]he incremental costs and benefits associated with each alternative."

Recognizing these deliberate congressional choices, courts have repeatedly held that an agency need not quantify the costs and benefits of a rule when a statute does not require it. *See, e.g., FMC Corp. v. Train*, 539 F.2d 973, 978-979 (4th Cir. 1976) (finding that 33 U.S.C. §§ 1314(b)(1)(B), (b)(2)(B) and § 1316 do not require quantification of the benefits in monetary terms). In fact, the D.C. Circuit has explicitly recognized that an agency's "predictions or conclusions" do not necessarily need to be "based on a rigorous, quantitative economic analysis." *Am. Fin. Services Ass'n. v. FTC*, 767 F.2d 957, 986 (D.C. Cir. 1985); *see also Pennsylvania Funeral Directors Ass'n v. FTC*, 41 F.3d 81, 91 (3d Cir. 1994) (recognizing that "much of a cost-benefit analysis requires predictions and speculation, in any context," and holding that the "absence of quantitative data is not fatal").

The Plaintiffs rely heavily on three cases from the D.C. Circuit that address the duty of the Securities and Exchange Commission ("SEC") to assess the economic consequences of its rules. Plaintiffs contend that under those decisions, the CFTC must quantify the Rule's costs and benefits, find that the Rule would yield a net benefit, and evaluate the Rule's costs and benefits

in relation to a baseline. *See, e.g.*, Pfs' Mem. at 21-22 (citing *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)). However, those decisions are distinguishable, since the statutes at issue, although similar in some important respects to Section 15(a), are also different. For example, unlike the securities laws, Section 15(a) includes the explicit reference to "other public interest considerations," a uniquely powerful indication that Congress intended to protect the public interest, not minimize industry costs.

In addition, the panels that decided the SEC cases failed to consider the precedents that interpret "consider" as imposing a limited duty, that require explicit statutory language before finding that cost-benefit analysis applies, and that mandate judicial deference to agency judgments. *See* discussion *supra* at Part I, A-C. Those panels also failed to weigh the challenges that cost-benefit analysis presents and its role as an obstacle to effective, efficient, and timely implementation of important policy objectives set by Congress. *See* discussion *infra* at Part I, D. The impact of *Business Roundtable v. SEC*, the most recent decision, illustrates the point. As a direct result of the court's decision, Congress's policy determination in the Dodd-Frank Act that proxy access was an appropriate regulatory measure was nullified. Investors have therefore been deprived of that enhancement in corporate governance. Further, the decision has induced regulatory paralysis at the SEC, slowing its implementation of regulatory reform to a crawl and forcing it to reallocate scarce resources. *See* Jesse Hamilton, *Dodd-Frank Rules Slow at SEC After Cost Challenge*, Bloomberg, Mar. 6, 2012.[6]

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[6] Further, the D.C. Circuit held without basis that the SEC was required to "assess the baseline" level of its statutorily mandated considerations. *Am. Equity Life Ins. Co. v. SEC*, 613 F.3d at 178. Thus, the court not only ignored the prophylactic approach to the SEC's rulemaking and refused to accord appropriate deference to its predictive judgments, *see, e.g.*, Indexed Annuities and Certain Other Insurance Contracts, Final Rule, 74 Fed. Reg. 3138, 3161-3163 (Jan. 16, 2009) ("anticipat[ing]" certain benefits), but also erroneously applied principles of cost-benefit analysis

Congress clearly chose not to require the CFTC to either balance or quantify the costs and benefits associated with its rules. Rather, it elected to impose a limited and flexible duty to "consider" the costs and benefits in light of five factors, with the public interest as the preeminent concern. This reflects Congress's longstanding and considered judgment that the benefits of protecting the public interest in commodity regulation must **not** be subordinated to concerns about the necessary costs of regulation.[7]

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found in inapplicable Executive Orders. In fact, the Plaintiffs suggest, and *amicus* Mutual Fund Directors Forum ("MFDF") insists, that the CFTC and other independent regulatory agencies are subject to the standards of costs benefit analysis imposed by various executive orders. Pfs' Mem. at 24; Brief for the Mutual Fund Directors Forum as *Amicus Curiae*, at 11, filed May 29, 2012 ("MFDF Br.)." This contention is flatly wrong. In fact, the CFTC and all independent regulatory agencies are expressly **excluded** from executive order provisions that require agencies to conduct cost-benefit analysis. For example, Executive Order 12,866, establishing the modern era duty to conduct cost-benefit analysis, expressly excludes all agencies "considered to be independent regulatory agencies." 58 Fed. Reg. 51,735, § 3(b) (Oct. 4, 1993). The two recent executive orders issued in 2011 did nothing to impose any obligation on independent regulatory agencies to conduct cost-benefit analysis. In fact, those orders scrupulously avoided doing so. Executive Order No. 13,563, 76 Fed. Reg. 3,821 (Jan. 21, 2011), expressly excludes the independent regulatory agencies from its scope. *Id.* at § 7. Executive Order 13,579, 76 Fed. Reg. 41,587 (July 14, 2011) ("Order"), addresses the independent agencies, but it does not obligate them to conduct cost-benefit analysis. First, the Order does **not require** independent agencies to do anything. Unlike preceding orders, it uses entirely advisory rather than mandatory language, consistently using "should" rather than "shall." Second, although it encourages agencies to follow certain specified guidelines in prior executive orders, and to conduct retrospective rule review, it carefully excludes from that list any reference to the specific sections dealing with cost-benefit analysis. *Id.* at § 1(c)

