August 13, 2012

David A. Stawick
Secretary
Commodity Futures Trading Commission
Three Lafayette Center
1155 21st Street, N.W.
Washington, DC 20581

**Re:** Exemptive Order Regarding Compliance with Certain Swap Regulations, RIN Number 3038–AD85

Dear Mr. Stawick:

This letter is submitted on behalf of Public Citizen's Congress Watch[1] in response to the Commodity Futures Trading Commission's ("CFTC") request for comment on the agency's proposed exemptive order[2] ("Proposed Exemption") that is based on the CFTC's proposed guidance on the cross-border application of Dodd-Frank[3] ("Proposed Guidance"). The Proposed Exemption would delay the extraterritorial application of the Dodd-Frank Wall Street Reform and Consumer Protection Act[4] ("Dodd-Frank") that is required without any provision for delay by section 722 of the statute where U.S. institutions and interests are involved.[5]

The Proposed Exemption would delay compliance with most entity requirements[6] and transaction requirements[7] for foreign subsidiaries and affiliates of U.S. financial institutions[8] and

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[1] Public Citizen was founded in 1971 and counts more than 300,000 members and supporters, and advocates for consumer-based reform in Congress and before regulatory agencies.
[2] Exemptive Order Regarding Compliance With Certain Swap Regulations, 77 Fed. Reg. 41110 (proposed July 12, 2012) [hereinafter "Proposed Exemption"].
[3] Cross-Border Application of Certain Swaps Provisions of the Commodity Exchange Act, 77 Fed. Reg. 41214 at 41237, 41218 (proposed July 12, 2012) [hereinafter "Proposed Guidance"]. *See also* Sullivan and Cromwell, *CFTC Guidance on Extraterritoriality*, July 12, 2012 [hereinafter "Sullivan and Cromwell"], *available at* http://www.sullcrom.com/files/Publication/c0c33ecf-cfed-4b8a-a84e-0bd693512f02/Presentation/PublicationAttachment/0f14ac92-c20d-4575-a7f2-0d78aff000b1/S%26C_Publication_CFTC_Guidance_on_Extraterritoriality.pdf.
[4] Dodd-Frank Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010) [hereinafter "Dodd-Frank Act"].
[5] *Id*. at § 722(d)(i).
[6] Proposed Exemption, *supra* note 2, at 41114 (identifying 6 entity-level requirements: capital adequacy, chief compliance officer, risk management, swap data recordkeeping, reporting to an SDR, and physical commodity swaps reporting).
[7] *Id*. at 41115 (identifying 9 transaction-level requirements: clearing and swap processing, margining and segregation for uncleared swaps, trade execution, trade confirmation, swap

for U.S. subsidiaries and affiliates of foreign banks[9] for a 12-month period following the publication of the exemption in the Federal Register.[10] For example, the exemption would permit a foreign subsidiary of JPMorgan to delay compliance with all entity-level requirements[11] except for Swap Data Repository reporting and Large Trading reporting for swaps conducted with U.S. counterparties[12] and with all transaction-level requirements for swaps conducted with non-U.S. counterparties.[13]

Contrary to the CFTC's claims,[14] delayed compliance would unnecessarily prolong American taxpayers' exposure to the systemic risks of U.S. institutions and interests associated with the global swaps market and increase market uncertainty regarding the implementation and

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trading relationship documentation, real-time public reporting, portfolio reconciliation and compression, daily trading records, and external business conduct standards).

[8] Proposed Guidance, *supra* note 3, at 41218 (stating that "a foreign affiliate or subsidiary of a U.S. person would be considered a non-U.S. person even where such an affiliate or subsidiary has certain or all of its swap-related obligations guaranteed by the U.S. person"); *see also id*. at 41219, 41231 (explaining that Dodd-Frank requires non-U.S. persons that book over an aggregate gross notional amount of $8 billion on an annual basis to register as a swap dealer or major swap participant); Proposed Exemption, *supra* note 2, at 41110 (delaying compliance for non-U.S. swap dealers and major swap participants). *See also* Sullivan and Cromwell, *supra* note 3, at 3 ("Under the general *de minimis* test, when a person engages in swap dealing transactions over the prior 12 months at a level above an aggregate gross notional amount of $8 billion, such person meets the definition of a swap dealer under the CEA and is required to register as a swap dealer."); Latham and Watkins, *CFTC Guidance on Extraterritoriality*, July 16, 2012, *CFTC Proposes Interpretative Guidance on the Extraterritorial Reach of Title VII of the Dodd-Frank Act and Exemptive Relief to Extend Compliance Deadlines for Many Title VII Requirements, Particularly for Non-U.S. Persons, available at* http://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=10&ved=0CFUQFjAJ&url=http%3A%2F%2Fwww.linklaters.com%2Fpdfs%2Fmkt%2Fnewyork%2FA15244359.pdf&ei=nyMpUM_-HeTx0gHQ4oCoDA&usg=AFQjCNF02wjvRbyR923U6J6kyCaipBc2MA ("Under the de minimis exception from the swap dealer definition, even if an entity is engaged in swap dealing activity, such entity does not need to register as long as the entity's dealing activity remains below the applicable de minimis threshold.").

