HEARING TO REVIEW H.R. 3283, H.R. 1838, AND H.R. 4235

HEARING

BEFORE THE

SUBCOMMITTEE ON
GENERAL FARM COMMODITIES
AND RISK MANAGEMENT

OF THE

COMMITTEE ON AGRICULTURE
HOUSE OF REPRESENTATIVES

ONE HUNDRED TWELFTH CONGRESS

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HEARING TO REVIEW H.R. 3283, H.R. 1838, AND H.R. 4235

WEDNESDAY, MARCH 28, 2012

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON GENERAL FARM COMMODITIES AND
RISK MANAGEMENT,
COMMITTEE ON AGRICULTURE,
Washington, D.C.

The Subcommittee met, pursuant to call, at 10:30 a.m., in Room 1300 of the Longworth House Office Building, Hon. K. Michael Conaway [Chairman of the Subcommittee] presiding.

Members present: Representatives Conaway, Neugebauer, Crawford, Huelskamp, Ellmers, Hultgren, Hartzler, Schilling, Boswell, McGovern, Scott, Sewell, and Peterson (*ex officio*)

Staff present: Tamara Hinton, Kevin Kramp, Ryan McKee, John Porter, Debbie Smith, Heather Vaughan, Suzanne Watson, Liz Friedlander, C. Clark Ogilvie, John Konya, and Jamie Mitchell.

OPENING STATEMENT OF HON. K. MICHAEL CONAWAY, A REPRESENTATIVE IN CONGRESS FROM TEXAS

The CHAIRMAN. Good morning. I call this hearing of the Subcommittee on General Farm Commodities and Risk Management to review H.R. 3283, the Swap Jurisdiction Certainty Act, H.R. 1838 to repeal section 716 of the Dodd-Frank, and H.R. 4235, the "Swap Data Repository and Clearinghouse Indemnification Correction Act of 2012," to come to order.

Well, good morning, and I want to thank all of you for joining us. I would like to extend a warm welcome to our panelists today, Mr. Chuck Vice of IntercontinentalExchange; Mr. Paul Saltzman of The Clearing House; Mr. Keith Bailey, Barclays Capital; and Michael Bodson, The Depository Trust & Clearing Corporation. Gentlemen, thank you for being here. I appreciate your time to come this morning and share your views with the Committee and have a chance to have your thumbs screwed to the table and grill you under hot lights. I am just kidding.

Today's meeting of the General Farm Commodities and Risk Management Subcommittee continues a series of hearings aimed at examining and correcting some of the problems that have arisen as regulators have worked through the Dodd-Frank rulemaking process. To the surprise of almost no one in this room except perhaps us here on the dais, Congress passed an imperfect bill. That is right. You heard it here last. The Dodd-Frank bill has some mistakes in it. That is about as funny as this CPA is going to get so

feel free to just have raucous laughter. There you go, I appreciate you sucking up to the chair.

Fortunately, two of the bills we are going to examine today are bipartisan solutions that will strengthen the underlying bill and reduce the unintended consequences of poorly vetted provisions and a third will provide clarity regarding the reach of Dodd-Frank to activities that occur outside the United States.

Our first bill, the "Swap Data Repository and Clearinghouse Indemnification Act," will remove requirements from Dodd-Frank that foreign regulators indemnify U.S. swap data repositories for any losses arising from the misuse of information the regulator requests from the SDR. And I thank you to both Ms. Sewell and Mr. Crawford—they are not here—for leading on this important issue.

Our second bill is the Swap Jurisdiction Certainty Act. This bill will provide clarity consistent with the Congressional intent regarding the territorial reach of Dodd-Frank provided this certainty will not only help market participants prepare for the new regulations but it will support coordination and organization with our international counterparts.

And finally, we will examine H.R. 1838, which modifies Section 718 of Dodd-Frank. Section 718 has the factor requiring banks to push some of their swap activities into separate standalone affiliates. H.R. 1838 would narrow the class of swaps covered by the rule to assure that the intent of segregating the riskiest swaps from a bank's balance sheet does not have the unintended consequence of needlessly diverting capital and introducing additional systemic risks.

As has been said many times, getting Dodd-Frank right is more important than getting it done quickly. Part of that means that Congress can never become complacent with its own handiwork. Our work did not end when it was signed into law by the President. Examining the rulemaking process for errors, unfinished instructions, and unintended consequences, and then fixing the mistakes is an essential part of our job.

I want to thank all Members of the Subcommittee on both sides of the aisle for their continued commitment to good oversight, support that Dodd-Frank, irrespective of our ideological differences, is implemented in a way that is logical, fair, and beneficial for the participants who depend on the financial markets. The three bills we are discussing today each improve Dodd-Frank in meaningful ways.

Finally, I want to again thank today's witnesses for their time. We on the Committee appreciate the opportunity to understand the unique perspectives each bring to this financial reform process.

[The prepared statement of Mr. Conaway follows:]

PREPARED STATEMENT OF HON. K. MICHAEL CONAWAY, A REPRESENTATIVE IN CONGRESS FROM TEXAS

Good morning, thank you all for joining us. I would like to extend a warm welcome to our panelists today: Mr. Charles Vice of IntercontinentalExchange; Mr. Paul Saltzman of The Clearing House; Mr. Keith Bailey of Barclays Capital; and Mr. Michael Bodson of the Depository Trust & Clearing Corporation.

Thank you each for taking the time to come to our Committee, to share your views, and to answer our questions.

Today's meeting of the General Farm Commodities and Risk Management Subcommittee continues a series of hearings aimed at examining and correcting some of the problems that have arisen as regulators have worked through the Dodd-Frank rulemaking process.

To the surprise of almost no one in this room—except perhaps to us up here on the dais—Congress passed an imperfect bill. That's right, you heard it hear last, Dodd-Frank has some mistakes.

Fortunately, two of the bills we are going to examine today are bipartisan solutions that will strengthen the underlying bill and reduce the unintended consequences of poorly vetted provisions; and a third will provide clarity regarding the reach of Dodd-Frank to activities that occur outside the U.S.

Our first bill, the "Swap Data Repository and Clearinghouse Indemnification Act," will remove requirements from Dodd-Frank that foreign regulators indemnify U.S. swap data repositories for any losses arising from the misuse of information the regulator requests from the SDR. Thank you to both Ms. Sewell and Mr. Crawford for leading on this important issue.

Our second bill is the "Swap Jurisdiction Certainty Act." This bill will provide clarity, consistent with Congressional intent, regarding the territorial reach of Dodd-Frank. Providing this certainty will not only help market participants prepare for the new regulations, but it will support coordination and harmonization with our international counterparts.

Finally, we will examine H.R. 1838, which modifies Section 716 of Dodd-Frank. Section 716 has the effect of requiring banks to push some of their swap activities into separate, stand-alone affiliates. H.R. 1838 would narrow the class of swaps covered by the rule, to ensure the intent of segregating the riskiest swaps from a bank's balance sheet does not have the unintended consequence of needlessly diverting capital or introducing additional systemic risk.

As I have said many times, getting Dodd-Frank right is more important than getting it done quickly. Part of that means that Congress can never become complacent with its own handiwork; our work did not end when this law was signed by the President. Examining the rulemaking process for errors, unclear instructions, or unintended consequences, and then fixing the mistakes is an essential part of our job.

I want to thank all the Members of this Subcommittee, on both sides of the aisle, for their continued commitment to good oversight. It is important that Dodd-Frank, irrespective of our ideological differences, is implemented in a way that is logical, fair, and beneficial for the participants who depend on the financial markets. The three bills we are discussing today each improve Dodd-Frank in meaningful ways.

Finally, I would like to again thank today's witnesses for their time; we on the Committee appreciate the opportunity to understand the unique perspectives each of you have on financial reform.

With that, I will turn to our Ranking Member, Mr. Boswell, for his opening remarks and then to our witnesses for their thoughts on how we can continue to improve Dodd-Frank.

I

112TH CONGRESS
1ST SESSION

H. R. 3283

To amend the Commodity Exchange Act and the Securities Exchange Act of 1934 to provide an exemption for certain swaps and security-based swaps involving non-U.S. persons, and for other purposes.

IN THE HOUSE OF REPRESENTATIVES

OCTOBER 31, 2011

Mr. HIMES (for himself and Mr. GARRETT) introduced the following bill; which was referred to the Committee on Financial Services, and in addition to the Committee on Agriculture, for a period to be subsequently determined by the Speaker, in each case for consideration of such provisions as fall within the jurisdiction of the committee concerned

---

A BILL

To amend the Commodity Exchange Act and the Securities Exchange Act of 1934 to provide an exemption for certain swaps and security-based swaps involving non-U.S. persons, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Swap Jurisdiction Certainty Act".

SEC. 2. COMMODITY EXCHANGE ACT.

Section 4s(a) of the Commodity Exchange Act (7 U.S.C. 6s(a)) is amended by adding at the end the following:

"(3) EXTRA-TERRITORIAL SWAP TRANSACTION APPLICATION OF TITLE VII.—

"(A) IN GENERAL.—A swap entered into between—

"(i) a swap dealer that is registered with the Commission who is either—

"(I) a U.S. person, or

"(II) a person that has a parent company that is a U.S. person, and

"(ii) a person who is—

"(I) a U.S. or non-U.S. subsidiary, branch, or affiliate of such swap dealer, or

"(II) any other non-U.S. person that is not registered as a swap dealer with the Commission,

shall not be subject to the provisions of title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act, and of amendments added by such title, so long as each swap dealer described under clause

(i) reports such swap to a swap data repository registered with the Commission.

"(B) SWAPS ENTERED INTO BY REGISTERED NON-U.S. PERSONS.—

"(i) IN GENERAL.—A non-U.S. person that registers as a swap dealer with the Commission shall only be subject to the requirements of title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act, and of amendments added by such title, with respect to swaps that such person enters into with a U.S. person who is not a U.S. subsidiary, branch, or affiliate of such non-U.S. person.

"(ii) CAPITAL REQUIREMENTS.—A non-U.S. person that registers as a swap dealer with the Commission shall be permitted by the Commission to comply with the capital requirements under subsection (e) by complying with comparable requirements established by the appropriate governmental authorities in the home country of the non-U.S. person, so long as such home country is a signatory to the Basel Accords.

"(C) NON-U.S. PERSON.—For purposes of this paragraph, the term 'non-U.S. person' includes—

"(i) any person that is not a U.S. person;

"(ii) any discretionary account or similar account (other than an estate or trust) held for the benefit or account of a non-U.S. person by a dealer or other professional fiduciary organized, incorporated, or (if an individual) resident in the United States;

"(iii) any agency or branch of a U.S. person located outside the United States if—

"(I) the agency or branch operates for valid business reasons; and

"(II) the agency or branch is engaged in the business of insurance or banking and is subject to substantive insurance or banking regulation, respectively, in the jurisdiction where it is located;

"(iv) any trust of which any professional fiduciary acting as trustee is a U.S. person, if—

"(I) a trustee who is a non-U.S. person has sole or shared investment discretion with respect to the trust assets; and

"(II) no beneficiary of the trust (and no settlor if the trust is revocable) is a U.S. person;

"(v) an employee benefit plan established and administered in accordance with the law, customary practices, and documentation of a country other than the United States; and

"(vi) the International Monetary Fund, the International Bank for Reconstruction and Development, the Inter-American Development Bank, the Asian Development Bank, the African Development Bank, the United Nations, a central bank or its functional equivalent which is located in a non-U.S. jurisdiction and that is a signatory to the Basel Accords, and their agencies, affiliates and pension plans,

and any other similar international organizations, their agencies, affiliates and pension plans.

"(D) U.S. PERSON.—For purposes of this paragraph, the term 'U.S. person' includes—

"(i) any natural person resident in the United States;

"(ii) any partnership or corporation organized or incorporated under the laws of the United States;

"(iii) any estate of which any executor or administrator is a U.S. person;

"(iv) any trust of which any trustee is a U.S. person;

"(v) any agency or branch of a foreign entity located in the United States;

"(vi) any non-discretionary account or similar account (other than an estate or trust) held by a dealer or other fiduciary for the benefit or account of a United States person;

"(vii) any discretionary account or similar account (other than an estate or trust) held by a dealer or other fiduciary

organized, incorporated, or (if an individual) resident in the United States; and

"(viii) any partnership or corporation—

"(I) organized or incorporated under the laws of any foreign jurisdiction; and

"(II) formed by a U.S. person principally for the purpose of investing in securities not registered under the Securities Act of 1933, unless it is organized or incorporated, and owned, by accredited investors (as such term is defined under section 230.501 of title 17, Code of Federal Regulations) that are not natural persons, estates, or trusts.

"(E) ANTI-EVASION.—Notwithstanding any other provision of this paragraph, each registered swap dealer shall be subject to the provision under section 2(i)(2).".

SEC. 3. SECURITIES EXCHANGE ACT OF 1934.