[7] The legislative proposals that seek to impose a duty to conduct cost-benefit analysis on the independent regulatory agencies further confirm this view. *See, e.g.*, H.R. 1840, 112th Cong. (introduced May 11, 2011); Financial Regulatory Responsibility Act of 2011, S. 1615, 112th Cong. (introduced Sept. 22, 2011). For example, H.R. 1840 would amend Section 15(a) to require the CFTC to quantify costs and benefits, to refrain from promulgating a rule unless the benefits justify the costs, and to consider a host of new factors aimed at protecting industry rather than the public interest. Courts have found that such proposed legislation is relevant in finding that an agency's current statute does not mandate a specific analysis of a rule's costs and benefits. *See, e.g., Am. Textile Mfrs. Inst. v. Donovan*, 452 U.S. 490, 512, n.30 (1981) (citing a Senator's proposal as evidence that the current law did not require cost benefit-analysis).

D. Requiring a stringent economic analysis under Section 15(a) would thwart the CFTC's ability to implement Congress's regulatory objectives, including, most importantly, the reforms required by and in furtherance of the Dodd-Frank Act.

The fundamental rationale for Congress's determination not to require the CFTC to conduct comparative or quantitative cost-benefit analysis in its rulemaking is clear: It would conflict with, and thereby frustrate, the CFTC's ability to implement Congress's objectives, including regulatory reform.

The process of evaluating the costs and benefits of regulation is complex, speculative, one-sided in its focus on cost, and imprecise. The Office of Management and Budget, the steward of executive branch compliance with cost-benefit analysis, acknowledges the inherent difficulty in quantifying regulatory costs and benefits:

> Many rules have benefits or costs that cannot be quantified or monetized in light of existing information. . . . In fulfilling their statutory mandates, agencies must often act in the face of substantial uncertainty about the likely consequences. In some cases, quantification of various effects is highly speculative.

OMB, 2011 REPORT TO CONG. ON THE BENEFITS AND COSTS OF FEDERAL REGULATIONS AND UNFUNDED MANDATES ON STATE, LOCAL, AND TRIBAL ENTITIES, at 4 (2011).

Thus, under cost-benefit analysis, many advantages of regulation, no matter how important to society or to properly functioning markets, may be disregarded or simply not captured in the calculation. *See Am. Fin. Services Ass'n v. FTC*, 767 F.2d 957, 986 (D.C. Cir. 1985); *Pennsylvania Funeral Directors Ass'n v. FTC*, 41 F.3d 81, 91 (3d Cir. 1994). Further, the process is not only imprecise, it is also enormously time consuming, costly, and resource intensive.

Because of these challenges, the application of cost-benefit analysis can delay or prevent the achievement of the ultimate objectives underlying a statutory scheme, whether it be controlling environmental pollution or ridding the financial markets of systemic risk and abusive

conduct. *See* Thomas J. Miles & Cass R. Sunstein, *The Real World of Arbitrariness Review,* 75 U. CHI. L. REV. 761, 814 n.29 (2008) (citing Stephen Breyer, *Judicial Review of Questions of Law and Policy*, 38 ADMIN. L. 363, 391-93(1986) for the proposition that "judicial requirements of an exhaustive investigation of alternatives may prevent agencies with scarce resources from making even minor changes," and Jerry L. Mashaw & David L. Harfst, *The Struggle for Auto Safety*, at 149-51 (Harvard 1990), for the proposition that the "hard look" judicial review of cost-benefit analysis led the "National Highway Traffic Safety Administration to avoid rulemaking and focus on product recalls").

In fact, critics of cost-benefit analysis have long warned that it is used as a "device not for producing the right kind and amount of regulation, but for diminishing the role of regulation even when it was beneficial." *See* Richard H. Pildes & Cass R. Sunstein, *Reinventing the Regulatory State*, 62 U. CHIC. L. REV. 1, 5-6 (1995). As observed by one court, the imposition of technical and burdensome requirements relating to cost-benefit analysis "serve[s] as a dilatory device, obstructing the agency from proceeding with its primary mission." *FMC Corp. v. Train*, 539 F.2d 973, 978-79 (4th Cir. 1976).

These challenges and uncertainties apply with special force in the context of financial market regulation, where the costs and benefits are often contingent, unpredictable, and exceedingly difficult to quantify. The costs of compliance will often vary greatly depending on how a market participant chooses to adapt to a new regulation. Assessing the benefits of a financial regulation is even more difficult, since it typically involves speculative predictions about injuries to investors or other market participants that are avoided because of the rule. It is impossible to reliably quantify the precise monetary value of the losses that are **never incurred** by investors as a result of a new regulatory protection, or the cascading economic harms that **are**

avoided when financial institutions are subjected to a stronger prudential standard and, as a direct result, do **not** collapse.[8]

On an even larger scale, the ultimate goal and benefit of the comprehensive regulatory regime envisioned under the Dodd-Frank Act is preventing a second Great Depression. While the enormous benefit of avoiding such a calamity can be monetized to a degree, the human suffering it would cause could never be adequately measured in a quantitative cost-benefit analysis. *See* discussion *infra* at Part II, C.