[9] Proposed Guidance, *supra* note 3, at 41219 (explaining that a U.S. branch, agent, affiliate, or subsidiary of a foreign financial institution is a non-U.S. person and therefore is only subject to Dodd-Frank if it qualifies as a swap dealer or major swap participant (i.e. it is the booking entity for an aggregate gross notional amount of $8 billion of swaps on a annual basis)); *see also* Proposed Exemption, *supra* note 2, at 41110 (delaying compliance for non-U.S. swap dealers and major swap participants).

[10] Proposed Exemption, *supra* note 2, at 41110.

[11] *Id*. at 41118.

[12] *Id*. at 41119.

[13] *Id*. at 41119.

[14] *Id*. at 41113 (claiming that the Proposed Exemption would "ensure an orderly transition to the Dodd-Frank Act regulatory regime" for non-US swap dealers and major swap participants and facilitate the "harmonization of international standards").

impact of Dodd-Frank rules. That is, foreign subsidiaries of U.S. parent companies and/or U.S. subsidiaries of foreign parent companies that collapse because of unregulated swaps trading would look to the U.S. taxpayer for rescue to the tune of trillions of dollars; or, in the absence of U.S. taxpayer support, drive the world economy into a deep recession or Depression. Additionally, such a delay would compromise U.S. leadership on derivatives reform and thereby frustrate Congress's intent to establish a global regulatory regime that will protect the U.S. economy and American taxpayers from international regulatory arbitrage and the need for continued bailouts of U.S. and foreign banks. In sum, the threat of systemic risk created by today's global derivatives market requires the prompt implementation of Dodd-Frank regulation.

The comments in this letter rely on comments made in our forthcoming comment letter[15] on the CFTC's Proposed Guidance. The forthcoming letter establishes that the plain language of Dodd-Frank requires the CFTC to classify foreign subsidiaries and affiliates of U.S. financial institutions and U.S. subsidiaries and affiliates of foreign financial institutions as U.S. persons in order to protect U.S. taxpayers from the risks posed by the global swap market.[16] Classifying a foreign subsidiary/affiliate of a U.S. person as a non-U.S. person hides the rabbit in the hat for Dodd-Frank purposes: Congress intended financial entities that are controlled by U.S. financial institutions and/or that could adversely impact the U.S. economy to be regulated as U.S. persons under Dodd-Frank in order to fully protect American taxpayers from the threat of future financial bailouts.[17] The forthcoming letter also establishes that substituted compliance has failed to ensure rigorous regulation of derivatives markets in the past and so should not be allowed for foreign subsidiaries of U.S. parents as these subsidiaries pose a severe risk to the U.S. economy.[18] The statutory analysis underpinning these comment letters can be found in the following forthcoming article in the University of Missouri Kansas City Law Review: *The Extraterritorial Provisions of the Dodd-Frank Act Protects U.S. Taxpayers From Worldwide Bailouts*.[19]

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[15] Comment Letter from Michael Greenberger, University of Maryland Center For Health and Homeland Security, to the Commodities Futures Trading Commission (forthcoming August 17, 2012) [hereinafter "Greenberger Comment Letter"].
[16] *Id*.
[17] *See* Dodd-Frank Act, *supra* note 4, at § 731 (requiring U.S. persons who meet certain criteria to register with the CFTC as swap dealers or major swap participants and, subsequently, to abide by Dodd-Frank swap regulation); *see also* COMMODITY FUTURES TRADING COMM"N & SEC. & EXCH. COMM'N, PUBLIC ROUNDTABLE TO DISCUSS INTERNATIONAL ISSUES RELATING TO THE IMPLEMENTATION OF TITLE VII OF THE DODD-FRANK ACT 155 (2011) [hereinafter ROUNDTABLE TO DISCUSS INTERNATIONAL ISSUES], *available at* http://www.sec.gov/news/press/2011/2011-151-transcript.pdf (testimony of Marcelo Riffaud) ("The minute you touch a U.S. person, as we've said repeatedly, you now have U.S. rules that will attach.").
[18] *See* Greenberger Comment Letter, *supra* note 15.
[19]Greenberger, Michael, *The Extraterritorial Provisions of the Dodd-Frank Act Protect U.S. Taxpayers From Worldwide Bailouts*, 80 U. MO. KAN. CITY 1 (2012), available at http://www.michaelgreenberger.com/files/Greenberger_UMKC_Final.pdf.