Section 15F(a) of the Securities Exchange Act of 1934 (78o–10(a)) is amended by adding at the end the following:

"(3) EXTRA-TERRITORIAL SWAP TRANSACTION APPLICATION OF TITLE VII.—

"(A) IN GENERAL.—A security-based swap entered into between—

"(i) a security-based swap dealer that is registered with the Commission who is either—

"(I) a U.S. person, or

"(II) a person that has a parent company that is a U.S. person, and

"(ii) a person who is—

"(I) a U.S. or non-U.S. subsidiary, branch, or affiliate of such security-based swap dealer, or

"(II) any other non-U.S. person that is not registered as a security-based swap dealer with the Commission,

shall not be subject to the provisions of title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act, and of amendments added by such title, so long as each security-based swap dealer described under clause (i) reports such security-based swap to a security-based swap

1 data repository registered with the Com-
2 mission.
3 "(B) SECURITY-BASED SWAPS ENTERED
4 INTO BY REGISTERED NON-U.S. PERSONS.—
5 "(i) IN GENERAL.—A non-U.S. person
6 that registers as a security-based swap
7 dealer with the Commission shall only be
8 subject to the requirements of title VII of
9 the Dodd-Frank Wall Street Reform and
10 Consumer Protection Act, and of amend-
11 ments added by such title, with respect to
12 security-based swaps that such person en-
13 ters into with a U.S. person who is not a
14 U.S. subsidiary, branch, or affiliate of such
15 non-U.S. person.
16 "(ii) CAPITAL REQUIREMENTS.—A
17 non-U.S. person that registers as a secu-
18 rity-based swap dealer with the Commis-
19 sion shall be permitted by the Commission
20 to comply with the capital requirements
21 under subsection (e) by complying with
22 comparable requirements established by
23 the appropriate governmental authorities
24 in the home country of the non-U.S. per-

son, so long as such home country is a signatory to the Basel Accords.

"(C) NON-U.S. PERSON.—For purposes of this paragraph, the term 'non-U.S. person' includes—

"(i) any person that is not a U.S. person;

"(ii) any discretionary account or similar account (other than an estate or trust) held for the benefit or account of a non-U.S. person by a dealer or other professional fiduciary organized, incorporated, or (if an individual) resident in the United States;

"(iii) any agency or branch of a U.S. person located outside the United States if—

"(I) the agency or branch operates for valid business reasons; and

"(II) the agency or branch is engaged in the business of insurance or banking and is subject to substantive insurance or banking regulation, respectively, in the jurisdiction where it is located;

"(iv) any trust of which any professional fiduciary acting as trustee is a U.S. person, if—

"(I) a trustee who is a non-U.S. person has sole or shared investment discretion with respect to the trust assets; and

"(II) no beneficiary of the trust (and no settlor if the trust is revocable) is a U.S. person;

"(v) an employee benefit plan established and administered in accordance with the law, customary practices, and documentation of a country other than the United States; and

"(vi) the International Monetary Fund, the International Bank for Reconstruction and Development, the Inter-American Development Bank, the Asian Development Bank, the African Development Bank, the United Nations, a central bank or its functional equivalent which is located in a non-U.S. jurisdiction and that is a signatory to the Basel Accords, and their agencies, affiliates and pension plans,

and any other similar international organizations, their agencies, affiliates and pension plans.

"(D) U.S. PERSON.—For purposes of this paragraph, the term 'U.S. person' includes—

"(i) any natural person resident in the United States;

"(ii) any partnership or corporation organized or incorporated under the laws of the United States;

"(iii) any estate of which any executor or administrator is a U.S. person;

"(iv) any trust of which any trustee is a U.S. person;

"(v) any agency or branch of a foreign entity located in the United States;

"(vi) any non-discretionary account or similar account (other than an estate or trust) held by a dealer or other fiduciary for the benefit or account of a United States person;

"(vii) any discretionary account or similar account (other than an estate or trust) held by a dealer or other fiduciary

organized, incorporated, or (if an individual) resident in the United States; and

"(viii) any partnership or corporation—

"(I) organized or incorporated under the laws of any foreign jurisdiction; and

"(II) formed by a U.S. person principally for the purpose of investing in securities not registered under the Securities Act of 1933, unless it is organized or incorporated, and owned, by accredited investors (as such term is defined under section 230.501 of title 17, Code of Federal Regulations) that are not natural persons, estates, or trusts.

"(E) ANTI-EVASION.—Notwithstanding any other provision of this paragraph, a registered security-based swap dealer shall not conduct any activities that are designed to evade any provision of this Act that was enacted by the Wall Street Transparency and Accountability Act of 2010.".

○

H.R. 1838, To repeal a provision of the Dodd-Frank Wall Street Reform and Consumer Protection Act prohibiting any Federal bailout of swap dealers or participants.

I

112TH CONGRESS
1ST SESSION

H. R. 1838

To repeal a provision of the Dodd-Frank Wall Street Reform and Consumer Protection Act prohibiting any Federal bailout of swap dealers or participants.

IN THE HOUSE OF REPRESENTATIVES

MAY 11, 2011

Ms. HAYWORTH introduced the following bill; which was referred to the Committee on Financial Services, and in addition to the Committee on Agriculture, for a period to be subsequently determined by the Speaker, in each case for consideration of such provisions as fall within the jurisdiction of the committee concerned

---

A BILL

To repeal a provision of the Dodd-Frank Wall Street Reform and Consumer Protection Act prohibiting any Federal bailout of swap dealers or participants.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. REPEAL.

Section 716 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (15 U.S.C. 8305) is repealed.

○

H.R. 4235, To amend the Securities Exchange Act of 1934 and the Commodity Exchange Act to repeal the indemnification requirements for regulatory authorities to obtain access to swap data required to be provided by swaps entities under such Acts.

I

112TH CONGRESS
2D SESSION

H. R. 4235

To amend the Securities Exchange Act of 1934 and the Commodity Exchange Act to repeal the indemnification requirements for regulatory authorities to obtain access to swap data required to be provided by swaps entities under such Acts.

IN THE HOUSE OF REPRESENTATIVES

MARCH 21, 2012

Mr. DOLD (for himself and Ms. MOORE) introduced the following bill; which was referred to the Committee on Agriculture, and in addition to the Committee on Financial Services, for a period to be subsequently determined by the Speaker, in each case for consideration of such provisions as fall within the jurisdiction of the committee concerned

---

A BILL

To amend the Securities Exchange Act of 1934 and the Commodity Exchange Act to repeal the indemnification requirements for regulatory authorities to obtain access to swap data required to be provided by swaps entities under such Acts.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

SECTION 1. REPEAL OF INDEMNIFICATION REQUIREMENTS.

(a) DERIVATIVES CLEARING ORGANIZATIONS.—Section 5b(k)(5) of the Commodity Exchange Act (7 U.S.C. 7a–1(k)(5)) is amended to read as follows:

"(5) CONFIDENTIALITY AGREEMENT.—Before the Commission may share information with any entity described in paragraph (4), the Commission shall receive a written agreement from each entity stating that the entity shall abide by the confidentiality requirements described in section 8 relating to the information on swap transactions that is provided.".

(b) SWAP DATA REPOSITORIES.—Section 21(d) of the Commodity Exchange Act (7 U.S.C. 24a(d)) is amended to read as follows:

"(d) CONFIDENTIALITY AGREEMENT.—Before the swap data repository may share information with any entity described in subsection (c)(7), the swap data repository shall receive a written agreement from each entity stating that the entity shall abide by the confidentiality requirements described in section 8 relating to the information on swap transactions that is provided.".

(c) SECURITY-BASED SWAP DATA REPOSITORIES.—Section 13(n)(5)(H) of the Securities Exchange Act of

1934 (15 U.S.C. 78m(n)(5)(H)) is amended to read as follows:

"(H) CONFIDENTIALITY AGREEMENT.—Before the security-based swap data repository may share information with any entity described in subparagraph (G), the security-based swap data repository shall receive a written agreement from each entity stating that the entity shall abide by the confidentiality requirements described in section 24 relating to the information on security-based swap transactions that is provided.".

(d) EFFECTIVE DATE.—The amendments made by this Act shall take effect as if enacted as part of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Public Law 111–203) on July 21, 2010.

○

The CHAIRMAN. I would like to turn to my Ranking Member and good friend, Mr. Boswell, for his opening remarks.

OPENING STATEMENT OF HON. LEONARD L. BOSWELL, A REPRESENTATIVE IN CONGRESS FROM IOWA

Mr. BOSWELL. Well, thank you, Mr. Chairman.

It is preliminary for my short remarks here, but we don't always agree. It is kind of interesting for us, the relationship, because I like you. That is my attempt at responding to humor but, no, it is true. I do like this man and I know something about where he comes from; I know something about the territory down there. I don't know if I have ever told you I was a roughneck in the oilfields just north of Monahans when I was a young man.

The CHAIRMAN. Let me see all five fingers. You got them all?

Mr. BOSWELL. I got them all.

The CHAIRMAN. All right, good.

Mr. BOSWELL. And I did lee tones, I did backups, I did the tower and it was an old standard tower where I got up there and I was a youngster, and the old driller had me up there and he said after—you know what I am talking about.

The CHAIRMAN. Yes.

Mr. BOSWELL. Yes. I bet you haven't done it but I bet you know what I am talking about.

The CHAIRMAN. *Au contraire.*

Mr. BOSWELL. Okay.

The CHAIRMAN. I spent summers roughnecking for Parker Drilling Company and Sharpe Drilling Company——

Mr. BOSWELL. Okay.

The CHAIRMAN.—and I still have all my fingers.

Mr. BOSWELL. Anyway, we are up in the tower and the well was about to come in. It was the old standard tower before the jackknives. I am kind of remembering the lingo here a little bit. And so I was substituting for people going on vacation. That was what my—the guy in the tower. I was a little nervous about it. I didn't mind heights and that kind of helped later on. I got into aviation, flying airplanes, and jumping out of airplanes. But there I was up in the standard tower way up there. And we were going to take the pipe out and change the bit, going to be up there a while and so I finally asked. I said what happens if there is a fire—because they kept telling us about safety. Oh, he said. I was going to tell you that just before I left and he showed me that little piece of cable with the handles on it and that cable went way out to a stake. He said if something happens, he said, your only escape is to wrap that thing around that cable, grab those handles, and you are going to slide down that and you are going to slow your speed down by putting pressure on it. He said we don't have time for you to practice. That was a sobering moment for a guy who was not quite 18 years old.

The CHAIRMAN. Well, but you would have been motivated to do it. It was called the Geronimo line and it is politically incorrect today to call it that but——

Mr. BOSWELL. Yes. Well, anyway. So I do thank you for the little dialogue there, but that is a little background.

And I want to thank our witnesses and everyone for joining us today as we review the implementation of Dodd-Frank Wall Street Reform Act, global derivatives, and so on. I am proud to say that this Committee is genuinely the more bipartisan operation in the House of Representatives and I think you have just seen the reason why.

In this effort, Chairman Conaway and I have introduced legislation not for today but legislation I hope makes it to the House floor for passage, H.R. 1840, which would improve cost-benefit analysis and operations of the CFTC.

Agricultural and the financial markets have a unique relationship that we need to be reminded of more regularly. Since the passage of Dodd-Frank, I have been wanting the change in this bill and the regulations surrounding it to ensure that farmers, producers, and their communities are not hurt by another financial market crisis.

I think it is clear to financiers that the hedging risk is a critical aspect of running a successful farm operation and doing so is good business for rural cooperatives and banks and producer communities. However, we must remind ourselves that not only does the integrity of our financial market impact our commodities but that our financial market relies on the commodities that hard-working Americans produce. Without them, there would be no basis for the derivatives traded among our banking institutions today.

The market was created in the heartland to improve the commodity market and preserve the value of both commodities and seasonal goods in the face of unforeseeable risks such as drought and flooding. This reliance and the integrity of our markets are critical to our nation for jobs, a healthy economy, and affordable food. Distortions of commodity values in trading have a negative impact on our long-term economic outlook and often place unfair costs on commodity consumers such as the speculation on Wall Street that some of us think raises gas prices on consumers.

I hope that we can have a healthy discussion of these issues and that your testimony here will improve functions in Congress and add to our understanding of the legislation before us. So I look forward to hearing the coming testimonies and working with you to ensure fair and practical implementation both at home and with our global partners on behalf of American taxpayers.

And I would say in closing that Dodd-Frank is not perfect. I think we all knew that when we started out. And it wasn't done overnight. A lot of pressure was on and I watched closely as this Committee and the Finance Committee worked on that for months, just not perfect. And I thought we all would surely expect some tweaking as the rubber hits the road and we get out there and put it in force. And that is what I am very willing to do. Other major legislation has required that so why wouldn't we expect this? But we don't want the debacle that happened that caused us to do that extensive review to happen again if we can prevent it.

So with that again, Mr. Chairman, thank you so much and I look forward to the hearing.

[The prepared statement of Mr. Boswell follows:]

PREPARED STATEMENT OF HON. LEONARD L. BOSWELL, A REPRESENTATIVE IN CONGRESS FROM IOWA

Thank you, Chairman Conaway. I would like to thank our witnesses and everyone for joining us today as we review implementation of the Dodd-Frank Wall Street Reform Act and global derivatives reform.

I'm proud to say that this Committee is generally one of our more bipartisan operations in the House of Representatives. In this effort, Chairman Conaway and I have introduced legislation not before you today, but legislation that I hope makes it to the House floor for passage, H.R. 1840, which would improve cost-benefit analysis and operations at the CFTC.

Agriculture and the financial markets have a unique relationship that we need to be reminded of more regularly. Since the passage of Dodd Frank, I have been monitoring the changes to this bill and the regulations surrounding it to ensure that farmers, producers, and their communities are not hurt by another financial market crisis.

I think it is clear to financiers that the hedging risk is a critical aspect of running a successful farm operation, and doing so is good business for rural cooperatives and banks in producer communities.

However, we must remind ourselves that, not only does the integrity of our financial market impact our commodities, but that our financial market relies on the commodities that hard working Americans produce. Without them, there would be no basis for the derivatives traded among our banking institutions today. The market was created in the heartland to improve the commodity market, and preserve the value of bulk commodities and seasonal goods in the face of unforeseeable risk such as drought and flooding.