In light of these difficulties, encumbering financial regulators like the CFTC with the duty to conduct rigorous cost-benefit analysis on a rule-by-rule basis would severely hamper, if not defeat, their ability to implement the comprehensive reforms necessary to avert another financial crisis. This is a result that Congress clearly did not intend. After witnessing the financial destruction caused by the crisis and spending trillions of dollars in emergency measures to contain it, Congress determined that the sweeping reforms in the Dodd-Frank Act were essential to protect investors, taxpayers, the financial system, and the economy from another financial disaster. It is inconceivable that Congress would intend the regulatory agencies to

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[8] One reason for the difficulty in quantifying costs and benefits stems from a lack of accessible data: It "doesn't (sic) exist or [it is] in the hands of market participants who don't want to share valuable intelligence." Josh Boak, *Dodd-Frank foes beating path to courthouse door*, POLITICO.COM, Nov. 29, 2011, http://www.politico.com/news/stories/1111/69353.html. Moreover, industry proponents themselves either cannot or will not develop concrete measurements of costs and benefits, preferring instead simply to criticize the analyses performed by the regulatory agencies. That is certainly the case in this Rule challenge. *Amicus* MFDF, for example, ominously warns that the Rule will impose "significant new costs on mutual funds, and these costs will inevitably be passed along to shareholders." MFDF Br. at 2, 7-8. Notwithstanding their apparent expertise in the management and operation of mutual funds—including regulatory compliance—they offer no concrete data or support for these vague but dire predictions. *See also* Df's. Mem. at 56. The same passive and obstructionist tactic in the application of cost-benefit analysis is evident in other rulemakings criticized by industry. *See, e.g.*, Peter Eavis, *Making a Theoretical Case About Volcker,* DEALBOOK N.Y. TIMES, Feb. 14, 2012, http://dealbook.nytimes.com/2012/02/14/making-a-theoretical-case-against-volcker/; John Kemp, *The Trojan Horse of cost benefit analysis*, REUTERS, Jan. 3, 2012, http://blogs.reuters.com/great-debate/2012/01/03/the-trojan-horse-of-cost-benefit-analysis/.

second guess this legislative determination and condition the implementation of such reforms on the outcome of cost-benefit analyses.

II. WHEN CONSIDERING THE COSTS AND BENEFITS OF RULES IMPLEMENTING FINANCIAL REFORM, THE CFTC MUST ALSO CONSIDER CONGRESS'S OVERRIDING GOAL, WHICH WAS TO PREVENT ANOTHER FINANCIAL CRISIS AND THE ENORMOUS COSTS IT WOULD INFLICT.

In considering the costs and benefits of its rules under Section 15 (a), the CFTC must also consider and place the highest importance on the overriding objective of the legislation that motivated the rule. Here, that legislation is the Dodd-Frank Act and its core objective is clear: preventing another financial crisis and avoiding the massive costs that it would impose. As the CFTC implements reforms in accordance with the letter and tenor of the Act, and as courts review those reforms, this larger goal must be considered.

A. The CFTC's obligation to consider Congress's overriding goal of preventing a future crisis derives from Section 15(a) and from the Dodd-Frank Act itself.

The CFTC's duty to consider the collective benefits of the Dodd-Frank Act arises from two sources: Section 15(a) of the CEA and the Dodd-Frank Act itself. As discussed above, Section 15(a) expressly requires the CFTC to consider not only the enumerated aspects of the public interest when it promulgates rules, but also "**any other public interest considerations**." This provision imposes a contextual obligation to consider whatever public interest goals a rule may serve under the conditions prevailing at the time of its promulgation.

The present-day conditions that warrant promulgation of the Rule are abundantly and painfully obvious: Beginning in 2007, the financial system experienced the worst crisis since the Stock Market Crash of 1929 and it triggered the worst economic downturn since the Great Depression, the consequences of which are still being felt to this day. In the aftermath of such a crisis, there is no more compelling public interest than preventing another crisis. The Rule

serves this purpose, and its costs and benefits must therefore be considered in this context, with the larger benefits of avoiding another crisis foremost in mind.

A second compelling rationale for a holistic analysis of the Rule springs from the Dodd-Frank Act itself. The fundamental remedial objective of a law, such as the Dodd-Frank Act, confers broad discretion on an agency as it considers the costs and benefits of a rule that is necessitated, if not mandated, by the statute. In the environmental context, for example, courts have long been guided by Congress's overriding statutory goals as they define the scope of an agency's duty to assess the economic impact of its rules. In *FMC Corp. v. Train,* 539 F.2d 973 (4th Cir. 1976), chemical manufacturers challenged water pollution standards set by the EPA, citing inadequate cost-benefit analysis. The statute simply required the agency to "consider" costs in establishing the standards, but industry representatives claimed that this provision required the agency to both quantify and compare costs and benefits. The Fourth Circuit Court of Appeals rejected the claim, holding that the EPA had extremely broad discretion in assessing the costs of pollution abatement measures, given Congress's overriding purpose in passing the Clean Water Act:

> The Act's overriding objective of eliminating by 1985 the discharge of pollution into the waters of our Nation indicates that Congress, in its legislative wisdom, has determined that the many intangible benefits of clean water justify vesting the Administrator with broad discretion, just short of arbitrary and capricious, in his consideration of the cost of pollution abatement.