## I. Any Delay in the Implementation of Dodd-Frank's Vast Extraterritorial Reach Must Serve the Public's Interest.

Dodd-Frank aims "[t]o promote the financial stability of the United States by improving accountability and transparency in the financial system."[20] It also aims "to protect the American taxpayer by ending bailouts" and the "abusive financial services practices"[21] that led to the 2008 financial crisis. To this end, Title VII of the statute transforms the regulation of the $700 billion notional value over-the-counter (OTC) derivatives market[22] by subjecting most swaps traded by financial entities that are controlled by a U.S. financial institution and/or may adversely impact the U.S. economy to clearing and exchange trading, including capital, margin, and reporting requirements.[23]

Additionally, section 722 applies Dodd-Frank protections extraterritorially when the swaps activities of non-U.S. financial entities threaten or otherwise involve U.S. financial interests. Specifically, section 722(d) states that Dodd-Frank applies to swaps that either "have a direct and significant connection with activities in, or effect on, commerce of the United States"[24] or that contravene regulations that prevent the evasion of Dodd-Frank provisions.[25] Thus, Dodd-Frank provides U.S. taxpayers with comprehensive protections from the substantial risks posed by global swap trading.

Section 4(c) of the Commodities Exchange Act ("CEA") authorizes the CFTC to exempt a transaction or class of transactions from Dodd-Frank protections in order to "promote responsible economic or financial innovation and fair competition."[26] However, as the CFTC concedes,[27] section 4(c) prohibits the agency from granting exemptive relief unless the relief is "consistent with the public interest" and with the purposes of the CEA.[28] Delaying the application of Dodd-Frank regulations to transactions that fall squarely within Title VII and/or have a direct and significant affect on U.S. commerce (section 722) prolongs U.S. taxpayers' exposure to the Hobson's choice of either rescuing failed systemically risky institutions or facing a Depression, as was the case in the fall of 2008. As previously mentioned, Dodd-Frank was

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[20] Dodd-Frank Act, *supra* note 4, at Preamble.

[21] *Id.*

[22] Peter Barnes, *CFTC, SEC Adopt Tougher Rules on Derivatives Markets*, FOX BUSINESS, April 18, 2012, *available at* http://www.foxbusiness.com/investing/2012/04/18/cftc-sec-adopt-tougher-rules-on-derivatives-markets/.

[23] BAIRD WEBEL ET AL., CONG. RESEARCH SERV., R40975, FINANCIAL REGULATORY REFORM AND THE 111TH CONGRESS 12 (2010), *available at* http://fpc.state.gov/documents/organization/141604.pdf ("H.R. 4173 . . . mandate[s] reporting, centralized clearing, and exchange-trading of OTC derivatives . . . . [the bill] require[s] regulators to impose capital requirements on swap dealers and 'major swap participants.'").

[24] Dodd-Frank Act, *supra* note 4, at § 722(d)(i)(1).

[25] *Id.* at § 722(d)(i)(2).

[26] 7 U.S.C. § 6(c)(1) (2010).

[27] Proposed Exemption, *supra* note 2, at 41113.

[28] 7 U.S.C. § 6(c)(2).

enacted to prevent U.S. taxpayers from having to face such a conundrum.[29] Moreover, not implementing Dodd-Frank protections on an extraterritorial basis for a one year period is not consistent with the CEA, as amended by Dodd-Frank, which promises to protect U.S. taxpayers from the systemic risk posed by unregulated swaps activities.

## II. The Global Swaps Market Poses a Direct, Significant, *and* Immediate Risk to the U.S. Economy.

Jamie Dimon, chief executive officer of JPMorgan Chase, has commented that banks such as JPMorgan "move trillions of dollars a day around the world, usually for global clients."[30] In this regard—and in light of the multi-billion dollar losses that JPMorgan recently incurred from synthetic derivatives trades made by its London subsidiary[31]—global derivatives trading poses an immediate and systemic risk to the U.S. economy.[32] Affiliates, branches, *and* subsidiaries[33] of U.S. parent companies that operate outside of the United States and subsidiaries of affiliates of foreign parent institutions that operate within the United States threaten U.S. economic interests and, therefore, should comply with Dodd-Frank without delay.

### 1. Global Swaps Trading Threatens the U.S. Economy and American Taxpayers Who Serve as Insurers of Last Resort.

The American taxpayers' $183 billion bailout of American International Group (AIG)[34] proves that the financial stability of even a major U.S. financial institution can be undercut by the irresponsible trading practices of a foreign subsidiary. AIG's British subsidiary, AIG Financial Products, sold vast numbers of synthetic derivatives on mortgage-backed securities. When the value of these securities plummeted in the fall of 2008, AIG owed billions of dollars to investors

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[29] *See supra* pp. 4-5.

[30] *Dimon on Price Wars, Volcker Rule, Stock Prices* (Fox Business broadcast Feb. 13, 2012), *available at* http://video.foxbusiness.com/v/1450367194001/dimon-on-price-wars-volcker-rule-stock-prices/.

[31] Maureen Farrell, *JPMorgan's Trading Loss: $5.8 billion*, CNNMONEY, July 13, 2012, [hereinafter "Farrell"], *available at* http://money.cnn.com/2012/07/13/investing/jpmorgan-earnings/index.htm.