This reliance and the integrity of our markets are critical to our nation for jobs, a healthy economy, and affordable food. Distortions of commodity values in trading have a negative impact on our long term economic outlook, and often place unfair costs on commodity consumers—such as the speculation on Wall Street that raises gas prices on consumers.

I hope that we can have a healthy discussion on these issues and that your testimony here will improve functions in Congress and add to our understanding of the legislation before us.

I look forward to hearing the coming testimonies and working with you to ensure fair and practical implementation both at home and with our global partners on behalf of American taxpayers.

Thank you.

The CHAIRMAN. I would like to thank the Ranking Member and remind that the chair has requested other Members to submit their opening statements for the record so the witnesses may begin their testimony to ensure that there is ample time for questions.

I would like to introduce our panel now. First up will be Mr. Chuck Vice, President, Chief Operating Officer, IntercontinentalExchange, Atlanta, Georgia; Mr. Paul Saltzman, President of The Clearing House Association, L.L.C., Executive Vice President and General Counsel, The Clearing House Payments Company, L.L.C., New York, New York; Mr. Keith Bailey, Managing Director, Fixed Income, Currencies and Commodities Division, Barclays Capital, on behalf of the Institute of International Bankers, New York, New York; and Mr. Michael Bodson, COO of The Depository Trust & Clearing Corporation, New York, New York. Thank you, gentlemen.

Mr. Vice, 5 minutes.

STATEMENT OF CHARLES A. VICE, PRESIDENT AND CHIEF OPERATING OFFICER, INTERCONTINENTALEXCHANGE, INC., ATLANTA, GA

Mr. VICE. Chairman Conaway, Ranking Member Boswell, my name is Chuck Vice. I am President and Chief Operating Officer at ICE. I appreciate the opportunity to appear before you today to testify on the extraterritorial application of the Dodd-Frank Wall

Street Reform and Consumer Protection Act, and in particular, the Swap Jurisdiction Certainty Act and "Swap Data Repository and Clearinghouse Indemnification Correction Act of 2012."

Since the launch of our Atlanta-based electronic OTC energy marketplace in 2000, ICE has expanded both in the United States and internationally. Over the past 10 years, ICE has acquired or founded derivative exchanges and clearinghouses in the United States, the UK, and Canada. As such, ICE is uniquely impacted by the financial reform efforts in the United States and abroad.

ICE has been supportive of the global financial reform efforts. Appropriate regulation of derivatives is of utmost importance to the financial system. However, the broad mandates of the Dodd-Frank Act create great uncertainty for international transactions and global businesses. While the CFTC and SEC have issued dozens of proposed and final regulations implementing the Dodd-Frank Act to date neither agency has defined what activity has a direct and significant impact on the United States. In particular, many of the CFTC's final rules require ICE to come into compliance without knowing whether our business is within the scope of Dodd-Frank.

Therefore, ICE welcomes the introduction of H.R. 3283, the Swap Jurisdiction Certainty Act, which would make two important clarifications to Dodd-Frank by defining U.S. person and non-U.S. person and by clarifying the applicability of Dodd-Frank requirements on international transactions. ICE believes that H.R. 3283 is an important step toward redefining what transactions and participants are subject to Dodd-Frank.

In addition, I support the introduction of H.R. 4235, the "Swap Data Repository and Clearinghouse Indemnification Act." One of ICE's subsidiaries, Trade Vault, has applied for registration with the CFTC as a Swap Data Repository, or SDR. Section 728 of Dodd-Frank requires foreign regulators to indemnify an SDR for any expenses resulting from litigation for data provided by the SDR to the foreign regulator. ICE believes that this provision is an error as most foreign regulators would be legally unable to indemnify an SDR. This would result in forcing an SDR to create separate subsidiaries in other countries to provide swaps transparency to foreign regulators.

ICE has always been and continues to be a strong proponent of open and competitive markets and appreciates the opportunity to work closely with Congress and regulators in the United States and abroad to address the evolving regulatory challenges presented by derivatives market.

Mr. Chairman, thank you for the opportunity to share our views with you. I would be happy to answer any questions.

[The prepared statement of Mr. Vice follows:]

PREPARED STATEMENT OF CHARLES A. VICE, PRESIDENT AND CHIEF OPERATING OFFICER, INTERCONTINENTALEXCHANGE, INC., ATLANTA, GA

Chairman Conaway, Ranking Member Boswell, I am Chuck Vice, President and Chief Operating Officer of IntercontinentalExchange, Inc., (ICE). I appreciate the opportunity to appear before you today to testify on the extraterritorial application of the Dodd-Frank Wall Street Reform and Consumer Protection Act and in particular, the "Swap Jurisdiction Certainty Act" and the "Swap Data Repository and Clearinghouse Indemnification Correction Act of 2012."

Background

Since the launch of its Atlanta, Georgia based electronic OTC energy marketplace in 2000, ICE has expanded both in the U.S. and internationally. Over the past 10 years, ICE has acquired or founded three derivatives exchanges and five clearing houses in the U.S., the UK, Brazil and Canada. Through our global operations, ICE's exchanges or clearing houses are directly regulated by the UK Financial Services Authority (FSA), the U.S. Commodity Futures Trading Commission (CFTC), the Securities and Exchange Commission (SEC) and the Manitoba Securities Commission. In addition, each exchange and clearing house is subject to lesser regulation or registration requirements with dozens of other jurisdictions. As such, ICE is uniquely impacted by the financial reforms efforts in the U.S. and abroad.

ICE has been supportive of the global financial reform efforts. Appropriate regulation of derivatives is of utmost importance to the financial system. ICE believes that increased transparency and proper risk and capital management, coupled with legal and regulatory certainty, are central to reform and to restoring confidence to these vital markets.

However, regulators need clear lines of jurisdiction. Regulators need certainty that they have the power to take actions to uphold the public good. Likewise, market participants need the certainty that their business transactions will not be held to conflicting standards of conduct. Further, regulatory certainty eliminates the possibility of regulatory arbitrage, or long-term damage to the competitiveness of the U.S. in a highly competitive global environment.

The need for certainty extends beyond U.S. borders. It is vital to recognize that the derivatives markets are international: the majority of the large companies globally use derivatives, and they conduct these transactions with U.S. counterparties. Thus, U.S. regulators must work with international regulators from a common set of regulatory principles. With this comes the recognition that no single country can regulate the entire global derivatives market.

The Unclear Extraterritorial Application of Dodd-Frank Creates Uncertainty

Unfortunately, the broad mandates of the Dodd-Frank Act create great uncertainty for international transactions and global businesses. The sole recognition of applicability of Dodd-Frank to international transactions is in Section 722 of Dodd-Frank which states "[t]he provisions of this Act relating to swaps that were enacted by the Wall Street Transparency and Accountability Act of 2010 . . . shall not apply to activities outside the United States unless those activities:

> (1) have a direct and significant connection with activities in, or effect on, commerce of the United States, or
>
> (2) contravene such rules or regulations as the Commission may prescribe . . . or to prevent the evasion of any provision of this Act . . ."

While the CFTC and SEC have issued dozens of proposed and final regulations implementing the Dodd-Frank Act, to date, neither agency has defined what activity has a direct and significant impact on the United States. In particular, many of the CFTC's final rules require ICE to come into compliance without ICE knowing whether our business is within the scope of Dodd-Frank. For example, our UK-based clearing house, ICE Clear Europe operates as a UK regulated Recognized Clearing House and a U.S. CFTC regulated Derivatives Clearing Organization and SEC regulated Clearing Agency. ICE Clear Europe clears European and Asian energy contracts which have little to no U.S. participation. However, it is unclear to ICE whether Dodd-Frank will apply to these transactions, even though the U.S. connection is negligible. Moreover, as an illustration of the complication of overlapping regulators, ICE Clear Europe is expected to seek approval for energy swaps from UK FSA, the CFTC and the SEC. Having to file approvals to clear swaps with three primary regulators, including one, the SEC, with no expertise in energy derivatives, hampers Dodd-Frank by making clearing swaps much more difficult for a clearing house.

Before Dodd-Frank, this overlap in regulation was not the case. Since 1984, Section 4(b) of the Commodity Exchange Act expressly excluded foreign transactions from CFTC jurisdiction. The CFTC relied on foreign regulators to regulate foreign transactions and worked with regulators to adopt common principles that all regulated markets should adopt. This approach was very successful, as it led to greater harmonization of regulation, yet allowed foreign regulators to oversee their institu-

tions. Importantly, many of the key goals of Dodd-Frank, such as swaps clearing and electronic trading, originally came from foreign markets.[1]

H.R. 3283, the Swap Jurisdiction Certainty Act

ICE welcomes the introduction of H.R. 3283, the Swaps Jurisdiction Certainty Act, which would make two important clarifications to Dodd-Frank by defining U.S. person and non-U.S. person and by clarifying the applicability of Dodd-Frank requirements on international transactions. ICE believes that H.R. 3283 is an important step forward to defining what transactions and participants are subject to Dodd-Frank.

"Swap Data Repository and Clearinghouse Indemnification Correction Act of 2012"

ICE also welcomes the introduction H.R. 4235, the "Swap Data Repository and Clearinghouse Indemnification Correction Act of 2012." One of ICE's subsidiaries, Trade Vault, has applied for registration with the CFTC as a Swap Data Repository (SDR). Section 728 of Dodd-Frank requires foreign regulators to indemnify a SDR for any expenses resulting from litigation for data provided by the SDR to the foreign regulator. ICE believes that this provision is in error as most foreign regulators would be legally unable to indemnify a SDR. This would result in forcing an SDR to create separate subsidiaries in other countries to provide swaps transparency to foreign regulators. ICE believes the Swap Data Repository and Clearinghouse Indemnification Correction Act will correct this provision of Dodd-Frank and allow U.S. SDRs to provide transparency for international swaps transactions.

Conclusion

ICE has always been and continues to be a strong proponent of open and competitive markets, and appreciates the opportunity to work closely with Congress and regulators in the U.S. and abroad to address the evolving regulatory challenges presented by derivatives market.

Mr. Chairman, thank you for the opportunity to share our views with you. I would be happy to answer any questions you may have.

The CHAIRMAN. Thank you, Mr. Vice.

Mr. Saltzman, 5 minutes.

STATEMENT OF PAUL SALTZMAN, PRESIDENT, THE CLEARING HOUSE ASSOCIATION L.L.C.; EXECUTIVE VICE PRESIDENT AND GENERAL COUNSEL, THE CLEARING HOUSE PAYMENTS COMPANY L.L.C., NEW YORK, NY

Mr. SALTZMAN. Chairman Conaway, Ranking Member Boswell, and Members of the Subcommittee, my name is Paul Saltzman and I am President of The Clearing House Association. I appreciate the invitation to appear before you this morning to share The Clearing House views on legislation currently pending before your Subcommittee.

The Clearing House was founded in 1853 and today is the nation's oldest banking association. We are a nonpartisan advocacy group that represents the interest of our owner banks in a variety of legal, legislative, and regulatory issues. Our members include the largest U.S. commercial banking organizations including regional banks, as well as several leading non-U.S. domiciled banks.

The Clearing House has been asked to testify on two of the three legislative proposals on this morning's hearing agenda, but before I do that, I would like to make clear that we are not here to advocate for fundamental changes to Title VII of Dodd-Frank nor do we take issue with the underlying policy goals in Title VII to increase transparency in the derivatives markets, identify and mitigate

[1] EUREX pioneered electronic trading and the London Clearing House founded SwapsClear, an early clearing solution for OTC derivatives.

against risk in the financial system, and promote overall market integrity. We embrace those goals.

I am here, however, to express our strong support for two thoughtful, targeted, balanced, and bipartisan bills neither of which would in any way undermine the protections afforded by the new regulatory regime established in Title VII.

Let me start with H.R. 1838 and one clarification of my own. My comments today are addressed to the bipartisan substitute amendment adopted by voice vote last month in the House Financial Services Committee, not the original bill as introduced in the House. The legislation would essentially do four things. First, it would permit banks to engage in swap activity for hedging and other similar risk-mitigating activities that are directly related to the bank's activities. Second, it would allow banks to engage in a broader range of swap activity than currently permissible under Section 716 other than structured finance swaps. Third, it would eliminate any ambiguity that bank exemptions to the push-out rule are also available to uninsured U.S. branches and agencies of non-U.S. banks. And finally, the bill would clarify that the push-out rule does not apply to swap activity conducted outside the United States between a non-U.S. swap entity which includes a non-U.S. branch of U.S. depository institution or a non-U.S. subsidiary and a non-U.S. counterparty.

We believe these modifications to Section 716 would preserve benefits that are derived from centralizing swap activity in a single entity. The enactment of H.R. 1838 would also reduce the competitive disadvantages that U.S. banks currently face under Section 716 as compared to their non-U.S. bank counterparts that are not subject to the similar push-out requirement and likely never will be.

Let me next turn to the Swap Jurisdiction Certainty Act, H.R. 3283. H.R. 3283 also involves the scope of certain Title VII requirements and is intended to provide clarity regarding the extraterritorial impact of Title VII. The statutory language itself makes it clear that the requirements of Title VII do not apply to activity outside the United States unless such activity has a direct and significant connection with activities in or effect on commerce in the United States or an entity seeking to evade U.S. law and regulation. We believe that the application of Title VII's requirements to U.S. banking organizations operations outside of the United States would run contrary to the statutory provision. Concerns have been raised that absent this statutory clarification, the CFTC or the SEC could apply Title VII broadly to U.S. banks non-U.S. operations in a manner that is inconsistent with Title VI.