Id. 978-79; *see also Florida Manufactured Hous. Ass'n v. Cisneros,* 53 F.3d 1565, 1578 (11th Cir. 1995) (recognizing HUD's broad discretion when considering factors, but also holding that the overarching statutory goal of reducing injuries, deaths, and property damage required HUD to consider the "general societal" benefits of avoiding wind damage to manufactured homes, not just the impact of construction standards on the price of each unit).

A similar analysis applies to the Dodd-Frank Act. There is no question that the Rule is an integral component of the comprehensive set of reforms envisioned by Congress. Although not expressly required under the Act, it is clearly necessary and appropriate in light of the specific provisions and goals of the statute. In the Dodd-Frank Act, Congress gave the CFTC primary and sweeping authority to administer an entirely new regulatory regime governing swaps; expanded the definition of commodity pool operator ("CPO") to encompass swap transactions; imposed new reporting requirements relating to private fund advisers, which present the same "sources of risk" posed by CPOs; and appointed the CFTC as a member of the Financial Stability Oversight Council, tasked with gathering data, monitoring financial markets, and taking appropriate steps to address the accumulation of systemic risk. 77 Fed. Reg. at 11,252-3 (citing Dodd-Frank Act, Titles I, VII and section 204). Thus, "[f]ollowing the recent economic turmoil, and consistent with the tenor of the provisions of the Dodd-Frank," the Commission appropriately reconsidered the level of regulation applicable to entities involved in futures and derivatives transactions—including investment companies—and adopted the Rule. 77 Fed. Reg. at 11, 253. The Rule is thus necessitated by and grounded in the Dodd-Frank Act. Therefore, the CFTC and this Court have wide latitude—indeed, an affirmative obligation—to consider the benefit of the Rule in terms of the benefit conferred by the entire collection of Dodd-Frank reforms.

B. The indisputable objective of the Dodd-Frank Act is avoiding another financial crisis.

The purpose 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. The statute itself reflects this core purpose through its sheer breadth and detail. It addresses weaknesses in every major financial sector, including derivatives, banking, commodities, securities, and insurance. It

establishes an entirely new regulatory framework where none formerly existed in the swaps markets; it fundamentally revises the tools necessary to monitor, limit, and remediate systemic risk; and it expands the existing regulatory structure in the commodities markets. Congress's intent was unmistakable: Fundamentally change the entire regulatory structure so our financial markets can never again generate the levels of risk, recklessness, and abusive conduct that triggered the 2008 financial crisis.

The legislative history is replete with examples describing the Dodd-Frank Act in terms that clearly reflect this overarching purpose. *See, e.g.*, S. REP. No. 111-176, at 2 (2010) (Introduction). Members of Congress consistently recognized the enormous costs of the crisis, and the need "to stop what happened from ever happening again," as the driving forces behind the Act. Senator Dorgan, 156 Cong. Rec. S 5931 (daily ed. July 15, 2010). For example, Senator Dodd, Chairman of the Senate Banking Committee, stated:

> The American public is sitting there in sort of stunned disbelief. Here we all acknowledge this huge problem that needs to be addressed for the 8.5 million people who have lost their job, the 7 million who have lost their homes, their retirement income. We know from the statistics what this financial crisis has caused.

156 Cong. Rec. S 2688 (daily ed. Apr. 27, 2010); *see also* Senator Dorgan, 156 Cong. Rec. S 5931 (daily ed. July 15, 2010).

Senator Carl Levin, Chairman of the Senate Permanent Subcommittee on Investigations, also observed that "for too long, too many firms on Wall Street have had free reign to profit at the expense of their own clients, to engage in the riskiest sorts of speculation, to prosper from their risky bets when they pan out, and to have the taxpayers cover the losses when they do not pan out." 156 Cong. Rec. S 5931 (daily ed. July 15, 2010). The solution was a complete overhaul of the financial system, which Senator Levin declared was necessary to "put an officer

back on the beat on Wall Street so the jobs, homes, and futures of Americans are not again destroyed by excessive greed." *Id.* In this context, it is untenable to claim that the benefits of the Rule, or any other element of the regulatory overhaul, can only be viewed in isolation, divorced from the larger, congressionally envisioned framework.