[32] *See* ROUNDTABLE TO DISCUSS INTERNATIONAL ISSUES, *supra* note 17, at 68 (testimony of Robert Cook) (arguing that "broad rules perhaps are best" because "activities in physical [commodities] and not in our country have a huge effect back into [the U.S.] market"); *see also* Gary Gensler, CFTC Chairman, Keynote Address on the Cross-Border Application of Dodd-Frank Swaps Market Reforms Before the 2012 FINRA Annual Conference (May 21, 2012) [hereinafter Gensler Keynote Address], *available at* http://www.cftc.gov/PressRoom/SpeechesTestimony/opagensler-113, (observing that swaps have "concentrated and heightened risk in international financial institutions . . . [and] can contribute to quickly spreading risk across borders").

[33] *See* Greenberger Comment Letter, *supra* note 15.

[34] Richard J. Herring, *Wind-Down Plans as an Alternative to Bailouts: The Cross-Border Challenges*, *in* ENDING GOVERNMENT BAILOUTS AS WE KNOW THEM, 156 (Kenneth E. Scott et al. eds., 2010).

who had bet against these subprime mortgages being paid off.[35] As CFTC Chairman Gary Gensler has observed, AIG's "fast collapse . . . was sobering evidence . . . of how transactions booked in London or anywhere around the globe can wreak havoc on the American public."[36]

As Chairman Gensler has also observed, the risk associated with extraterritorial swaps activities "inevitably comes crashing back onto U.S. shores."[37] In its Proposed Guidance, the CFTC explains that Lehman Brothers's bankruptcy in 2008 constitutes a "stark lesson on how risks can spread quickly across the affiliated entities of a multinational financial institution."[38] Additionally, shortly before the financial crisis Citigroup received a $2 billion taxpayer infusion[39] after it assumed approximately $49 billion of debt generated by risky international swaps trades that were conducted in the Cayman Islands.[40] Similarly, in 2007 Bear Stearns received extensive support from the Federal Reserve after it bailed out two of its failing hedge fund affiliates located in the Cayman Islands.[41]

The multi-billion dollar trading losses recently incurred by JPMorgan confirm that unregulated global swaps trading by foreign subsidiaries of U.S. financial institutions presents a significant risk to the U.S. economy and should be promptly regulated. JPMorgan, the largest U.S. bank holding company,[42] is assuming almost $6 billion in losses from bad trades in complex synthetic credit derivatives that were made by a single trader—the "London Whale"[43]—in the bank's U.K. subsidiary. JPMorgan's multi-billion-dollar losses confirm that even sophisticated U.S. banks cannot effectively manage the risks associated with global swaps trading; the losses also prove that U.S. taxpayers are susceptible to bailing out U.S. financial institutions whose swap trades, as was true of the subprime meltdown trades, surpass their capital reserves.[44] As

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[35] *See* Peter Koeing, *AIG Trail Leads to London 'Casino'*, TELEGRAPH, Oct. 18, 2008, http://www.telegraph.co.uk/finance/financialcrisis/3225213/AIG-trail-leads-to-London-casino.html.

[36] *See Implementing Derivatives Reform: Reducing Systemic Risk and Improving Market Oversight*, *Hearing Before the S. Comm. on Banking, Housing, & Urban Affairs*, 112th Cong. (2012) (statement of Gary Gensler, CFTC Chairman), *available at* http://www.cftc.gov/PressRoom/SpeechesTestimony/opagensler-114.

[37] Gary Gensler, CFTC Chairman, *Testimony of Gary Gensler Before the H. Comm. on Agriculture*, 112th Cong. (2012) (testimony of Gary Gensler), *available at* http://agriculture.house.gov/sites/republicans.agriculture.house.gov/files/documents/Gensler120725.pdf.

[38] Proposed Guidance, *supra* note 3, at 41215.

[39] Gensler Keynote Address, *supra* note 32.

[40] *Id.*

[41] *Id.*

[42] *See* Jake Zamansky, *Wall Street Compensation and JP Morgan: It's Déjà Vu All Over Again*, FORBES (June 1, 2012), http://www.forbes.com/sites/jakezamansky/2012/06/01/wall-street-compensation-and-jp-morgan-its-deja-vu-all-over-again/.

[43] Farrell, *supra* note 31.

[44] Jennifer Liberto, *CFTC Investigating JPMorgan Chase*, CNN MONEY (May 22, 2012), http://money.cnn.com/2012/05/22/news/economy/jp-morgan-senate/index.htm (explaining that

Senator Tim Johnson, Chair of the Senate Committee on Banking, Housing, and Urban Affairs, has stated, JPMorgan's "massive trading loss is a stark reminder of the financial crisis of 2008 and the necessity of Wall Street reform."[45] This "massive" loss is also a reminder that Dodd-Frank's extraterritorial protections—which include strict capital, margin, and transparency requirements for swaps dealers[46]—need to be quickly implemented in order to protect U.S. economic interests.