Specifically, the regulators could seek to apply these Title VII requirements both to non-U.S. subsidiaries of U.S. banks, as well as to non-U.S. branches of U.S. banks that register as swap dealers even when the activity conducted by such non-U.S. operations occurs outside the United States. An extraterritorial application of these requirements would create an unlevel playing field for U.S. banking organizations that compete outside the United States with non-U.S. banks that would be required to register as swap dealers under Title VII.

Extending the scope of Title VII to non-U.S. transactions will also have a negative impact on commercial end-users and will make their hedging activities more costly and less efficient. Although the scope of extraterritorial application of Title VII remains uncertain and subject to final rulemaking and regulatory interpretation, H.R. 3283 would provide the legal certainty necessary for market participants and end-users and more clearly defining Title VII's intended extraterritorial scope.

In summary, The Clearing House and its members strongly endorse swift passage and enactment of these two bipartisan bills. Thank you very much for your time and consideration, I appreciate the opportunity to testify and would be pleased to answer any questions you might have.

[The prepared statement of Mr. Saltzman follows:]

PREPARED STATEMENT OF PAUL SALTZMAN, PRESIDENT, THE CLEARING HOUSE ASSOCIATION L.L.C.; EXECUTIVE VICE PRESIDENT AND GENERAL COUNSEL, THE CLEARING HOUSE PAYMENTS COMPANY L.L.C., NEW YORK, NY

Chairman Conaway, Ranking Member Boswell and Members of the Subcommittee, my name is Paul Saltzman, and I am President of The Clearing House Association L.L.C. ("The Clearing House"). I appreciate the invitation to appear before you this morning to share The Clearing House's views on the important legislation currently pending before your Subcommittee.

Established in 1853, The Clearing House is the oldest banking association in the United States. We are a nonpartisan advocacy organization and represent our owner banks on a variety of legal, legislative, and regulatory issues. Our members include the largest U.S. commercial banking organizations, including large regional banks, as well as several leading non-U.S. domiciled banks. I am also Executive Vice President and General Counsel of our affiliate, The Clearing House Payments Company L.L.C., which provides payment, clearing, and settlement services to its member banks and other financial institutions. The Clearing House Payments Co. clears almost $2 trillion and 63 million transactions every day in automated-clearing-house, funds-transfer, and check-image payments made in the United States.

The Clearing House has been asked to testify today on two of the three legislative proposals on this morning's hearing agenda. But before I do that, I would like to make clear that we are not here today to advocate for any fundamental changes to the basic protections that are embodied in Title VII of the Dodd-Frank Act ("Dodd-Frank"). Nor does The Clearing House take issue with the overarching policy goals expressed by Congress in Title VII to increase transparency in the derivatives markets; identify and mitigate against risk in the financial system; and promote overall market integrity. On the contrary, we fully embrace those goals. Instead, I am here today, on behalf of The Clearing House and its members, to express our strong support for two thoughtful, targeted, balanced, and bipartisan bills, neither of which would in any way undermine the new regulatory regime established by Title VII. The two bills are H.R. 1838, which would amend the so-called bank derivatives "push-out" provisions of Section 716 of Dodd-Frank;[1] and H.R. 3283, the "Swaps Jurisdiction Certainty Act." We strongly support both bills and urge their swift passage. These carefully crafted, bipartisan proposals would provide clarity and help avoid unintended consequences. The first bill, H.R. 1838, would clarify the scope of swaps and security-based swaps activities that may be conducted in a bank and would clearly extend the exemptions to the push-out requirement in Section 716 to uninsured U.S. branches and agencies of non-U.S. banks. The second bill, H.R. 3283, would clarify the extent to which the requirements of Title VII applicable to swap and security-based swap transactions would apply extraterritorially and to inter-affiliate transactions. These bills will enhance the efficiency of the risk management services provided by banks to their commercial counterparties, and facilitate the banks' management of the risks to which they are exposed in their business activities.

[1] As requested, this testimony addresses the bipartisan substitute amendment to H.R. 1838, adopted in the Financial Services Committee on Feb. 16, 2012, not H.R. 1838 as originally introduced on May 11, 2011.

Although some of the concerns targeted by these bills could potentially be addressed through appropriately tailored regulations and interpretations by the Commodity Futures Trading Commission ("CFTC"), the Securities and Exchange Commission ("SEC"), and the prudential bank supervisors, we strongly believe that enactment of these two bipartisan bills is a better approach, which will provide greater certainty and address any limitations on the authority of the regulators. Moreover, the bills would provide needed clarity regarding the scope of these particular Title VII provisions and the Congressional intent underlying them.

In short, we believe these bills provide balanced and reasonable solutions to serious risks posed by the swaps push-out provision and the application of certain Title VII requirements to extraterritorial and inter-affiliate transactions, targeting, in each case, the most troublesome, and likely unintended, consequences.

Swaps Push-Out and H.R. 1838

Section 716

In general, and unless amended prior to its effective date,[2] Sec. 716 will require that U.S. insured depository institutions and U.S. branches and agencies of non-U.S. banks "push out" certain types of swaps dealing activity from the bank (or the branch). Sec. 716 provides exemptions for "insured depository institutions" (but not explicitly for uninsured U.S. branches and agencies, as discussed below) that would permit them to engage in (i) hedging and risk-mitigating swaps activity; and (ii) swaps involving rates, currencies, and other underlying assets that are permissible for national banks, including cleared credit default swaps. However—and importantly for commercial and agricultural end-users throughout the country—most commodity swaps currently conducted by banks,[3] both large and small, are subject to the push-out requirement in Sec. 716.

H.R. 1838 would amend Section 716 to:

- permit banks to engage in swap activity for hedging and other similar risk mitigating activities that are directly related to the bank's activities;
- permit banks to engage in swaps and security-based swaps activity other than most types of structured finance swaps;
- eliminate any ambiguity that the exemptions from the requirement to push-out swaps activity that are clearly available to insured depository institutions are also available to uninsured U.S. branches and agencies of non-U.S. banks; and
- clarify that the push-out requirement does not apply to swap or security-based swap activity outside the United States between a non-U.S. swap entity, which includes a non-U.S. branch of a U.S. depository institution or a non-U.S. subsidiary, and a non-U.S. counterparty.

Benefits of H.R. 1838

Because H.R. 1838 would permit banks to continue to engage in a wider range of swaps and security-based swaps activity without creating safety and soundness risk, it would be a significant step towards addressing concerns that have been raised regarding the negative unintended consequences of Sec. 716. Indeed, U.S. bank regulators have raised concerns about the potential harm the push-out requirement could have on the safety and soundness of institutions that are subject to its prohibition, as well as its potential to increase systemic risk. For example, in a May 12, 2010, letter to the Chairman of the Senate Banking Committee, Chairman Bernanke wrote the following: "Section 716 would force derivatives activities out of banks and potentially into less regulated entities . . . The movement of derivatives to entities outside the reach of the Federal supervisory agencies would increase, rather than reduce the risk to the financial system." Similarly, then-Chairman of the Federal Deposit Insurance Corporation ("FDIC") Sheila Bair, in an April 30, 2010, letter to then-Senators Dodd and Lincoln, took issue with the entire concept of pushing derivatives activities out of the bank and warned that "one unin-

[2] Although there is some ambiguity regarding whether Sec. 716 is effective 2 years after the date of enactment of Dodd-Frank (which would be July 2012) or 2 years after the effective date of Title VII (which would be July 2013), we believe the better reading of the statutory language is that Sec. 716 is effective 2 years after the effective date of Title VII. That July 16, 2013 is the effective date is supported by the legislative history of the provision in which Senator Lincoln stated that the effective date of the provision is 2 years from the effective date of the *title*. (*Cong. Rec.,* July 15, 2010, S5922)

[3] As noted above, banks would not be prohibited from engaging in swap dealing activity with respect to swaps with bank-permissible commodity reference assets, such as precious metals, or with respect to hedging and risk-mitigating activities.

tended outcome of this provision would be weakened, not strengthened, protection of the insured bank and the Deposit Insurance Fund."

Promotes Efficient Risk Management

As a general matter, customers prefer to engage in derivatives transactions with banks, rather than their non-bank affiliates, because banks are typically more comprehensively regulated and more highly-rated entities with stronger credit than their non-bank counterparts and can therefore offer lending and derivative products at reduced cost and with greater security. In addition, end-users typically establish relationships with one or a limited number of banks and then depend on those banks to service their hedging and other derivatives needs. This approach has the advantages of allowing end-users to work with banks that understand their businesses, needs and objectives, and have previously reviewed and made determinations with respect to the end-user's credit. In addition, end-users are able to execute transactions based on agreements and documentation already in place with their banks, without the need for separate review and negotiation of new documentation. To the extent that end-users would be required to establish relationships with additional banks for one-off transactions, or for transactions in particular product categories, the process will become slower, more costly and less efficient and will impede the end-users' ability to engage in necessary hedging activities.

H.R. 1838 would avoid this result by allowing U.S. banking organizations to provide their customers with a wider range of products and services and maintain the scope of banks' lending opportunities. By permitting a greater range of swaps activity in the bank, H.R. 1838 would also help maintain other benefits that are derived from centralizing the activity in a single entity. In particular, these additional benefits include the ability to set-off in the event of a default where lending and derivatives activities are conducted in the same entity and the cost savings to customers by restoring certain netting opportunities, which can reduce their collateral obligations without increasing risks to the bank or systemic risks. This in turn, as noted above, facilitates more efficient and effective risk management by banks and their counterparties. For example, a commercial agricultural producer might enter into swaps on agricultural commodities with its bank counterparty in order to hedge its price risk to agricultural commodities arising from its production of such commodities. If that activity is subject to push-out, as it would be under Section 716, and the agricultural entity is also entering into interest rate swaps with the bank to hedge its financing risks, it will no longer be able to net the exposures arising in connection with the two types of transactions. The agricultural entity will therefore not be able to net its agricultural swaps against its interest rate swaps, which will increase its margin requirements, thereby making its hedging more costly—and potentially not cost-effective at all—and exposing it to greater risk in the event of a default by the bank. These results would increase systemic risk, reduce hedging opportunities (or make them more costly) and serve no purpose in providing greater protection to the markets or market participants.

Promotes U.S. Bank Competitiveness

Enactment of H.R. 1838 would also be a key step towards lessening the competitive disadvantage that U.S. banks would face under Sec. 716, as compared to their non-U.S. bank counterparts that are not subject to similar requirements—and likely never will be. Indeed, there is a general and growing recognition that the swaps push-out provision is highly unlikely to be adopted in any other jurisdiction in any form, as Federal Reserve Board Governor Tarullo recently acknowledged in testimony before the Senate Banking Committee. Similarly, nearly 2 years ago, Chairman Bernanke warned Congress that "foreign jurisdictions are highly unlikely to push derivatives out of their banks."[4] In light of this practical reality, the broadening of the scope of swap activities that a bank may continue to engage in reflected in H.R. 1838 is even more critical, especially relative to the lending business. In this regard, U.S. banks could be placed at a serious competitive disadvantage in their traditional lending businesses if borrowers migrate their loans to non-U.S. banks in order to realize the benefits of set-off between their loans and their swaps exposure. Set-off and netting are just as important to customers as they are to banks.

Clarifies Treatment of U.S. Banks' Non-U.S. Operations

H.R. 1838 would also appropriately clarify that Sec. 716 does not limit the swaps activities of foreign branches of U.S. banking organizations. We believe this clari-

[4] In fact, some non-U.S. jurisdictions actually *require* that derivatives transactions be conducted in the bank, as opposed to an affiliate, in part because of the supervisory benefits cited by Sheila Bair, among others.

fication to be wholly consistent with the Congressional intent underlying Sec. 716. Indeed, the legislative history of Sec. 716 is focused exclusively on domestic application and demonstrates no intent by Congress to extend the push-out requirement to the overseas branches of U.S. banks. Moreover, this clarification is consistent with longstanding precedent in U.S. banking law allowing U.S. banks to engage in a wider range of activities in their overseas branches than is permissible in their U.S. offices. Most importantly, however, extending the extraterritorial reach of Sec. 716 in this way would create undue and unnecessary competitive disadvantages for U.S. banks operating abroad, by limiting their ability to provide a full range of swaps to their overseas customers, which include overseas affiliates of their U.S. customers.

Clarifies Treatment of Non-U.S. Banks' U.S. Operations

Without the technical correction in H.R. 1838, the swaps push-out provision could also have a very negative impact on non-U.S. banking organizations with U.S. operations. As the result of an acknowledged drafting error in the statute,[5] certain exemptions from Section 716 that permit banks to continue to engage in certain swaps activity may be available only to "insured depository institutions," a term that could be read to exclude the uninsured U.S. branches and agencies of non-U.S. banks. Accordingly, these exemptions may not apply to swaps activities conducted in these U.S. branches and agencies, which would leave all of their swaps activity potentially subject to the push-out requirement. This result would violate longstanding principles of national treatment and international comity and could, eventually, expose U.S. banks operating abroad to reprisals by foreign regulators. This issue is of most critical concern to The Clearing House member banks that are headquartered outside the United States, but it is an issue of concern for all of our members.

* * * * *

As noted above, we believe H.R. 1838, as reported in overwhelmingly bipartisan fashion by the Financial Services Committee, is a balanced and reasonable approach to addressing the unintended consequences of Section 716. It is also an important step towards competitive equity-extending exemptions to the push-out requirement to uninsured U.S. branches of non-U.S. banks and clarifying that the push-out prohibition does not apply to the non-U.S. operations of U.S. banking organizations. This would be reinforced by the clarification of the extraterritorial application of Title VII in H.R. 3283, described below. Moreover, as noted earlier, enactment of this legislation would in no way undermine Title VII's enhanced regulatory scrutiny of derivatives or compromise bank safety and soundness.[6] These modifications to Sec. 716 are critically important, both to the banking industry, end-users, and our overall economy, and we strongly support their enactment.