C. The benefits of avoiding another potentially worse financial crisis are enormous, totaling trillions of dollars.

The value of a stronger and more comprehensive regulatory framework is huge. It includes the benefits of sparing our economy and our society the devastating consequences that a future financial crisis would bring in the form of both monetary losses and human suffering. A reasonable starting point for determining the cost of a future crisis is the cost of the current crisis that began in 2007, reached a crescendo in 2008, and continues to be felt to this day. The impact of that crisis is staggering, as illustrated by the following statistics:

- Gross domestic product ("GDP") has fallen dramatically and it is not expected to return to normal levels until at least 2018. At that time, the cumulative shortfall in GDP relative to potential GDP is expected to reach **$5.7 trillion**. CBO, THE BUDGET AND ECONOMIC OUTLOOK: FISCAL YEARS 2012 TO 2022 at 26 (Jan. 2012).
- The unemployment rate skyrocketed to 10.1% in October of 2009, representing **15.4 million workers**, many of whom have become permanently unemployed. BLS, SPOTLIGHT ON STATISTICS: THE RECESSION OF 2007-2009 (Feb. 12, 2012).
- Government expenditures, including Wall Street bailouts, special lending facilities, unemployment benefits, and the economic stimulus package are well in excess of a trillion dollars. The value of the government's total commitment of support, provided through some 50 separate programs, is estimated at **$23.7 trillion**. OFFICE OF THE SPECIAL INSPECTOR GEN. FOR THE TARP, QUARTERLY REP. TO CONGRESS, 137 (July 21, 2009).

- The national debt will increase by **$8 trillion** by 2018 as a result of the crisis, due to the combined effects of government expenditures and reduced revenues. CBO, THE BUDGET AND ECONOMIC OUTLOOK (Jan. 2008); CBO, THE BUDGET AND ECONOMIC OUTLOOK: AN UPDATE (Aug. 2009).
- The stock market fell by more than 50% in just 18 months, from October 2007 until March of 2009, representing **$11 trillion** in evaporated wealth. FRB OF ST. LOUIS, FRED ECONOMIC DATA, DOW JONES INDUSTRIAL AVERAGE (DJIA) (2011), *available at* https://research.stlouisfed.org/.
- From 2007 to 2010 median family net worth fell 38.8% and median family income fell 7.7%, from $49,600 to $45,800. BOARD OF GOVERNORS OF THE FED. RESERVE SYS., FED. RESERVE BULLETIN VOL. 99 NO. 2, CHANGES IN U.S. FAMILY FINANCES FROM 2007 TO 2010: EVIDENCE FROM THE SURVEY OF CONSUMER FINANCES, at 1, 17 (June 2012). Thus, the financial collapse and the economic crisis it created "**eras[ed] almost two decades of accumulated prosperity**." Binyamin Appelbaum, *Family Net Worth Drops to Level of Early '90s, Fed Says*, N.Y. TIMES, June 11, 2012 (emphasis added).
- Home values have declined 33% since the crisis began, representing **$7 trillion** in lost value. BOARD OF GOVERNORS OF THE FED. RESERVE SYS., WHITE PAPER, THE U.S. HOUSING MARKET: CURRENT CONDITIONS AND POLICY CONSIDERATIONS, at 3 (Jan. 4, 2012).
- A total of **at least 3.6 million** homes—and by some accounts **5 million**—have been lost to foreclosure since the crisis began, with millions of additional foreclosures to come. Corelogic, *CoreLogic Reports 66,000 Completed Foreclosures Nationally in April* (May 30, 2012); *Still Depressed, After All These Years*, N.Y. TIMES, June 23, 2012, at SR12.

- The number of families falling below the poverty line has climbed steadily since 2007, rising from 12.5 to 15.1%, representing over **46 million** individuals now deemed poor. CARMEN DENAVAS-WALT ET AL., U.S. CENSUS BUREAU, INCOME, POVERTY, AND HEALTH INSURANCE COVERAGE IN THE UNITED STATES: 2010, at 14 (Sept. 2011).
- The human anguish caused by the crisis has been enormous and incalculable, encompassing all of the psychological and physical health effects that come with unemployment, poverty, homelessness, delayed retirements, abandoned college educations, increased crime rates, and lost healthcare. *See, e.g.*, Daniel Sullivan & Till von Wachter, *Job Displacement and Mortality: An Analysis Using Administrative Data*, QUARTERLY J. OF ECON., 1265 (Aug. 2009).

It is impossible to quantify all of the consequences of the still-unfolding financial and economic crisis. Moreover, the actual costs of another crisis are almost certain to be far greater than what we have witnessed since 2007, because our fiscal and monetary capacities to institute remedial measures and to absorb the costs of a future crisis are so depleted. With the annual budget deficit now exceeding $1.2 trillion, CBO, THE BUDGET AND ECONOMIC OUTLOOK: FISCAL YEARS 2012 TO 2022, at Summary Table 1 (Jan. 2012), the Treasury will have far fewer fiscal tools at its disposal to manage another financial crisis. This vulnerability will persist for years to come, until something approximating a full recovery has been achieved.

The reform effort, initiated by Congress through the passage of the Dodd-Frank Act, now rests in the hands of the financial regulators who must adopt the necessary rules. Those rules promise an enormous **collective benefit**—avoiding the costs of what we have witnessed since 2007 and what could likely be a second Great Depression—but only if they are implemented on a **collective basis**. As regulators promulgate financial reform regulations, and as courts review

those regulations, they must consider the entire set of reforms envisioned by Congress and the benefits that those reforms can provide as a single, coherent collection. If this approach fails, and if the cohesive framework is unraveled rule by rule on cost-benefit grounds, then the public, the markets, and the economy as a whole will once again be vulnerable to financial downfall.