Further, foreign banks that operate in the United States pose an additional and immediate threat to the U.S. economy and the American taxpayer. For example, Norinchukin Bank borrowed almost $22 billion of emergency funds from the Federal Reserve during the 2008 financial crisis.[47] Similarly, the Royal Bank of Scotland ("RBS") borrowed approximately $85 billion from the Federal Reserve[48]—more than the $74 billion in aid that RBS received from the Bank of England[49]—and Deutsche Bank, Germany's biggest bank, borrowed $66 billion from the Federal Reserve during the financial crisis (even though it did not receive capital injections from the German government).[50] Thus, delayed compliance would increase the risk that U.S.

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U.S. banks like JPMorgan have "direct access to the Federal Reserve's discount window and federal deposit insurance").

[45] *Implementing Derivatives Reform: Reducing Systemic Risk and Improving Market Oversight*, *Hearing Before the S. Comm. on Banking, Housing, & Urban Affairs*, 112th Cong. (2012) (statement of Tim Johnson, Chair, S. Comm. on Banking, Housing, & Urban Affairs), *available at* http://banking.senate.gov/public/index.cfm?FuseAction=Newsroom.PressReleases&ContentRecord_id=75aea17c-d90e-40e0-4809-0791b8d6bb74.

[46] *See* Barbara Roper, *Will JPMorgan's Loss Provide a Win for Wall Street Reform?*, HUFFINGTON POST BUS. (May 14, 2012), http://www.huffingtonpost.com/barbara-roper/jpmorgan-wall-street-reform_b_1516352.html#es_share_ended; *see also* Steven Pearlstein, *Why Do They Trade This Stuff Anyway?*, WASH. POST, May 20, 2012, at G1.

[47] Yalman Onaran, *Bank Lobby Widened Volcker Rule, Inciting Foreign Outrage*, BLOOMBERG (Feb. 23, 2012, 2:56 PM), http://www.bloomberg.com/news/2012-02-23/banks-lobbied-to-widen-volcker-rule-before-inciting-foreigners-against-law.html.

[48] *The Fed's Secret Liquidity Lifelines: Royal Bank of Scotland Group Plc Details*, BLOOMBERG, http://www.bloomberg.com/data-visualization/federal-reserve-emergency-lending/#/Royal_Bank_of_Scotland_Group_PLC/?total=true&mcp=true&mc=true&taf=false&cpff=false&pdcf=false&tslf=false&stomo=false&amlf=false&dw=false/.

[49] *Id*.

[50] *The Fed's Secret Liquidity Lifelines: Deutsche Bank AG Details*, BLOOMBERG, http://www.bloomberg.com/data-visualization/federal-reserve-emergency-lending/#/Deutsche_Bank_AG/?total=true&mcp=true&mc=true&taf=false&cpff=false&pdcf=false&tslf=false&stomo=false&amlf=false&dw=false/. *See also* Bradley Keoun & Craig Torres, *Foreign Banks Tapped Fed's Secret Lifeline Most at Crisis Peak*, BLOOMBERG (Apr. 1, 2011, 12:53 PM), http://www.bloomberg.com/news/2011-04-01/foreign-banks-tapped-fed-s-lifeline-most-as-bernanke-kept-borrowers-secret.html (reporting that in the aftermath of the 2008 financial crisis many foreign banks borrowed from the Federal Reserve's discount window: Dexia, a Belgian- and French-based bank, borrowed approximately $33.5 billion and Depfa Bank, based in Dublin and now owned by the German government, borrowed $24.5 billion).

taxpayers would have to continue to spend trillions of dollars to bailout financial institutions, headquartered in the United States and abroad, that engage in global swaps trading.

### 2. Foreign Financial Regulatory Regimes Do Not Safeguard U.S. Taxpayers Against the Risk of Additional Bank Bailouts.

The slow pace of financial reform outside of the United States means that any delay in applying Dodd-Frank regulations across foreign jurisdictions would leave U.S. taxpayers without significant protection against the demonstrated risks associated with the global swaps market. Although many non-U.S. jurisdictions have adopted guiding principles for financial reform,[51] they have not fully engaged the arduous process of translating statutory principles into operational regulations. For example, the United Kingdom has indicated that it may not implement the general reforms stipulated by the Independent Commission on Banking until 2019, when the new rules established by the Basel III international agreement on capital held by banks must come into effect.[52] The European Union is in a similar position: it has enacted financial reform legislation, but has only recently begun the rule-making process.[53] Additionally, a joint report issued by the CFTC and SEC at the beginning of this year observed that "only the United States and Japan have adopted recent legislation" that deals with the "regulation of market participants, clearing, reporting, and trading of OTC derivatives."[54] The same report also

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[51] *See infra* p. 10.

[52] Robert Peston, *Banks Face Biggest Shake-Up for Decades*, BBC NEWS (Sept. 12, 2011), http://www.bbc.co.uk/news/business-14877861; *see also* Mark Hoban, Fin. Sec'y to the Treasury, *Britain Still Leads Critical Financial Reform Talks*, TELEGRAPH, Feb. 19, 2012, http://www.telegraph.co.uk/finance/newsbysector/banksandfinance/9091829/Britain-still-leads-critical-financial-reform-talks.html (discussing how European leaders are still working to construct a strong "framework" for financial reform and admitting that "there remains much work to do" regarding European financial reform).