Extraterritorial Application of Title VII and H.R. 3283

Effect of H.R. 3283

H.R. 3283[7] would provide clarity regarding the scope of Title VII's requirements by:

- Clearly defining who is a U.S. person and subjecting only those transactions that involve U.S. persons to the transaction-level requirements of Title VII. Importantly, agencies or branches of a U.S. person located outside the United States would be non-U.S. persons provided that they are established for valid business reasons and subject to substantive regulation in the local jurisdiction;
- Permit a non-U.S. swap dealer or security-based swap dealer to meet Title VII's capital requirements by complying with comparable home country standards; and

[5] In a colloquy with Senate Banking Committee Chairman Dodd shortly after Senate passage of Dodd-Frank, Senator Blanche Lincoln, who was the principal author of Sec. 716, acknowledged a "significant oversight" in the technical drafting of Sec. 716 but stated unequivocally that Congress intended the exemptions for "insured depository institutions" to be available also to the U.S. branches of non-U.S. banks. (156 *Cong. Rec.,* S5869, 5903–5904 (daily ed. July 15, 2010))

[6] Congressman Barney Frank strongly backed this bipartisan substitute in the Financial Services Committee and had this to say during the full Committee markup last month: "passing this bill . . . will not in any way, shape or form reduce sensible regulation of derivatives. It will not increase any exposure to the financial system from derivatives. [Sec. 716] was an unnecessary and, I think, somewhat unwise amendment. The bill before us . . . will restore this to what I think is the appropriate balance." Congressman Frank also noted that the legislation would in no way alter the application of the basic substantive regulatory requirements of Title VII (*i.e.,* swap dealer registration, capital and margin requirements, and execution and clearing).

[7] This testimony addresses the text of H.R. 3283, as introduced on Oct. 31, 2011.

- Clarify that the transaction-level requirements of Title VII do not apply to inter-affiliate transactions.

Extraterritorial Application

H.R. 3283 provides important clarity regarding the extent to which Title VII may be applied to activities conducted outside the United States—a critical issue for U.S. and non-U.S. banking organizations alike, and one that has raised concerns in the banking industry, on both sides of the aisle in Congress, and among U.S. and non-U.S. regulators. Although Title VII's extraterritorial impact on U.S. and non-U.S. banking organizations would differ, the effects would be felt across all banking organizations and would have a negative impact on the U.S. financial markets.

The statute itself makes clear that the requirements of Title VII do not apply to activity outside the United States unless such activity has a "direct and significant connection with activities in, or effect on, commerce of the United States" or to prevent evasion of U.S. law and regulation. Application of Title VII's requirements to U.S. banking organizations' operations outside of the U.S. would run contrary to this statutory prohibition and would place U.S. banks at a significant competitive disadvantage to their non-U.S. counterparts in the global markets. In addition, broad extraterritorial application of Title VII could very well result in non-U.S. banking organizations pulling this activity, and potentially their banking activities as well, out of the United States.

Absent the statutory clarification provided in this legislation, the CFTC or SEC could apply Title VII broadly to U.S. banks' non-U.S. operations in a manner inconsistent with the statutory limitations set out in Title VII. Specifically, certain statements by the CFTC indicate an intent to apply the Title VII requirements both to non-U.S. subsidiaries of U.S. financial institutions, as well as to non-U.S. branches of U.S. banks that register as swap dealers, even when the activity conducted by such non-U.S. operations occurs entirely outside of the United States. For example, with respect to a U.S. banking organization registered as a swap dealer, this could mean that even transactions entered into by a non-U.S. branch of such U.S. bank with a non-U.S. person may be subject to all the transaction-level requirements of Title VII (including, most significantly, margin requirements) even when the transactions take place entirely outside the United States. Moreover, these non-U.S. transactions could potentially become subject to U.S. execution and clearing requirements, which is impractical and would not advance U.S. policy interests. For non-U.S. banking organizations, Title VII requirements, if applied broadly, may be imposed on their overseas transactions. These results are particularly inappropriate given the fact that activities of non-U.S. branches of U.S. banks are subject to the jurisdiction of, and robust prudential supervision by, U.S. bank regulators.

An extraterritorial application of these requirements would create an unlevel playing field for U.S. banking organizations that compete outside the United States with non-U.S. banks that would not be required to register as swap dealers under Title VII or would not be subject to all of Title VII's requirements. The competitive disadvantage that U.S. banking organizations would likely face would be particularly pronounced through the application of Title VII margin requirements to swaps conducted between two non-U.S. counterparties. An example of the adverse impact the uneven application of margin requirements could have is evident in the prudential regulators' proposed rules regarding margin requirements for uncleared swaps. Those proposed rules provide for an exemption from margin requirements that would otherwise apply to a swap conducted between a non-U.S. swap dealer and a non-U.S. counterparty, subject to certain conditions. However, non-U.S. subsidiaries of U.S. financial institutions may not avail themselves of this exemption. The competitive disadvantages raised by such a limited exemption are obvious: if non-U.S. counterparties are required to post margin on their derivatives transactions with the non-U.S. branches and subsidiaries of U.S. banking organizations, these transactions are likely to migrate to non-U.S. competitors that do not have the same margin requirements.

Extending the scope of Title VII to non-U.S. transactions will also have a negative impact on commercial end-users and will make their hedging activities more costly and less efficient. For example, if the Title VII scope of application were to extend to a non-U.S. branch of a U.S. bank, or a non-U.S. bank operating outside the U.S., and an end-user that is a non-U.S. subsidiary of a U.S. parent wishes to trade with that branch or bank, its transactions would become more costly, due to the associated compliance obligations. That, in turn, potentially makes the end-user's hedging less effective.

Although the scope of extraterritorial application of Title VII remains uncertain, subject to final rulemaking and regulatory interpretation, H.R. 3283 would be helpful in more clearly defining Title VII's scope. Resolution of this issue is critical be-

cause today's swap markets are global, and conflicting or overlapping requirements across jurisdictions harm all market participants. We recognize and appreciate the ongoing efforts among regulators to work towards global harmonization of the OTC derivatives regimes. At this point, however, broad harmonization of requirements across all jurisdictions most active in these markets remains unlikely. Even if such international harmonization could be achieved, U.S. requirements are likely to become effective earlier, which would subject U.S. banking organizations to a substantial competitive disadvantage before comparable requirements emerge (if at all) in other jurisdictions. Once lost, experience suggests that these relationships will never return.

Inter-affiliate Transactions

The treatment of inter-affiliate swaps transactions under Title VII is also of critical importance to all banking organizations. Title VII itself does not differentiate between affiliate and non-affiliate swap transactions and, as a result, it remains unclear whether the full range of requirements would apply to affiliate transactions.

U.S. and non-U.S. banking organizations alike rely on inter-affiliate swaps transactions for internal hedging and risk management purposes. Imposing requirements such as margin on these trades may increase operational and credit risk associated with the transactions with no offsetting benefits to the institutions themselves or U.S. financial stability, and imposing clearing and execution requirements on these transactions would effectively eliminate their utility. These inter-affiliate transactions do not threaten the safety and soundness of the individual institutions nor do they contribute to systemic risk.

These amendments would in no way undermine the overarching goals of Title VII to increase transparency in the derivatives markets, to mitigate against systemic risk in the broader financial system, and to promote overall market integrity.

* * * * *

Conclusion

In summary, The Clearing House and its members strongly endorse swift passage and enactment of these two bipartisan bills, each of which is carefully crafted to address these specific but significant concerns in a manner that does not imperil financial stability, undermine the regulation of derivatives or the safety and soundness of our banks, or jeopardize the international competitiveness of our institutions and markets. Mr. Chairman, The Clearing House and its members stand ready to assist you in this endeavor in any way we can. Again, we appreciate your invitation to testify before you today and would be pleased to answer any questions you may have.

The CHAIRMAN. Thank you, sir.

Mr. Bailey for 5 minutes.

STATEMENT OF KEITH A. BAILEY, MANAGING DIRECTOR, FIXED INCOME, CURRENCIES AND COMMODITIES DIVISION, BARCLAYS CAPITAL, NEW YORK, NY; ON BEHALF OF INSTITUTE OF INTERNATIONAL BANKERS

Mr. BAILEY. Chairman Conaway, Ranking Member Boswell, and Members of the Subcommittee, my name is Keith Bailey. I am a Managing Director in the Fixed Income, Currencies and Commodities Division of Barclays where I have responsibilities for evaluating and implementing the changes to our derivatives businesses globally resulting from the enactment of Dodd-Frank. I am very pleased to be here today to testify on behalf of the Institute of International Bankers, the IIB, in support of H.R. 3283, H.R. 1838, and the "Swap Data Repository and Clearinghouse Indemnification Correction Act of 2012."

The IIB represents internationally headquartered financial institutions from over 35 countries around the world. Its members include international banks that operate branches and agencies, bank and broker dealer subsidiaries in the United States. In the aggregate, our members' U.S. operations have approximately $5

trillion in assets, contribute to the depth and liquidity of U.S. financial markets, and provide 25 percent of all commercial and industrial bank loans made in this country, which includes agricultural lending.

H.R. 3283, the Swaps Jurisdiction Certainty Act, introduced by Representatives Himes and Garrett was approved yesterday by the Financial House Services Committee. This bill provides certainty with respect to the extraterritorial application of the Dodd-Frank Act, allowing for the harmonization of derivative regulations and ensuring there is a level playing field between U.S. and foreign banks with respect to their cross-border swap activities.

The swap markets are global markets that permit investors access to a range of risk-management products and investment opportunities across a range of international financial markets. Many countries are working to supplement their existing regimes to incorporate derivatives clearing and market transparency reforms similar to those of Dodd-Frank pursuant to the commitments made by the G20 leaders in September of 2009. The Dodd-Frank Act recognizes the need for international coordination of swaps regulations, as well as the need to limit the extraterritorial application of Title VII.

The extraterritorial application of Title VII is a very real concern. For example, different regions may take different approaches regarding what products need to be cleared, what exemptions if any there will be for certain market sectors, and how collateral is to be protected by clearinghouses and clearing members.

H.R. 3283 brings much-needed certainty to the question of extraterritorial reach of Title VII. The bill makes certain that internationally headquartered banks, non-U.S. swap and security-based swap transactions will not be subject to U.S. regulatory requirements. The bill also provides certainty for both U.S. banks and the U.S. operations of internationally headquartered banks with respect to their swap and security-based swap transactions with non-U.S. persons.

With respect to internationally headquartered banks that register as swap dealers under Title VII, the bill makes certain that such banks may satisfy the capital requirements of Title VII by relying on their home country capital requirements provided that such home country requirements are comparable to those expressed under Title VII and the bank's home country is a signatory to the Basel Capital Accords. In this way, the bill recognizes the resource constraints of U.S. regulators and that U.S. regulators should leverage rather than duplicate effective foreign supervision while still retaining their ability to apply U.S. regulations where inadequate protections exist.

The bill recently approved by the House Financial Services Committee, H.R. 1838, was amended to modify rather than repeal Section 716. The IIB supported that amendment cosponsored by Representatives Himes and Maloney and the bill's sponsor, Representative Hayworth, as it provided U.S. branches and agencies of foreign banks parity with insured depository institutions. The bill was reported by the Committee on a voice vote. The bill fixes an unintended and acknowledged oversight in the drafting of Section 716

that has resulted in the disparate treatment of uninsured U.S. branches and agencies of foreign banks as compared to IDIs.

The general prohibition under Section 716 relating to Federal assistance applies to both U.S. FDIC-insured banks and uninsured U.S. branches and agencies of foreign banks that are swap entities. The general prohibition is, however, subject to several important exclusions—grandfathering provisions and transition periods—but these apply only to IDIs. As a result, Section 716 IDIs can continue to engage in certain traditional swap dealing activities, including dealing in interest rate swap and foreign currency swaps and to use swaps for hedging and other similar risk-mitigating activities.

Uninsured U.S. branches and agencies are facing a cliff come July 2013 by which time they must have pushed out all of their existing swap positions and ongoing swaps activities. This will be very disruptive to markets and end-users. Many swap dealers have thousands of clients that would be affected. The assignment or novation of these agreements would almost always require counterparty consent. Under that agreement, there is the prospect of litigation. Given that swap dealing is typically conducted as an integral part of a bank's overall lending and other non-swap business, the failure to rectify this situation could have a major impact on the commercial and industrial lending in the United States by international banks.

Uninsured U.S. branches and agencies of foreign banks are subject to the same type of safety and soundness examination and oversight as U.S. banks, and there is no reason to treat them differently than U.S. banks. Indeed, doing so represents a significant departure from the longstanding U.S. policy that U.S. branches and foreign agencies and agencies of foreign banks are subject to the same rules, regulations, and oversight—*i.e.,* national treatment as U.S. banks.

In this connection, we would like to bring to the Committee Members' attention another instance in Dodd-Frank where the term *insured depository institution* is used unintentionally excluding the U.S. branches and agencies of foreign banks. The definition *swap dealer* in Section 721 provides that an IDI shall not be considered 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. As a result, potentially any uninsured U.S. branch or agency of a foreign bank will have to register with the CFTC if it enters into a swap in connection with its lending activities. Requiring these uninsured U.S. branches and agencies to register would have an impact on their willingness to lend in this country and strain the supervisory resources of the CFTC

In closing, I would like to express my support for the "Swap Data Repository and Clearinghouse Indemnification Act of 2012," and I thank you for the opportunity to testify today on behalf of the IIB. We urge the Committee to consider and approve these important bills and I am happy to answer any questions.

