

## **SPEECHES & TESTIMONY**

### **Public Meeting Opening Statement of Commissioner Rostin Behnam**

**November 5, 2018**

Thank you Mr. Chairman. I would like to start by thanking all of the Commission staff who worked to make today's meeting possible – both those who will be presenting at the table today and those who provided the knowledge and analysis supporting their statements. I'd also like to welcome Commissioners Stump and Berkovitz to the dais. I look forward to continuing to deliberate on these and other issues on the agenda.

#### **The De Minimis Exception**

Today, the Commission puts an end to undue and prolonged uncertainty in the swaps market and acts decisively to set the aggregate gross notional amount ("AGNA") threshold for the de minimis exception at \$8 billion in swap dealing activity entered into by a person over the preceding 12 months. Despite opposing the rule as proposed in June,<sup>[1]</sup> I am comfortable supporting today's final rule because it is limited to establishing a clear and certain de minimis threshold.

My gravest concern with the proposal for the de minimis exception was that the Commission may have been using the rulemaking to redefine swap dealing activity absent meaningful collaboration with the Securities and Exchange Commission (“SEC”), as required by the Dodd-Frank Act,<sup>[2]</sup> and to the detriment of market participants eager for regulatory certainty. I was also concerned that the proposal’s multiple ancillary components might signify a willingness to exploit the de minimis exception as a means to further unilaterally alter the swap dealer definition in clear circumvention of Congressional intent. In short, I was disappointed that the Commission was not focusing on what it needed to do—provide regulatory certainty for a critical cohort of market participants—and instead, was exploring the limits of its authority and creating impracticable expectations.

I appreciate the Chairman and staff’s willingness to address my concerns and for their thoughtful consideration of the comments.

Inasmuch as I am pleased that the final rule is narrowly focused purely on the numerical setting of the AGNA threshold, I am concerned that the Commission has yet to resolve longstanding concerns with the IDI loan-related swap exclusion referred to in today’s final rule as the “IDI Swap Dealing Exclusion.” The IDI Swap Dealing Exclusion codifies part of the statutory swap dealer definition in section 1a(49)(A) of the Commodity Exchange Act<sup>[3]</sup> and was jointly adopted with the SEC as paragraph (5) to the regulatory swap dealer definition.<sup>[4]</sup> This is not to be confused with the proposed IDI De Minimis Provision, which would have established an alternative to the exclusion, absent SEC coordination, that would have in effect, revised the scope of activity that constitutes swap dealing.

Today’s final rule is vague regarding whether the Commission will work with the SEC in its ongoing commitment to continue considering issues raised by commenters towards appropriately amending the Swap Dealing Exclusion, consistent with the Dodd-Frank Act, or whether it will continue to attempt to finalize a separate exception. I stand by my prior statement and continue to believe that the only correct path forward is for the CFTC and SEC to jointly consider and amend, as appropriate, the IDI Swap Dealing Exclusion. I would be happy to participate in support of this effort.

The current data—absent consideration of the non-financial commodity (“NFC”) asset class—demonstrates that allowing the AGNA to decrease to \$3 billion may capture an additional 13 swap dealers.<sup>[5]</sup> Almost all are banking entities subject to prudential or comparable regulation in their respective jurisdictions, such that they are examined for safety and soundness and required to comply with customer protection rules.<sup>[6]</sup> The few that are not banking entities are financial entities that are likely subject to regulation on a federal or state level. Moreover, for all thirteen entities, the Commission was unable to exclude data regarding swaps that fall under the IDI Swap Dealing Exclusion, possibly lowering that number even further.

I’m pointing this out because I would like to stress that, while I support today’s decision to maintain the AGNA threshold at \$8 billion, there is still work to be done on improving our data. While swap data repository (“SDR”) data quality has improved, AGNA data was unavailable for NFC swaps.<sup>[7]</sup> Nevertheless, Commission staff used counterparty and transaction counts and a series of assumptions to analyze likely swap dealing activity in the NFC swap market and concluded that reducing the \$8 billion AGNA threshold could lead to reduced liquidity in NFC swaps, negatively impacting end-users and commercial entities who utilize NFC swaps for hedging.<sup>[8]</sup> The Commission further relied upon findings and comments that the unique characteristics of the NFC swap market poses less systemic risk than financial swaps.<sup>[9]</sup>

It is my hope that Commission staff will continue to examine and monitor data and activities in the NFC swap market to ensure that concentrated activity by unregistered NFC counterparties in segments of that swap market, such as in energy-related swaps, do not present outsized risk or harm to end-users, and most importantly the general public.

## **Swap Execution Facilities and Trade Execution Requirement**

Staff also will be presenting proposed rules that would constitute an overhaul of the existing framework for swap execution facilities, or SEFs. The Commission's action today begins the process of public notice and comment under the Administrative Procedure Act.<sup>[10]</sup> Given the breadth and complexity of the rule before us, the process of public comment is particularly important for this rule. I look forward to receiving input from the many market participants who would be impacted, in any way, by a reworking of the SEF rules.