D. The benefits of preventing another crisis take precedence over the costs to industry, since Congress passed the Dodd-Frank Act knowing that financial reform would necessitate the imposition of significant costs.

Congress determined that the financial industry would have to bear substantial costs to make our financial markets more stable and to ensure that the public would never again have to pay for Wall Street's abuses. Those costs include the elimination of extremely profitable lines of business as well as initial and ongoing compliance costs. For example, the Dodd-Frank Act prohibits bank holding companies from almost all proprietary trading and investing in hedge funds, which has been a source of tens of billions of dollars in annual revenue for the largest banks. The law also provides that many over-the-counter derivatives, such as swaps, must be subjected to enhanced regulatory oversight, exchange trading, and central clearing. This too will require the financial industry to incur significant set-up costs, ongoing compliance costs, margin and collateral costs, and the costs of reduced revenues and profits.

Congress fully understood these consequences. The entire overhaul of the financial system in the Dodd-Frank Act reflects Congress's unflinching determination to increase the financial industry's costs across the board—or, more accurately, to **shift** those costs back to industry from a society that has paid the bill for industry's unregulated excesses. In short, Congress conducted its own cost-benefit analysis and concluded that the enormous collective benefits of financial reform far exceeded the costs and lost profits that industry would have to absorb. *Cf. BASF Wyandotte Corp. v. Costle,* 598 F.2d 637, 657 (1st Cir. 1979) ("Congress

‘self-consciously made the legislative determination that the health and safety gains that achievement of the Act's aspirations would bring to future generations will in some cases outweigh the economic dislocation it causes to the present generation.’”) (citing *Weyerhaeuser Co. v. Costle*, 590 F.2d 1011, 1037 (D.C. Cir. 1978)).

Requiring the financial regulators like the CFTC to subject their rulemaking to a cost-benefit analysis would ignore Congress’s calculation. Indeed, it would threaten to defeat the very purpose of the law and the impetus for the regulation. Congress did not initiate such a vital set of reforms only to have the implementing agencies—or reviewing courts—effectively repeal them out of concern for the imposition of costs that Congress has already determined to impose.[9]

III. THE CFTC COMPLIED WITH ITS OBLIGATIONS UNDER SECTION 15(A) BY CONSIDERING THE COSTS AND BENEFITS OF THE RULE IN LIGHT OF THE OVERRIDING NEED TO AVOID ANOTHER FINANCIAL CRISIS.

The CFTC complied with its statutory duty under Section 15(a). First, the agency **considered** the costs and benefits of the Rule in light of each of the Section 15(a) factors, and second, it appropriately considered the larger benefit of regulatory reform: avoiding a recurrence of the financial crisis.

A. The CFTC complied with Section 15(a) by considering costs and benefits.

As demonstrated throughout the Adopting Release, the CFTC considered a wide range of specific costs and benefits associated with the Rule. *See* Section III. C., 77 Fed. Reg. at 11,275-83. With respect to costs, the Commission catalogued all of the compliance costs that would

[9] One of the arguments advanced by *amicus* MFDF reflects the fundamental failure to appreciate the necessity and proprietary of regulatory costs. MFDF argues that the Rule will prove costly because it will “inevitably lead to a reduction in the variety of investment strategies that can be efficiently offered by a mutual fund.” MFDF Br. at 9. However, upon registering as a CPO—a process that the financial industry has followed in one form or another for nearly a 100 years without detrimental impact—any mutual fund would be unconstrained in its investment strategies. To the extent a fund is unwilling to register, then it would indeed be subject to “costs” in the form of limits on its investment options, but that is precisely the desired result, not an unjustifiable or unintended cost of the Rule.

result from the registration and data collection provisions and the variables that would impact those costs. *See* 77 Fed. Reg. at 11,272-75; 11,277. The agency's qualitative assessment of these administrative costs was directly responsive to commenters, and it addressed the same costs that have drawn the Plaintiffs' criticism. Pfs' Mem. at 35.[10]

The CFTC also detailed the many benefits of the Rule, which include important investor protections and enhanced regulatory tools that will better equip the CFTC to oversee the swaps markets. For example, the CFTC found that the registration provisions would help ensure minimum levels of competency and fitness, which will allow the Commission to better "protect the public and markets from unfit persons and conduct." 77 Fed. Reg. at 11,277; *see also* Chairman Gary Gensler, Statements of Support, Amendments to Compliance Obligations and Harmonization Proposal, Feb. 9, 2012 (recognizing the benefits of bringing commodity pools "that have been in the dark back into the light so that their customers can benefit from CFTC's oversight"). The CFTC also explained that registration of CPOs "provides the Commission and members of the public with a clear means of addressing the wrongful conduct by individuals and entities participating in the derivatives markets." *Id.* at 11,254. By virtue of the Rule, the CFTC will have the authority to take punitive and remedial actions against registered CPOs, and the public will have access to the Commission's reparations programs.[11] 77 Fed. Reg. at 11,277.

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[10] At least one entity that expects to be covered by the Rule has stated that it "does not expect that compliance with CFTC regulations, if required, will materially adversely affect the ability of the Fund to achieve its objective" of obtaining positive absolute returns. AQR Managed Futures Strategy Fund, Fund Summary, May 1, 2012, *available at* http://www.sec.gov/Archives/edgar/data/1444822/000119312512204886/d335207d497k.htm.