[53] *See* ATLANTIC COUNCIL & THOMSON REUTERS, THE DANGER OF DIVERGENCE: TRANSATLANTIC COOPERATION ON FINANCIAL REFORM I (2010), *available at* http://www.brookings.edu/~/media/Files/rc/reports/2010/1007_atlantic_council_elliott/1007_atlantic_council_elliott.pdf (commenting that while Europe is still considering major financial-reform legislation, the U.S. "has already set a framework to address the root causes" of the 2008 financial crisis); *see also Laws For All: Lots of Rules, But Not All Good Ones*, ECONOMIST, Feb. 18, 2012, http://www.economist.com/node/21547835 (reporting that the European Commission has issued over twenty proposed rules that are at different stages in the legislative process—forthcoming, under negotiation, and adopted—but that overall E.U. regulations are fragmented and trail U.S. efforts to regulate derivatives trading under Dodd-Frank); *see also* John O'Donnell, *EU Considers New Controls for Shadow Banking*, REUTERS, Mar. 19, 2012, *available at* http://www.reuters.com/article/2012/03/19/us-eu-shadowbanking-idUSBRE82I0KM20120319 (reporting that the E.U. has been criticized for being "slow to tackle the causes of a financial crisis that struck Europe roughly five years ago").

[54] CFTC and SEC, Joint Report on International Swap Regulation Required by Section 719(c) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Jan. 31, 2012, 98 [hereinafter "Joint Report"], *available at* http://www.cftc.gov/ucm/groups/public/@swaps/documents/file/dfstudy_isr_013112.pdf.

observed that the United Kingdom is the only foreign jurisdiction to have "proposed rules similar to the Push-Out and Volcker Rules"[55] and concludes that many "[o]ther jurisdictions have not yet proposed or adopted statutory or regulatory changes" to regulate OTC derivatives.[56]

Although international regulatory organizations have proposed global standards for financial reform, these proposals do not discuss how specific principles should be applied to derivatives markets. For example, the International Organization of Securities Commissions (IOSCO) recently released a report entitled *International Standards For Derivatives Market Intermediary Regulation* in which it observed that "[c]ross-border consistency among market authorities . . . is essential to successful oversight of the global OTC derivatives market."[57] The report offers 15 recommendations regarding intermediaries in the swaps market that are similar to U.S. regulations;[58] however, these recommendations offer general principles without providing the details necessary for the successful implementation of global financial reforms. By way of illustration, IOSCO recommends that market intermediaries "should be subject to business conduct standards designed to ensure they operate in an ethical manner . . . [and] be strictly prohibited from engaging in any illegal or abusive practices."[59] In contrast, the CFTC has adopted specific prohibitions against fraud, manipulation, and other market abuses, and requires swaps parties to communicate in good faith.[60]

Additionally, IOSCO's survey of different jurisdictional approaches to market reform affirms that the United States remains well ahead of other jurisdictions with respect to derivatives reform. For example, the report observes that while "[s]ome jurisdictions are in the process of developing recordkeeping requirements" for market intermediaries, the CFTC is the only market authority that has already adopted rules that will require market intermediaries to submit specific documentation to a trade repository.[61] Also, IOSCO identifies the CFTC's "robust standards for business supervision"[62]—the monitoring of trades, risk management procedures, conflict of interest controls, and qualifications for supervisors—as a model for the majority of jurisdictions that have yet to develop business supervisory obligations of any kind.[63]

Even if select foreign countries develop seemingly comprehensive and rigorous regulatory regimes, such regimes cannot adequately protect U.S. taxpayers against the risks

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[55] *Id*. at 102.
[56] *Id*. at 7.
[57] INT'L ORG. OF SEC. COMM'NS, INTERNATIONAL STANDARDS FOR DERIVATIVES MARKET INTERMEDIARY REGULATION 1 (2012), *available at* http://www.iosco.org/library/pubdocs/pdf/IOSCOPD381.pdf.
[58] *Id*. at 9, 16-17 (recommending that market intermediaries register with market regulators and that intermediaries be subject to margin and capital requirements); *see also id*. at 1 (stating that the report's recommendations pertain to substantive areas such as business conduct, capital, registration, and recordkeeping standards).
[59] *Id*. at 22.
[60] *Id*. at 20. *See also* 17 C.F.R. § 23.410 (2011).
[61] *Id*. at 32.
[62] *Id*. at 28.
[63] *Id*. at 26.

posed by an interconnected and systemically risky global derivatives market. As previously mentioned,[64] so-called comparative financial regulation and enforcement by foreign countries have consistently failed to provide rigorous oversight of derivatives activities that present a risk to the U.S. economy.[65] Thus, even if foreign jurisdictions like the United Kingdom and the European Union were to complete their financial reform efforts in the near future—an extremely unlikely proposition—American taxpayers would remain at risk of a further bailout until Dodd-Frank regulations apply extraterritorially.