[The prepared statement of Mr. Bailey follows:]

PREPARED STATEMENT OF KEITH A. BAILEY, MANAGING DIRECTOR, FIXED INCOME, CURRENCIES AND COMMODITIES DIVISION, BARCLAYS CAPITAL, NEW YORK, NY; ON BEHALF OF INSTITUTE OF INTERNATIONAL BANKERS

Chairman Conaway, Ranking Member Boswell and Members of the Subcommittee:

My name is Keith Bailey. I am a Managing Director in the Fixed Income, Currencies and Commodities Division of Barclays where I have responsibilities for evaluating and implementing the changes to our derivative businesses globally resulting from enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank). I have over twenty-five years of experience in the derivatives market both here in the U.S. and abroad. I am very pleased to be here today to testify on behalf of the Institute of International Bankers (IIB) in support of H.R. 3283, H.R. 1838, and "the Swap Data Repository and Clearinghouse Indemnification Correction Act of 2012." H.R. 1838 addresses a technical correction of critical importance to IIB's membership. The other two pieces of legislation will provide greater certainty with respect to the cross-border regulation of swaps, while preserving the protections put in place by Dodd-Frank and helping to insure that the global swaps market operates optimally for the benefit of both investors and end-users.

The IIB represents internationally headquartered financial institutions from over 35 countries around the world; its members include international banks that operate branches and agencies, as well as bank, securities broker-dealer and futures commission merchant subsidiaries, in the United States. In the aggregate, our members' U.S. operations have approximately $5 trillion in assets and provide 25% of all commercial and industrial bank loans made in this country, which includes agriculture lending, and contribute to the depth and liquidity of U.S. financial markets. Our members also contribute more than $50 billion each year to the economies of major cities across the country in the form of employee compensation, tax payments to local, state and Federal authorities, as well as other operating and capital expenditures.

At the outset, let me say that the IIB and its members support Dodd-Frank's objectives of reducing systemic risk and increasing transparency in the financial markets. Many IIB members' home country jurisdictions are also working to supplement their existing regimes to incorporate derivatives clearing and market transparency reforms to achieve regulatory objectives similar to those in Dodd-Frank and to support the commitments of the G20 leaders to setting high, internationally consistent requirements for OTC derivatives (see below).

The swap markets are liquid, global markets that permit investors access to a range of risk management products and investment opportunities across a wide range of international financial markets. Unlike the futures and securities markets, swap markets are not dominated by regional exchanges. The global nature of the swap markets brings important benefits to U.S. end-users and other market participants by increasing competition and liquidity.

H.R. 3283

H.R. 3283, *the Swaps Jurisdiction Certainty Act,* introduced by Representative Himes and Garrett provides certainty with respect to the extraterritorial application of Title VII and will ensure there is a level playing field between U.S. and foreign banks with respect to their cross-border swap activities.

While Title VII of Dodd-Frank lays the framework for the U.S. regulation of swaps, it also recognizes the need for international coordination of swaps regulations and, in Sections 722(d) and 772(c), the need to limit the extraterritorial application of Title VII. Many other countries have regulated swap dealers, including branches and affiliates of U.S. firms, for years under their existing regimes for regulation of market professionals. G20 leaders agreed to OTC derivatives regulatory objectives in September 2009, which called for: the trading of all standardized OTC derivative contracts on exchanges and their clearance through central counterparties; reporting of OTC derivatives contracts to trade repositories; and the imposition of higher capital requirements on OTC derivatives contracts that are not centrally cleared.

Consistent with that agreement, the European Union ("EU"), for example, is undertaking regulatory reforms with respect to enhanced pre- and post-trade transparency requirements, clearing of OTC swaps, segregation of client collateral, and the use of organized trading venues. Existing and proposed EU legislation also broadly address business conduct by market professionals. Similar measures are being contemplated by the Commodity Futures Trading Commission (CFTC) and the Securities Exchange Commission (SEC).

However, when these regulatory efforts are neither coordinated nor take into account their extraterritorial impact they can lead to conflicting requirements. For example, firms may be subject to an obligation to clear the same OTC swap as a matter of both U.S. and European regulation. We are hopeful that there will be an agreement between the CFTC and the SEC and regulators from other regions and countries, including the EU, Asia and Canada, to address this issue, as it is impossible to clear the same contract through two clearinghouses. Even with such agreement, issues of likely greater divergence may exist, such as when differing regions implement differing approaches to which products need to be cleared; what exemptions, if any, there will be for any sectors of the markets; and, how collateral is to be protected by clearinghouses and clearing members. Finally, there is no guarantee that the rules being drafted in the U.S. and the EU relating to the permitted execution venue for swaps will be sufficiently similar to allow mutual recognition.

These conflicts, which can occur as a result of the extraterritorial application of swaps regulations, can result in a number of other harmful results. It is not disputed that internationally headquartered banks' transactions with U.S. persons from outside the United States may trigger the registration and regulatory requirements prescribed under Title VII. However, if internationally headquartered firms with U.S. operations are subject to U.S. regulation of business conducted with non-U.S. persons, they face the risk of operating at a competitive disadvantage relative to an international firm that lacks a sufficient U.S. nexus to be subject to such rules. As a result, international firms with operations in the U.S., many of which use a single internationally located "central booking location" to book swaps, may choose to establish separate subsidiaries in the U.S. to try to limit these conflicts. However, this would be capital inefficient, introduces risk management concerns, is disadvantageous to large clients (who themselves prefer to transact globally), and potentially leads to inconsistent prudential regulation. This "silo" or "fragmented" approach may also result in U.S. end-users having difficulty accessing overseas markets directly.

The extraterritorial application of Title VII is a very real concern. The industry has been engaged in ongoing dialogue with the CFTC, SEC and other regulators, and has sought guidance on the territorial scope of Dodd-Frank from the inception of the rulemaking process. Nevertheless, nearly every question on this topic and related issues, such as the treatment of inter-affiliate transactions, guarantees and branches, remains open.

Against this backdrop, it is challenging that the CFTC finalized rules on January 11, 2012 requiring companies to register provisionally as swap dealers or major swap participants as soon as the definitional rules under Dodd-Frank go into effect. All indications are, however, that the CFTC will not have finalized its extraterritorial guidance by that time, and possibly without a sufficient transition period for companies to come into compliance. Other significant CFTC rules have yet to be finalized as well, making the business decision on how best to comply with the CFTC's provisional registration rules difficult.

H.R 3283 brings much-needed certainty to the question of the extraterritorial reach of Title VII. The bill makes certain that internationally headquartered banks' non-U.S. swap and security-based swap transactions will not be subject to U.S. regulatory requirements. The bill also provides certainty for both U.S. banks and the U.S. operations of internationally headquartered banks with respect to their swap and security-based swap transactions with non-U.S. persons.

With respect to internationally headquartered banks that register as swap entities under Title VII based on their transactions with U.S. persons, the bill makes certain that such banks may satisfy the capital requirements of Title VII by relying on their home country capital requirements, provided that such home country requirements are comparable to the requirements under Title VII and the bank's home country is a signatory to the Basel Capital Accords. This approach conforms to the approach that has been taken for many years by the banking regulators in assessing the capital of foreign banks for U.S. regulatory purposes. It also ensures that appropriate protections are in place with respect to transactions that involve U.S. persons.

H.R. 1838

This bill, as introduced and referred to the Committee, would repeal Section 716 of Dodd-Frank, also known as the swaps "push-out" provision. Our principal concern with Section 716 is the unintended and acknowledged oversight in according significantly different and negative treatment for uninsured U.S. branches and agencies of foreign banks compared to that provided to insured depository institutions. Many foreign banks operate uninsured branches and agencies in the U.S. In the aggregate, these branches and agencies have more than $2 trillion in assets. In addition

to lending and engaging in certain securities, asset management and other similar activities, many such branches and agencies also engage in swap dealing. Dodd-Frank provides that branches and agencies engaged in swap dealing activity be required to register with the CFTC and/or the SEC with respect to their swap dealing activity. Accordingly, they will be "swap entities" under Section 716.

Section 716 generally provides that no "Federal assistance" may be provided to any swaps entity with respect to any swap, security-based swap or other activity of the swap entity. "Federal assistance" is defined to include advances from the discount window and FDIC insurance. Uninsured U.S. branches and agencies of foreign banks are licensed by a Federal or state banking authority; they are subject to the same type of safety and soundness examination and oversight as U.S. banks, and, like U.S. banks, they are eligible to borrow from the Federal Reserve discount window so long as the advance is secured by high quality collateral and subject to discount.[1] From the Federal Reserve's perspective, maintaining U.S. branches' and agencies' access to the discount window is an important tool for maintaining a sound and orderly financial system.

The general prohibition under Section 716 relating to Federal assistance applies to both U.S. FDIC-insured banks and uninsured U.S. branches and agencies of foreign banks that are swap entities. The general prohibition is, however, subject to several important exclusions, grandfathering provisions and transition periods, but these provisions apply only to "insured depository institutions" (IDIs). As a result, uninsured U.S. branches and agencies would appear not to be eligible for the exclusions, grandfathering and transition provisions applicable to IDIs.

When Section 716 was enacted, Members of Congress acknowledged that this differential treatment of uninsured U.S. branches and agencies of foreign banks was "clearly unintended" and recognized the need "to ensure that uninsured U.S. branches and agencies of foreign banks are treated the same as insured depository institutions," consistent with the U.S. policy of national treatment.[2] However, as was explained at the time, in the rush to complete the conference and finalize Section 716 there was no opportunity to rectify this "significant oversight."[3]

As a result, the exclusion in Section 716(d) that permits IDIs to continue to engage in certain traditional swap dealing activities, including dealing in interest rate and foreign currency swaps, and to use swaps for hedging and other similar risk-mitigating activities, would appear not to be available to uninsured U.S. branches and agencies of foreign banks. If uninsured branches and agencies that are swap entities were ineligible for this exclusion, then their U.S. customers would lose the benefit of trading with them. These customers would have to establish new trading relationships away from the U.S. branch or agency in order to engage in traditional swap transactions, as well as those swap activities that are not covered by the Section 716's exceptions. This would significantly reduce competition and worsen pricing in the U.S. swaps market, especially given that 8 of the 14 largest global derivatives dealers are foreign banks.

In addition, the resulting differential treatment relative to U.S. FDIC-insured banks would overtly discriminate against and competitively disadvantage foreign banks. This represents a significant departure from the long-standing U.S. policy that U.S. branches and agencies of foreign banks are subject to the same rules, regulations and oversight, *i.e.,* national treatment, as U.S. banks. Finally, it would provide precedent for foreign jurisdictions to provide advantages to their local banks at the expense of the foreign operations of U.S. banks, if not in the context of swaps then potentially in other contexts.

Section 716(b)(2)(B) also excludes from the scope of Section 716 an IDI that is a major swap participant or major security-based swap participant. This exclusion is important to those IIB members that may be deemed to be major swap or security-based swap participants. The definition of major swap participant encompasses not only persons engaged in ongoing swap activities but also potentially persons with only legacy positions. Thus, if uninsured branches and agencies were not treated as IDIs for this purpose, then they could be subject to Section 716 as a result of legacy positions in a way that a U.S. FDIC-insured bank would not.

Finally, Section 716(e) provides that Section 716's prohibition on Federal assistance "shall only apply to swaps or security-based swaps entered into by an insured depository institution after the end of [Section 716's] transition period." Therefore, the existing swaps of IDIs are grandfathered from Section 716. Relatedly, Section

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[1] *See* Federal Reserve Regulation A, 12 CFR § 201.1 (extending rules relating to eligibility for Federal Reserve Bank lending to "United States branches and agencies of foreign banks").

[2] 156 *Cong. Rec.* S5903–S5904 (daily ed. July 15, 2010) (colloquy between Senator Dodd and Senator Lincoln).

[3] *Id.*

716(f) gives an IDI's appropriate Federal banking agency the authority to grant the institution a transition period of up to 3 additional years beyond Section 716's July 16, 2013 effective date before the institution must divest or cease its swap activities. The purpose of this transition period is to prevent the restructurings necessary to comply with Section 716 from adversely disrupting the institution's lending and other non-swaps activities. But this provision is available only to IDIs.

The implications of these issues are potentially serious. There are approximately 16 months before uninsured U.S. branches and agencies that are swap entities must "push out" all their existing swap positions and ongoing swaps activities, which is precious little time, particularly relative to the longer period—up to more than 4 years—before IDIs will have to make their transition. Moreover, the absence of any grandfathering of existing positions would mean that the transition for foreign banks and their counterparties would be much more disruptive, more similar to insolvency in many respects than to an orderly business restructuring. This is true because:

- Swap dealing is typically conducted as an integrated part of a bank's lending and other non-swap businesses. Swap positions often hedge loan and other non-swap positions, and risk management and other systems are often shared across many different types of trading activities, not just those involving swaps. Winding down or restructuring swap dealing activities will as a result tend to decrease lending and market-making activity, with material adverse effects on the U.S. economy.
- A significant number of customers have master agreements directly with the uninsured U.S. branches and agencies of foreign banks, or have multi-branch netting agreements to which one or more uninsured U.S. branches or agencies are parties. The assignment or novation of these agreements, even to an affiliate, almost always requires counterparty consent, forcing customers and foreign banks to negotiate the terms for assigning, novating or modifying agreements for swap portfolios held with uninsured U.S. branches and agencies. Major swap dealers have thousands of clients who would be affected.
- International banks and their customers may not always agree to the terms of an assignment or novation, thereby forcing the parties to litigate over whether Section 716 triggers "illegality" and similar provisions in those agreements.
- Renegotiation and litigation will lead to delays in trading; resulting in diminished liquidity and higher spreads for customers.
- Assignment or novation could also potentially trigger other requirements under Dodd-Frank, such as mandatory clearing and trading requirements inasmuch as any such novated or assigned swap potentially would constitute a new swap that would be subject to those requirements.
- There are significant capital and technology costs associated with using a new booking structure, and the modification of existing systems to track new booking structures will put a very heavy strain on information technology resources that are already overwhelmed with the other changes necessary because of Dodd-Frank.