[11] *Amicus* MFDF argues that the CFTC failed to identify any "direct investor-protection benefits to shareholders" provided by the Rule. MFDF Br. at 7. This is both false and irrelevant. As described in text, the release details numerous direct benefits that investors will receive from the fitness and competency standards, the CFTC's enhanced enforcement authority, and the remedial procedures available to investors suffering injury at the hands of CPOs. In any case, even if the sole benefit of the Rule was the "indirect" one of helping to contain systemic risk and prevent another crisis, it would be unquestionably justified. It is safe to assume that every one of the 90 million mutual fund

Similarly, the agency found various benefits from the data collections provisions of the Rule. 77 Fed. Reg. at 11,281. For example, the CFTC stated its belief that the data collected from CPOs "increases the amount and quality of information available regarding a previously opaque area of investment activity and, thereby, enhances the ability of the Commission to protect investors and oversee derivatives markets." *Id.* Because the data to be collected by the agency is not otherwise available, the CFTC "will be able to tailor its regulations to the needs of, and risks posed by, entities in the market, and to protect investors and the general public from overly risky behavior." *Id*; *see also* Chairman Gary Gensler, Statements of Support, Amendments to Compliance Obligations and Harmonization Proposal, Feb. 9, 2012 (recognizing the benefits of increasing transparency to regulators through the data collection provisions that "will help the Commission develop further regulatory protections for customers of these entities, market participants and the American public").[12]

The CFTC's rulemaking record also highlighted the importance of these benefits, as applied to investment company CPOs, and mutual funds in particular, by describing the nature and magnitude of the threat that these entities pose to investors and the financial system. The Release cites the petition for rulemaking submitted by the National Futures Association ("NFA"). 77 Fed. Reg. at 11,254 n. 27. The petition indicates that there are "at least three entities filing for exclusions under Regulation 4.5 with respect to registered investment companies that they operate;" that they have the same goal as public commodity pools; that they

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investors in the United States would regard avoiding the 2008 financial crisis as a benefit of enormous and incalculable value, whether labeled "direct" or "indirect."

[12] *Amicus* MFDF suggests that the CFTC harbored an ulterior motive in adopting the Rule and its "true purpose" was "not to improve investor protections" but to "advance the CFTC's own institutional interest in acquiring a source of market information." MFDF Br. at 6, 16. This contention is also false and irrelevant—false because the Rule plainly serves many valuable investor protection purposes, as discussed in text, and irrelevant because even if the CFTC's sole aim was to ensure greater transparency in the commodities and swaps marketplace through data collection, that alone would have justified the Rule.

market themselves to customers, including retail customers, as commodity futures investments; and that they indirectly invest substantially in derivatives and futures products to achieve a managed futures exposure equal to the full net value of the fund. NFA, Petition for Rulemaking to Amend CFTC Regulation 4.5, at 2, Aug. 8, 2010 ("NFA Pet."); *see also* Letter from Senators Carl Levin & Tom Coburn to IRS, at 3 (Dec. 20, 2011) (estimating that 40 and as many as 72 mutual funds circumvent federal regulation in the same manner as those three entities mentioned by NFA).

The Release also explains several major problems with mutual funds being exempt from CPO registration. First, their investments are inherently risky, and even "a relatively small investment in a derivative instrument can expose a fund to potentially substantial gain or loss—or outsized exposure to an individual counterparty." 77 Fed. Reg. at 11,255. Second, without registration with the CFTC, investors are deprived of crucial information that would otherwise be required under the CEA. *See* NFA Pet., at 3 (finding that the three entities "omit[] substantial disclosures that would otherwise be mandated by Part 4."); 77 Fed. Reg. at 11,255. Third, "[s]ince Rule 4.5 is an exclusion rather than an exemption, the anti-fraud provisions of Section 4(o) do not apply," thus depriving investors of important legal protections. *Id*. at 2.

In fact, investment companies acting as unregistered CPOs pose a serious threat to investors: "[i]nvestments in these vehicles can be—and often are—sold to unsophisticated customers." *Id.* Indeed, an estimated 52.3 million U.S. households (or 44%) own shares in mutual funds, with 94% investing for retirement, 48% for emergencies, and 24% for education. ICI, *2012 Investment Company Fact Book: A Review of Trends in the U.S. Investment Company Industry*, at 87 (2012). Without the important registration and data collection provisions of the Rule, these investors are at heightened risk of exploitation at the hands of up to 8,684 mutual

funds that are increasingly inclined to engage in this activity without sufficient oversight. *Id*. at 18; 77 Fed. Reg. at 11,255; *see also CFTC. v. British Am. Commodity Options Corp.*, 560 F.2d 135, 139-140 (2d Cir. 1977) ("Registration is the kingpin in this statutory machinery, giving the Commission the information about participants in commodity trading which it so vitally requires to carry out its other statutory functions of monitoring and enforcing the Act.").