## III. Delaying the Implementation of Dodd-Frank on an Extraterritorial Basis for U.S.-Controlled Entities and When U.S. Interests Are at Stake, Defies Congress's Intent to Protect U.S. Taxpayers from "Foreign" Systemic Failures that Implicate U.S. Taxpayer Bailouts.

The CFTC's Proposed Exemption flaunts Congress's desire for the speedy implementation of a global financial regulatory regime[66] and the American public's need for prompt protection from the risk of future bailouts of global financial institutions. The CFTC correctly states that Congress mandated the harmonization of international swaps regulation;[67] however, this mandate only applies to the regulation of swaps activity that occurs outside of the scope of Dodd-Frank.

Section 752(a) instructs the CFTC and SEC to "promote effective and consistent global regulation of swaps and security-based swaps" by "consult[ing] and coordinat[ing] with foreign regulatory authorities on the establishment of consistent international standards with respect to . . . [swaps] regulation."[68] Similarly, section 719(c) requires the CFTC and SEC to study swap and clearinghouse regulations in foreign jurisdictions and to identify areas where these regulations might align with U.S. regulations.[69] Section 719 also requires both agencies to "identif[y] areas of regulation that are similar in the United States, Asia and Europe" and to locate "other areas of regulation that could be harmonized."[70]

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[64] *See supra* p. 3.
[65] *See* Greenberger Comment Letter, *supra* note 15.
[66] *See* Dodd-Frank Act, *supra* note 4, at §§ 712(a)(3) (requiring regulators to issue final rules by July 16, 2011 (i.e., 360 days after Dodd-Frank's enactment)); 716(h) (requiring the Lincoln Rule to take effect "2 years following the date on which this Act is effective"); 619 (requiring the Volcker Rule to take effect on the earlier of "12 months after the date of the issuance of final rules under subsection" or "2 years after the date of enactment of this section"); *see also* Letter from Committee on Capital Markets Regulation to Senator Christopher Dodd *et al.*, 1-2 (Dec. 15, 2010), *available at* http://capmktsreg.org/category/letters/congress/ (commenting that Dodd-Frank has required federal agencies to issue 230 new rules in a short amount of time: the statute required the SEC to issue approximately sixty new rules and the CFTC to issue approximately forty new rules within a year of the statute's enactment).
[67] Proposed Exemption, *supra* note 2, at 41113.
[68] Dodd-Frank Act, *supra* note 4, at § 752(a).
[69] *Id*. at § 719(c)(1).
[70] *Id.*

Sections 752 and 719 have encouraged U.S. regulators to examine foreign laws and rules and to consult with their foreign counterparts regarding financial reform.[71] The international cooperation required by sections 752 and 719 is, however, only necessary to ensure worldwide regulation of systemic risk where the U.S. does not have extraterritorial reach. Congress intended U.S. regulators to subject U.S. persons as well as financial institutions that have a direct and significant impact of the U.S. economy to Dodd-Frank without concern for foreign regulatory requirements. Thus, the harmonization provisions in sections 752 and 719 do not warrant delaying the implementation of Dodd-Frank for the likes of foreign subsidiaries of U.S. banks that clearly are within the scope of section 722.

Congress did not pass Dodd-Frank to establish a malleable regulatory regime that prioritizes (and accommodates) foreign jurisdictions' concerns above American taxpayers' economic interests or that allows foreign jurisdictions to regulate swap activity that poses a real threat to the U.S. economy. Additionally, Congress did not pass Dodd-Frank to allow global banks to easily evade financial regulation or to continue to engage in risky swaps trades that have wrought havoc on the U.S. and global economies. Rather, Congress passed Dodd-Frank to prevent U.S. taxpayers from having to choose between spending trillions of dollars to bail out major financial institutions or suffer the effects of a severe economic recession or even a Depression.[72] If another financial crisis ensues because the CFTC failed to assert its full statutory authority to protect American taxpayers from the risks posed by the global swaps market, the American taxpayer will not forgive the CFTC because of concerns related to "comity" and/or "the sovereign interests of other nations."[73]

## IV. U.S.-Controlled Foreign Subsidiaries and Foreign Financial Institutions Operating in the United States Do Not Require Additional Time to Comply With Dodd-Frank Regulation.

Delayed compliance for foreign subsidiaries and affiliates of U.S. financial institutions and for foreign financial institutions with U.S. affiliates and subsidiaries is not, as the CFTC claims, necessary to "facilitate an orderly transition to the Entity-Level Requirements . . . while minimizing undue disruptions to current market operations."[74] Non-U.S. financial organizations have had adequate notice of Dodd-Frank requirements and sufficient time to anticipate and respond to CFTC regulations. In this respect, further delaying the implementation of Dodd-Frank would prolong U.S. taxpayers' exposure to the demonstrated risks associated with global swap trading without advancing the public's interest in strict compliance with Dodd-Frank regulation.