While the underlying bill deals with this disparate treatment of uninsured branches and agencies of foreign banks by striking Section 716 in its entirety, the bill recently approved by the House Financial Services Committee modifies Section 716. The IIB supported this amendment, which was cosponsored by Representatives Himes and Maloney and the bill's sponsor Representative Hayworth, as it provided U.S. branches and agencies parity with insured depository institutions.

Swap Dealer Definition

In this connection, we would like to thank Chairman Lucas for his attention to another instance in Dodd-Frank where uninsured U.S. branches and agencies of foreign banks are similarly harmed compared to insured depository institutions. Section 721 defines "Swap Dealer" (Section 1a(49) of the Commodity Exchange Act (CEA)) to exclude "insured depository institutions" which "enter into a swap with a customer in connection with originating a loan with that customer." Because the exclusion is limited to IDIs, **any** uninsured U.S. branch or agency of a foreign bank potentially will have to register with the CFTC if it enters into a swap in connection with its lending activities. Requiring these uninsured U.S. branches and agencies to register could have an impact on their willingness to lend in this country and strain the supervisory resources of the CFTC. We would urge Members to support a fix to this definition that would provide uninsured U.S. branches and agencies of foreign banks the same treatment accorded IDIs under Section 1a(49) of the CEA.

Swap Data Repository and Clearinghouse Indemnification Correction Act of 2012

Under Dodd-Frank, OTC derivatives transactions are required to be reported to swap data repositories and securities-based swap data repositories. Dodd-Frank contemplates that information reported to the CFTC by derivatives clearinghouses and information reported to data repositories can be accessed by U.S. and foreign regulators. However, access to such information is conditioned on the recipient agreeing to keep such information confidential and to indemnify the CFTC or data repository, as the case may be, for "any expense arising from litigation relating to the information provided." This indemnification requirement is a significant barrier to foreign regulators and, in some instances, to U.S. regulators to obtaining this data. *The Swap Data Repository and Clearinghouse Indemnification Correction Act of 2012* would eliminate this barrier. The IIB supports the bill and urges its approval by the Committee.

Conclusion

Thank you for the opportunity to testify today on behalf of the IIB. We urge the Committee to consider and approve these important bills.

The CHAIRMAN. Thank you, Mr. Bailey.

Mr. Bodson?

STATEMENT OF MICHAEL C. BODSON, CHIEF OPERATING OFFICER, DEPOSITORY TRUST & CLEARING CORPORATION, NEW YORK, NY

Mr. BODSON. Thank you. Chairman Conaway, Ranking Member Boswell, and Members of the Subcommittee, my name is Michael Bodson and I am COO of the Depository Trust & Clearing Corporation. DTCC is creating global trade data repository system for all swap asset classes, including interest rates, credit default swaps, foreign exchange, and commodities. We applaud the leadership of this Subcommittee and the sponsors of the bills—Representatives Sewell and Crawford—for holding today's hearing on bipartisan legislation to ensure effective swap transaction reporting for monitoring systemic risk in global financial markets.

DTCC has been working diligently with regulators in the United States and globally to address these issues, but it is clear that a legislative fix is needed. Today, I will address two technical provisions in the Dodd-Frank Act that make it more difficult for regulators around the world to share information. They are referred to as indemnification and plenary access and both may result in data fragmentation.

The first issue, indemnification, is an immediate problem. Many regulators worldwide are unable or unwilling to provide an indemnity agreement. The concept of indemnification is unfamiliar to them and inconsistent with their traditions and legal structures. More plainly, though, foreign government agencies will not indemnify private, third-party entities such as SDRs. The indemnification provision is also not needed in light of the current international data sharing guidelines developed through the cooperative efforts of more than 40 regulators worldwide, including the CFTC, SEC, and Federal Reserve.

Without an indemnity agreement, U.S.-based repositories would be legally prohibited from providing regulators outside the United States with market data on OTC derivative transactions under their jurisdictions. The clear risk is that global supervisors will have no viable option other than to fragment data globally by creating local repositories to avoid indemnification.

DTCC strongly supports H.R. 4235, which would remove the indemnification provisions from Dodd-Frank and make U.S. law consistent with existing international protocols. This legislation will go a long way to ensuring global regulators can effectively monitor systemic risk. However, resolving indemnification without addressing the second issue, plenary access over the data held within an SDR, still makes it likely that swap data will be fragmented by jurisdiction. Addressing both issues concurrently can preempt the future crisis for information sharing.

Dodd-Frank gives U.S. regulators direct electronic access to data held by the SDR. This provision was intended to insure immediate access to swap data in machine-readable format. However, non-U.S. regulators are concerned that direct electronic access may be interpreted too broadly by the U.S. agencies to gain plenary access to all swap data they hold, including data for transactions with no identifiable nexus to U.S. regulation. This is unworkable because the scope of an SDR can be broader than just U.S. data and regulators should have access to only that data to which they have a material interest. Concerns over plenary access will again lead to data fragmentation.

DTCC fully supports regulators having plenary access for SDR supervision activities related to the operation of the SDR and transactions held within it with a U.S. nexus. However, we oppose plenary access for other purposes because non-U.S. financial firms executing transactions without a U.S. nexus will avoid reporting their trade data to a global repository if that data could become subject to U.S. regulatory access.

As an example, global data may be held in the United States for purposes of aggregation for public transparency and system risk oversight. However, if this leads to U.S. regulators claiming access to non-U.S. transactions, foreign participants and regulators will raise concerns over confidentiality and prevent the data from being aggregated. If data fragmentation occurs, regulators, including the SEC, CFTC, and Office of Financial Research will face the daunting and time-consuming challenge of having to aggregate data from multiple repositories for purposes of market oversight and systemic risk mitigation.

Additionally, in meetings with regulators worldwide over the past year, these supervisors have said they will not permit the use of a U.S.-based trade repository for its domestic transactions if there are asymmetric access rights and no protection of confidentiality for the market participants.

To illustrate the combined impact of these provisions, let's examine the case of two British banks executing an interest rate swap in the UK involving the Euro. There is no direct U.S. connection. Under plenary access, if the trade was reported to a European-based global repository but the transaction was sent to the United States for aggregation, U.S. regulators could claim a legal right to view data on this transaction even though the U.S. regulator has no material interest in it. Even worse, the indemnification provision could require the British regulator to indemnify the U.S.-registered SDR to access the same data despite the fact that the entirety of the trade falls within the British regulators' jurisdiction.

Mr. Chairman, the issues of indemnification and plenary access must be dealt with together to prevent data fragmentation from occurring. Congress needs to address plenary access by clarifying the intent of the statute and reinforcing that regulators only have access to the data in which the regulator has a material interest. By amending and passing the H.R. 4235 to ensure technical corrections to both indemnification and plenary access, Congress will create the proper environment for the development of a global trade repository system to support systemic risk management and oversight.

Thank you for your time this morning.

[The prepared statement of Mr. Bodson follows:]

PREPARED STATEMENT OF MICHAEL C. BODSON, CHIEF OPERATING OFFICER, DEPOSITORY TRUST & CLEARING CORPORATION, NEW YORK, NY

Chairman Conaway and Ranking Member Boswell:

Thank you for scheduling today's hearing on Representatives Rick Crawford (R–AR) and Terry Sewell's (D–AL) bipartisan legislation, introduced with Representatives Robert Dold (R–IL) and Gwen Moore (D–MI), to address the indemnification provisions and modify the confidentiality requirements in the Dodd-Frank Wall Street Reform and Consumer Protection Act (DFA). I appreciate the opportunity to testify and bring greater attention to the unintended consequences of these provisions, which have the potential to fragment the current global data set for over-the-counter (OTC) derivatives and derail efforts to increase transparency and help regulators mitigate risk in this marketplace.

Over the past year, DTCC, among others, has been raising concerns over the impact of the DFA's broad extraterritorial reach, particularly as it relates to the confidentiality of market data and the indemnification agreement provisions of the law. These concerns have been echoed by regulatory officials and policymakers globally, including by Representatives of the European Parliament, European Commission and Council, by Asian governments and by both Republican and Democratic Members of the U.S. Congress.

The House Agriculture Committee's leadership is vital as there is a clear need to shine a light on these technical provisions of the DFA—provisions that, if not addressed, risk decreasing the current level of transparency into OTC derivatives markets. Having a bipartisan group of Members in both the House and Senate recognize the unintended consequences of these provisions and commit to working within Congress and with policymakers internationally to develop a mutually agreeable resolution is very promising.

Two Important DFA Extraterritorial Provisions Require Congressional Action

The two key extraterritorial provisions in the DFA that risk fragmenting global swap data are the confidentiality and indemnification provisions and the so-called "plenary access" duties imposed on swap data repositories (SDRs). These issues merit further examination by Congress and require legislative resolution.

First, Sections 728 and 763 of the DFA require SDRs registered with the Commodity Futures Trading Commission (CFTC) or Securities and Exchange Commission (SEC) to receive a written agreement from "third-party" non-U.S. regulators confirming that the supervisory agency requesting the information will abide by certain confidentiality requirements and indemnify the SDR and the regulating U.S. Commission(s) for any expenses arising from litigation relating to the information.

Second, the duties imposed on a registered SDR—both with the CFTC and the SEC—require, among other things, that the SDR provide "direct electronic access to the Commission (or any designee of the Commission, including another registered entity)." The phrase "direct electronic access" has been identified by non-U.S. regulators as problematic because it creates an unnecessary degree of ambiguity and may be interpreted by the regulatory agencies and others as a requirement that a registered SDR must provide access to all swap data retained by the SDR—even when that SDR might maintain swap data for transactions with no identifiable nexus to U.S. regulation.

The concern that a U.S. regulator might demand data that falls wholly outside its jurisdiction as part of its "direct electronic access," coupled with the lack of clear

extraterritorial guidance from the CFTC and the SEC, would functionally prevent non-U.S. SDRs from registering in the United States. If this occurs, swap data would fragment across jurisdictions and frustrate regulators' abilities to monitor global systemic risk.

Plenary Access & Indemnification in Dodd-Frank: Solving a Problem That Does *Not* Exist

The original indemnification and plenary access provisions, while well-intended, are unworkable as currently drafted and threaten to undo the existing system for data sharing that was developed through the cooperative efforts of more than 50 regulators worldwide under the auspices of the OTC Derivatives Regulators' Forum (ODRF) and, more recently, taken up by the Committee on Payment and Settlement Systems and the International Organization of Securities Commissions (CPSS IOSCO).

For nearly 2 years, regulators globally have followed the ODRF guidelines to access the information they need for systemic risk oversight. It is the standard that DTCC uses to provide regulators around the world with access to global credit default swap (CDS) data in its Trade Information Warehouse (TIW), which holds more than 98% of all CDS trades globally. It is accurate to say that the plenary access and indemnification provisions attempt to solve a problem that does *not* exist—and, in doing so, create several new problems that heretofore did not exist.

Asian and European regulators have identified indemnification and plenary access as among the most troubling extraterritorial provisions of the DFA because of their potential to fragment the current global data set for OTC derivatives. They recognize, as do many Members of the House and Senate here in the United States, that these provisions would reduce the level of transparency that currently exists in these markets.

In an effort to avoid unintended consequences, European policymakers specifically considered and rejected an identical indemnification requirement in the European Market Infrastructure Regulation (EMIR). This was a positive development because, as the SEC noted in testimony before the House Financial Services Committee last week, the agency "would be legally unable to meet any such indemnification requirement and has argued vigorously against similar requirements in other contexts." The CFTC would have a similar challenge.

In addition, the early EMIR texts in Europe, which called for "direct access," were amended to call for "immediate access." In Asia, the Monetary Authority of Singapore (MAS) has indicated in its public consultation that it will align its regulations with the Europeans in this area, and we expect the Japanese FSA, whose draft regulations are due shortly, to be similarly aligned. However, policymakers in Hong Kong have responded by beginning to move forward with the development of a national repository for its swap data.

Indemnification Would Fragment the Global Data Set and Impede Regulatory Oversight

It is highly unlikely third-party regulators will comply with the DFA requirement that they must provide indemnification in order for U.S.-registered SDRs to share critical market data with them for two primary reasons.

First, the concept of indemnification is based on U.S. tort law and, therefore, inconsistent with many of the traditions and legal structures in other parts of the world. Many regulators worldwide have indicated that they would be unable or unwilling to provide an indemnity agreement to a private third party as required under the DFA. Second, these same regulators have noted that they are already following policies and procedures to safeguard and share data based on both the ODRF and IOSCO's Multi-Lateral Memorandum of Understanding.

Without an indemnity agreement, U.S.-based repositories may be legally precluded from providing regulators outside the U.S. with market data on transactions that are under their jurisdiction. The clear risk is that global supervisors will have no viable option other than to create local repositories to avoid indemnification—a move that is the definition of data fragmentation. While each jurisdiction would have an SDR for its local information, it would be extremely difficult and time consuming to effectively share information between regulators.