In sum, on the most basic level, the CFTC complied with its Section 15(a) duty, comprehensively reviewing the costs and the crucial benefits of the Rule.[13] *See Pub. Citizen v. Fed. Motor Carrier Safety Admin.,* 374 F.3d 1209, 1216 (D.C. Cir. 2004).

B. The CFTC also considered the benefits of preventing another crisis.

In accordance with Section 15(a), the Dodd-Frank Act, and the relevant case law, the CFTC also considered the core objective that Congress sought to achieve by passing a comprehensive collection of regulatory reforms: preventing another financial and economic crisis. This consideration was implicit in the sense that, at the time it promulgated the Rule, the CFTC was fully cognizant of the damage done by the financial crisis, Congress's resolve to prevent a recurrence of the crisis through the Dodd-Frank Act, and the agency's own duty to promulgate and finalize regulations that fulfill the letter and spirit of the law.

In addition, there is ample evidence in the rulemaking record that the CFTC explicitly considered the need to implement the Rule not only to effectively protect consumers, but also to

[13] The CFTC actually exceeded its duty and "quantified estimated costs and benefits where it [was] reasonably practicable to do so." 77 Fed. Reg. 11,276. For example, the agency listed the $200 registration fee, the $750 annual NFA membership dues, and the $90 examination fee that registrants will incur. 77 Fed. Reg. at 11,273; 11,277. Although neither its statute nor the relevant case law requires such quantification, the CFTC's effort to do so illustrates its good faith attempt to address industry concerns, despite the fact that "[m]any comments addressed the costs and benefits of the proposed rule in *qualitative* terms." *Id*. (emphasis added). *Cf. BASF Wyandotte Corp. v. Costle,* 598 F.2d 637, 657 (1st Cir. 1979) ("There is no way the cost analysis could be more than an estimate, especially given the reticence of the industry to supply information, and EPA needed to develop no more than a rough idea of the costs the industry would incur."); *see also* Df's Mem. at 56.

contribute to the entire regulatory reform effort. The Adopting Release includes the all-important observation that "Congress enacted the Dodd-Frank Act in response to the financial crisis of 2007 and 2008," as well as a finding that the Rule itself would supplement the Act and thus help to prevent a future crisis. 77 Fed. Reg. at 11, 253. The Release also observes that the need to reinstate stronger oversight of CPOs through the Rule was prompted by "the recent economic turmoil" and is "consistent with the tenor of the provisions of the Dodd-Frank Act." 77 Fed. Reg. at 11, 253; *see also id.* at 11,275 ("[T]he Dodd-Frank Act has given the Commission a more robust mandate to manage systemic risk and to ensure safe trading practices by entities involved in the derivatives markets"). Commissioner Scott O'Malia, when voting to adopt the final Rule, also recognized the Rule's benefit in terms of preventing another crisis, stating that "[t]he financial crisis, and now the collapse of MF Global, highlights the need for more accessible and effective consumer protection measures." Statement of Concurrence, Commodity Pool Operators and Commodity Trading Advisors: Amendments to Compliance Obligations, Feb. 2, 2012.

With respect to the specific registration and data collection provisions at issue, the CFTC found that "[t]he sources of risk delineated in the Dodd-Frank Act with respect to private funds [which are regulated by Title IV of the Act] are also presented by commodity pools," *id.,* and that the registration and data collection provisions of the Rule will assist the agency in complying with the spirit and letter of the Title I provisions relating to financial stability. 77 Fed. Reg. 11,252. Consequently, the agency stated that the necessary data collection provisions of the Rule will yield the benefits of "risk mitigation as it pertains to the overall financial stability of the United States," which although not quantifiable, "is significant insofar as the Commission may be able to use this data to prevent further future shocks to the U.S. financial

system." 77 Fed. Reg. at 11,281; *see also* 76 Fed. Reg. at 7980 (The required forms reflect a number of factors, including "the purpose and requirements of the Dodd-Frank Act").

Similarly, Title VII of the Dodd-Frank Act expanded the CFTC's authority over swaps and amended the definitions of "commodity pool" and "commodity pool operator" to include entities that trade swaps. 77 Fed. Reg. at 11,258. Thus, the inclusion of swaps with respect to the registration and data collection provisions will help ensure that the CFTC can effectively oversee this previously opaque investment activity. *See* 77 Fed. Reg. at 11,252; 11,256; 11,258. Chairman Gary Gensler also emphasized the Rule's inclusion of swaps trading as "consistent with the [Act]" and that "[i]f CPOs and CTAs are trading swaps, they will have to register with the Commission, giving their customers the benefit of the protections in the Dodd-Frank Act." Statements of Support, Amendments to Compliance Obligations and Harmonization Proposal, Feb. 9, 2012.

All of this evidence demonstrates that the CFTC was appropriately guided by a full appreciation of the need for reform and the important role of the Rule in achieving the primary congressional objective of preventing another financial crisis. This process, along with the agency's reasoned consideration of costs and benefits in accordance with Section 15(a), fully satisfied the CFTC's obligation.

CONCLUSION

For all of the foregoing reasons, the Court should uphold the Rule, grant the CFTC's Cross-Motion for Summary Judgment, deny the Plaintiffs' Motion for Summary Judgment, and dismiss the Plaintiffs' Complaint in Part.

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Respectfully submitted,

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