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[71] Letter from Treasury Secretary Timothy Geithner to Congressman Spencer Bachus, 1 (Sept. 14, 2011) (explaining that the SEC and CFTC have studied the international implications of Dodd-Frank regulations and are working with their European and Asian counterparts to produced comparable financial regulations)[hereinafter "Geithner Letter"].
[72] *Supra* pp. 4-5.
[73] Proposed Guidance, *supra* note 3, at 41223.
[74] Proposed Exemption, *supra* note 2, at 41112.

Although the CFTC is nearing the end of the rulemaking process,[75] this process has been considerably delayed; consequently, financial institutions have had plenty of time to anticipate and adopt practices that would satisfy Dodd-Frank. For example, the CFTC failed to finalize its rules by the July 16, 2011, deadline set by Congress[76] and has repeatedly pushed back internal deadlines.[77] Also, the CFTC's current rulemaking schedule means that Dodd-Frank derivatives regulation will be implemented approximately five years after the 2008 financial collapse that devastated the U.S. and world economies, and about three years since President Obama signed Dodd-Frank into law in July 2010. Delayed compliance for non-U.S. financial entities would unnecessarily compound the delays that have afflicted the U.S. rule-making process, as the process aims to prevent another economic meltdown as well as successive taxpayer bailouts of the Too Big To Fail swap dealing institutions.[78]

Further, non-U.S. financial institutions have consistently demonstrated their willingness and ability to quickly and efficiently reorganize their operations to comply with anticipated Dodd-Frank regulations. For example, Deutsche Bank and Barclays have already moved their commercial banks from their U.S. subsidiaries into their global firms to avoid Dodd-Frank's capital requirements, even though these requirements do not go into effect until July 2015.[79] Similarly, many large U.S. financial institutions—including Goldman Sachs and Bank of America—closed their independent proprietary trading desks shortly after Dodd-Frank became law in 2010 in anticipation of the Volcker Rule.[80] The fact that most large financial institutions are capable of modifying their processes to avoid Dodd-Frank regulation, strongly suggests that these same institutions are capable of speedy compliance with Dodd-Frank regulations with minimal expense or confusion.

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[75] *See supra* pp. 8-9.

[76] Testimony of CFTC Chairman Gary Gensler, *Hearing before the H. Comm. on Agriculture* (2011), *available at* http://www.cftc.gov/PressRoom/SpeechesTestimony/opagensler-88.

[77] *See* Davis Polk, *Two Year Anniversary Report*, DAVIS POLK REGULATORY TRACKER, July 18, 2012, 9, *available at* http://www.sullcrom.com/files/Publication/c0c33ecf-cfed-4b8a-a84e-0bd693512f02/Presentation/PublicationAttachment/0f14ac92-c20d-4575-a7f2-0d78aff000b1/S%26C_Publication_CFTC_Guidance_on_Extraterritoriality.pdf; *see also* Brian Schied, *CFTC Surprises No One By Delaying Dodd-Frank Rules Some More*, PLATTS: THE BARREL, May 11, 2012, *available at* http://www.platts.com/weblog/oilblog/2012/05/11/cftc_surprises.html; *see also* Sarah N. Lynch & Christopher Doering, *CFTC Insiders Blow Whistle on Position Limit Rule*, THOMAS REUTERS, Sept. 14, 2011, *available at* http://newsandinsight.thomsonreuters.com/Securities/News/2011/09_-_September/Exclusive__CFTC_insiders_blow_whistle_on_position_limit_rule/ (reporting that the CFTC has repeatedly delayed the vote on a final position limits rule).

[78] Dodd-Frank Act, *supra* note 4, at Preamble.

[79] Suzy Khimm, *Banks' Preemptive Strike Against Dodd-Frank*, WASHINGTON POST, March 24, 2012, *available at* http://www.washingtonpost.com/business/economy/banks-preemptive-strike-against-dodd-frank/2012/03/23/gIQATnUmWS_story.html.

[80] Benn Protess, *With Volcker Rule, Wall Street Braces for Change,* NYTIMES*,* Oct. 11, 2001, *available at* http://dealbook.nytimes.com/2011/10/11/with-volcker-rule-wall-street-braces-for-change/.

## V. Conclusion

The rigorous and immediate regulation of the $700 trillion global swaps market—a market that facilitated the 2008 financial crisis and continues to generate worldwide systemic risk—is necessary to comply with the provisions of Dodd-Frank and to safeguard the American taxpayer's economic interests. Congress clearly intended for the CFTC to quickly implement Dodd-Frank regulations on an extraterritorial basis when U.S. economic interests are involved in order to protect American taxpayers from the severe risks associated with foreign subsidiaries controlled by U.S. entities, foreign institutions conducting swaps in the United States, and/or where the stability of the U.S. economy is threatened. Delaying compliance with the protections afforded by Dodd-Frank belies Congress's express intent and, even worse, it has the CFTC sanctioning the U.S. taxpayer's unnecessary prolonged exposure to the threat of having to bailout large banks and financial institutions on an ongoing basis or, in the absence of such trillion dollar bailouts, of a worldwide Second Depression.

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