As we start to consider the direction and breadth of SEF reform, I think it is very important that we first review how we got where we are today. Prior to the 2008 financial crisis, swaps were largely exempt from regulation and traded exclusively over-the-counter, rather than on a regulated exchange.<sup>[11]</sup> The opaque over-the-counter swaps market contributed to the financial crisis because both regulators and market participants lacked the visibility necessary to identify and assess swaps market exposures and counterparty relationships.<sup>[12]</sup> In the aftermath of the financial crisis, Congress enacted the Dodd-Frank Act in 2010.<sup>[13]</sup>

The Dodd-Frank Act largely incorporated the international financial reform initiatives for over-the-counter derivatives laid out at the 2009 G20 Pittsburgh Summit aimed at improving transparency, mitigating systemic risk, and protecting against market abuse.<sup>[14]</sup> Title VII of the Dodd-Frank Act amended the Commodity Exchange Act to establish a comprehensive new swaps regulatory framework that includes the registration and oversight of a new registered entity – SEFs. A key goal of Title VII of the Dodd-Frank Act is to bring greater pre-trade and post-trade transparency to the swaps market. The concept of transparency runs throughout Title VII – starting with the title itself: the “Wall Street *Transparency and Accountability Act of 2010.*”<sup>[15]</sup>

As part of the Dodd-Frank effort to provide more transparency, in 2013, the Commission adopted the part 37 rules in order to implement a regulatory framework for SEFs.<sup>[16]</sup> In so doing, the Commission emphasized that “[pre-trade] transparency lowers costs for investors, consumers, and businesses; lowers the risks of the swaps market to the economy; and enhances market integrity to protect market participants and the public.”<sup>[17]</sup>

The SEF framework has in many ways been a success. There are currently 28 registered SEFs.<sup>[18]</sup> Trading volume on SEFs has been steadily growing each year.<sup>[19]</sup> The Commission's work to promote swaps trading on SEFs has resulted in increased liquidity, while adding pre-trade price transparency and competition.<sup>[20]</sup>

This is not to say that the SEF rules were perfect from the start and would not benefit from some targeted improvement. Most SEFs rely upon multiple no-action letters granted by the Division of Market Oversight. While the purpose of this form of targeted relief was often to smooth the implementation of the SEF framework, codifying or eliminating the need for existing no-action relief would provide market participants with greater legal certainty.

The current SEF rules have not brought as much trading onto SEFs as intended or envisioned. We can improve upon that, and I am hopeful that this process will bring about a thoughtful, inclusive, well-reasoned debate that limits changes to those issues that will result in policy consistent with congressional intent and the overarching goals of supporting strong, liquid, transparent markets.

## **Conclusion**

Thank you again to staff for your hard work on today's rules. I look forward to the presentations.

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<sup>[1]</sup> De Minimis Exception to the Swap Dealer Definition, 83 FR 27444, 27481-4 (proposed June 12, 2018).

<sup>[2]</sup> The Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203 § 712(d), 124 Stat. 1376, 1644 (2010). Additionally, with respect to rulemakings and orders regarding swap dealers, among other things, § 712(a) requires the CFTC to consult and coordinate to the extent possible with the SEC and the prudential regulators to ensure consistency and comparability, to the extent possible. Such consultation must occur before the CFTC commences such rulemaking or order issuance.

- [3] See CEA 1a(49)(A), 7 U.S.C. 1a(49)(A) (providing that “in no event shall an insured depository institution be considered to be a swap dealer to the extent it offers to enter into a swap with a customer in connection with originating a loan with that customer.”)
- [4] 17 CFR 1.3, Swap Dealer, paragraph (5).
- [5] 83 FR at 27453-4.
- [6] *Id.*
- [7] 83 FR at 27445.
- [8] 83 FR at 27450, 27456-7.
- [9] 83 FR at 27457, De Minimis Exception to the Swap Dealer Definition, 83 FR , ( , 2018) (to be codified at 17 CFR pt. 1).
- [10] The Administrative Procedure Act, 5 U.S.C. § 500 *et seq.*
- [11] See Commodity Futures Modernization Act of 2000, Public Law 106-554, 114 Stat. 2763 (2000).
- [12] See The Financial Crisis Inquiry Commission, The Financial Crisis Inquiry Report: Final Report of the National Commission on the Causes of the Financial and Economic Crisis in the United States (Official Government Edition), at 299, 352, 363-364, 386, 621 n. 56 (2011), available at <https://www.gpo.gov/fdsys/pkg/GPO-FCIC/pdf/GPO-FCIC.pdf>.
- [13] See Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 124 Stat. 1376 (2010).
- [14] G20, *Leaders’ Statement, The Pittsburgh Summit* (Sept. 24-25, 2009) at 9, available at [https://www.treasury.gov/resource-center/international/g7-g20/Documents/pittsburgh\\_summit\\_leaders\\_statement\\_250909.pdf](https://www.treasury.gov/resource-center/international/g7-g20/Documents/pittsburgh_summit_leaders_statement_250909.pdf).
- [15] See Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, tit. VII, Section 701, 124 Stat. 1376 (2010).
- [16] Core Principles and Other Requirements for Swap Execution Facilities, 78 FR 33476 (Jun. 4, 2013).
- [17] *Id.* at 33477.
- [18] See *Trading Organizations – Swap Execution Facilities (SEF)*, CFTC.GOV, <https://sirt.cftc.gov/SIRT/SIRT.aspx?Topic=SwapExecutionFacilities> (last visited Nov. 4, 2018).
- [19] See *FIA SEF Tracker*, FIA.ORG, <https://fia.org/node/1901/> (last visited Nov. 4, 2018).

[20] See Bank of England Staff Working Paper No. 580, Centralized Trading, Transparency and Interest Rate Swap Market Liquidity: Evidence from the Implementation of the Dodd-Frank Act (May 2018), pp. 2-4, 18-24, *available at* <https://www.bankofengland.co.uk/-/media/boe/files/working-paper/2018/centralized-trading-transparency-and-interest-rate-swap-market-liquidity-update>.