A proliferation of local repositories would undermine the ability of regulators to obtain a comprehensive and unfragmented view of the global marketplace. If a regulator can only "see" data from the SDR in its jurisdiction, then that regulator cannot get a fully aggregated and netted position of the entire market as a whole. And if a regulator cannot see the whole market, then the regulator cannot see risk building up in the system or provide adequate market surveillance and oversight. In short,

regulators will be blind to market conditions as a direct result of the indemnification provision. In the name of transparency, this provision creates opacity.

The CFTC and the SEC have carefully reviewed the impact of the indemnification provision and in a joint report concluded, "Congress may determine that a legislative amendment to the indemnification provision is appropriate."

Furthermore, the SEC testified in support of removing the indemnification provision from the DFA during a hearing of the House Financial Services Capital Markets Subcommittee last week. The agency said the "indemnification requirement interferes with access to essential information, including information about the cross-border OTC derivatives markets. In removing the indemnification requirement, Congress would assist the SEC, as well as other U.S. regulators, in securing the access it needs to data held in global trade repositories. Removing the indemnification requirement would address a significant issue of contention with our foreign counterparts, while leaving intact confidentiality protections for the information provided."

Plenary Access: Congress Needs to Clarify Intent of Statute and Rules

Direct oversight is necessary to ensure thorough examination of the SDR's operations, guaranteeing the completeness and accuracy of the data published by the SDR. This type of access, which could more easily be achieved by imposing a statutory books and records obligation related to the operation of the SDR, is distinct from that required by non-supervisory regulators who rely upon the SDR's data for systemic risk oversight. The level of access to an SDR's data should reflect the purpose for which a regulator seeks to review the SDR's information and remain within the regulator's authority.

The DFA rules proposed and adopted by the CFTC and SEC are helpful, but they do not adequately address this problem. The concern remains that it can be interpreted too broadly, giving U.S. regulators access to data in which a U.S. nexus does not exist.

While DTCC fully supports regulators having plenary access for SDR supervision activities, we oppose plenary access for other purposes because, as a result of this provision, non-U.S. financial firms executing transactions without a U.S. nexus will avoid reporting their trade data to a U.S.-registered SDR. Much like indemnification, plenary access would fragment swap transaction data across countless repositories that reside around the world, frustrating systemic risk oversight efforts.

In the course of dozens of meetings with global regulators, including discussions we held last week in several Asian countries and at the ODRF, non-U.S. supervisors have consistently indicated that they will not permit the use of a U.S.-based trade repository for its domestic transactions if there are asymmetric access rights and no protection of the confidentiality for their market participants, particularly their private individual and sovereign data.

If data fragmentation occurs, U.S. regulators like the SEC would face the daunting, expensive and time-consuming challenge of having to aggregate data with a U.S. nexus for purposes of market oversight and surveillance and systemic risk mitigation. This creates several significant burdens for the agency, including (1) the need to develop and enter into information-sharing agreements because current Memoranda of Understanding (MOU) limit transfer of data for only certain situations, such as market abuse investigations, and (2) the need to harmonize their rules with the European standard of equivalent recognition contained in EMIR.

Data fragmentation would also impose a significant financial burden on the SEC, CFTC as well as the Office of Financial Research (OFR), which would be responsible for aggregating and standardizing data and resolving issues of data omission and duplication. Furthermore, the resulting fragmentation of data would negatively impact systemic risk analysis—if not make it completely impossible.

DTCC has analyzed potential methods to resolve this complicated issue and remains ready and willing to assist legislators in fashioning a remedy to ensure regulators can access the information they need. Congress should seriously consider finding an appropriate legislative solution that clarifies that U.S. regulators may access the swap data of its registrant SDRs only to the extent necessary to perform its oversight and surveillance responsibilities or to regulate the operation of the SDR.

Within the context of considering legislation that would repeal the indemnification provisions, addressing the concerns over plenary access would complement these efforts and help create a framework for global swaps data that is accessible to regulators in the United States and around the world. The goal of any amendment to the bill should be to appropriately position the DFA and U.S. regulators on plenary access. The SEC, CFTC, foreign regulatory agencies, governmental staff and lawmakers should be more comfortable that the intent of the ultimate regulatory inter-

pretations of statute is designed to respect privacy and confidentiality, where there is no risk to the U.S. financial system.

Indemnification and Plenary Access: A Case Study

To illustrate the combined impact of indemnification and plenary access and underscore why it has emerged as a major source of concern for regulators worldwide, let's examine the case of two British banks executing an interest rate swap in the UK involving a Sterling reference rate. Under the plenary access provision, if the trade was reported to a UK-based but U.S.-registered SDR, U.S. regulators could claim, as the regulator of the SDR, a legal right to view data on this transaction—even though the U.S. SDR regulator has no material interest in the counterparties, the transaction, or the underlying entity (as opposed to a Prudential Regulator seeking data for market oversight purposes). To compound the situation, the indemnification provision would require the British regulator to indemnify the U.S.-registered SDR in order to access this same data—despite the fact that the entirety of the trade falls within the British regulator's jurisdiction.

Just as a U.S. regulator would not be inclined to have sensitive data on U.S. trades available to non-U.S. supervisors—or, for that matter, have to provide indemnity to access data that is rightly theirs to view—regulators globally consider this extraterritorial reach inappropriate and inconsistent with widely established and agreed upon data sharing practices.

In contrast, under both the current ODRF guidelines that have served regulators and the markets well, supervisors are authorized to access data where there is a nexus to the jurisdiction or entity. Therefore, U.S. regulators can view data where there is a U.S. nexus and, equally, British regulators can view data with a UK nexus. And in no case is an indemnification agreement needed before access to data is provided.

"Swap Data Information Sharing Act of 2012": A Potential Legislative Solution

The *Swap Data Information Sharing Act of 2012* (H.R. 4235), introduced by Representatives Dold, Moore, Crawford and Sewell, would make U.S. law consistent with existing international protocols by removing the indemnification provisions from sections 728 and 763 of the DFA. DTCC strongly supports this legislation, which represents the only viable solution to the unintended consequences of indemnification.

The *Swap Data Information Sharing Act of 2012* is necessary because the statutory language in the DFA leaves little room for regulators to act without U.S. Congressional intervention. This point was reinforced in the recent CFTC/SEC *Joint Report on International Swap Regulation.* The Report noted that the Commissions "are working to develop solutions that provide access to foreign regulators in a manner consistent with the DFA and to ensure access to foreign-based information." It goes on to say, as noted earlier, "Congress may determine that a legislative amendment to the indemnification provision is appropriate."

This bill would send a strong message to the international community that the United States is strongly committed to global data sharing and determined to avoid fragmenting the current global data set for OTC derivatives.

However, resolving indemnification without addressing plenary access leaves open the likelihood that global swap data will be fragmented by jurisdiction. The two pieces must be dealt with together. Resolving one without the other does not diminish the likelihood of data fragmentation occurring. While this legislation is a strong step in the right direction, it is one of two key technical corrections that is required to ensure regulators continue to have the highest degree of transparency into OTC derivatives markets.

Congress needs to address the issue of plenary access by simply and clearly clarifying the intent of the statue and reinforcing that regulators have access to the data in which the regulator has a material interest. We are pleased that several Members of the House Capital Markets Subcommittee voiced their concerns with plenary access during last week's hearing on H.R. 4235 and indicated their interest in crafting a legislative solution to address this problem. We stand ready to work with them and their colleagues on a technical correction to clarify the intent of the law.

Toward that end, under the attached suggested amendment, which would add the so-called "books and records" provision to the law, regulators in the U.S. would continue to have full and complete access to any and all data to which there is a U.S. nexus and according to their regulatory domain. This would align U.S. policy with the current global data sharing standards that have been in place since 2010 and which have provided regulators with all of the information needed to oversee market participants and activity in their jurisdiction.

By amending and passing this legislation to ensure that technical corrections to both indemnification and plenary access are addressed, Congress will help create the proper environment for the development of a global trade repository system to support systemic risk management and oversight.

Bipartisan, Bicameral Congressional Support for Resolving Indemnification

As the unintended consequences of the indemnification provisions have been brought to light, there is bicameral, bipartisan support to resolve this issue. For example, Senator Agriculture Committee Chairwoman Debbie Stabenow (D–MI) and Ranking Member Pat Roberts (R–KS), and House Appropriations Agriculture Subcommittee Congressman Jack Kingston (R–GA) and Ranking Member Sam Farr (D–CA), authored separate letters last year to their counterparts in the European Parliament expressing interest in working together on a solution to the issue.

In addition, several other Members of Congress have also publicly declared their support for a technical correction to the provision. As CFTC Chairman Gary Gensler indicated in testimony to this Committee in June 2011, both he and SEC Chairman Schapiro have written to European Commissioner Michel Barnier regarding the indemnification provisions of the DFA and are currently engaged in efforts to find a solution to the challenges of this section.

DTCC Has Deep Experience Operating Global Trade Repositories

DTCC currently operates two subsidiaries specifically responsible for providing repository services to the global derivatives community: the TIW operated by The Warehouse Trust Company LLC for credit derivatives, a U.S. regulated entity; and DTCC Derivatives Repository Limited (DDRL) for equity derivatives, a UK regulated entity.

In response to the G20 commitments made at the September 2009 Pittsburgh Summit, the Financial Stability Board (FSB) Report on OTC Derivatives Market Reform, and forthcoming statutory legislation in various jurisdictions, the international financial community recently selected DTCC's DDRL entity to provide global repository services for interest rates and FX swaps. DTCC also was selected to operate the commodities repository (together with the European Federation of Energy Traders) under its newly established Netherlands entity, Global Trade Repository for Commodities B.V.

DTCC is working closely with global partners and asset class experts to design repositories to meet the regulatory reporting requirements identified in the respective regional or national jurisdictions. DTCC has completed its first phase of creating and operating the new Global Trade Repository for Interest Rates (GTR for Rates) and Commodities (GTR for Commodities). The GTR for Rates recently began regulatory test reporting. DTCC is currently in discussions with industry and regulatory authorities, developing consensus on the right framework for the GTR for Commodities' reporting.

DTCC has extensive experience operating as a trade repository and meeting transparency needs. In November 2008, in response to mounting concerns and speculation regarding the size of the CDS market following the collapse of Lehman Brothers, DTCC began public aggregate reporting of the CDS open position inventory. Today, this reporting includes open positions and volume turnover, providing aggregate information that is extremely beneficial to both the public and regulators in understanding the size of the market and activity.

Further, following the ODRF data access guidelines for the TIW, DTCC launched a regulatory portal in February 2011, which provides automated counterparty exposure reports and query capability for market and prudential supervisors and transaction data for central banks with aggregate report views by currency and concentration. Nearly 40 regulators world-wide have signed up to the portal. DTCC plans to expand on this portal as it launches its global trade repository services for the other asset classes.

Thank you for your time and attention this morning. I am happy to answer any questions that you may have.

The CHAIRMAN. Well, thank you so much, I appreciate those opening remarks. The chair will remind Members they will be recognized for questioning in order of seniority for Members who were here at the start of the hearing. After that, Members will be recognized in order of arrival and I appreciate the Members' understanding.

All right. I will reserve my time for the end and will recognize Mrs. Ellmers—you were here next—for 5 minutes.

Mrs. ELLMERS. I would like to ask a question of Mr. Bodson since we were talking about the plenary access in your testimony, and basically, you argue that this legislation, there is a need to change the plenary access provisions in addition to indemnification, why aren't the actions of the agency sufficient? Can you restate again for us why you feel it is not sufficient?

Mr. BODSON. Well, I think there is legal uncertainty with global regulators over the issue of plenary access. It is in the legislation. People respect the law. And while we are working with both the CFTC and SEC to clarify their approach, the level of certainty that is encompassed in having legislation fix the issue and clarify exactly what plenary access means would provide a great level of comfort and avoid the data fragmentation. So it really is a legislative issue.

Mrs. ELLMERS. Yes.

Mr. BODSON. Legislation should fix it.

Mrs. ELLMERS. Okay. For Mr. Bailey and Mr. Saltzman, as you know, the CFTC recently finalized a swap dealer registration rule. In the absence of guidance on the territorial scope of Dodd-Frank, how are you preparing to comply with the rule once it is in effect? And I will start with Mr. Saltzman and then Mr. Bailey.

Mr. SALTZMAN. I think our member banks are engaged in a duplicative exercise of planning for every possible contingency. Obviously, our members are committed to complying with the law, but unfortunately, the regulatory agencies have not yet issued any pronouncement, and it is very, very difficult. There are corporate structural issues, there are documentation issues——

Mrs. ELLMERS. Yes.

Mr. SALTZMAN.—capital issues, funding issues, and unfortunately, banks and swap dealers are having to plan for a multiplicity of contingencies, which obviously adds a layer of inefficiency and cost. But there is tremendous legal uncertainty right now, which is why we urge the Committee to swiftly pass H.R. 3283.

Mr. BAILEY. I agree with the comments of Mr. Saltzman. This issue is presenting some very real difficulties for a number of international banks who do not know which entities they need to register——

Mrs. ELLMERS. Yes.

Mr. BAILEY.—the extent of that registration requirement, and the obligations that registration brings in terms of requirements to have accounting requirements, a compliance officer, and a whole variety of regulations that rightly stem from registration. It is impossible to properly assess which entities you register. And that can affect the entire structure of the business. So we think this is unfortunate. The approach that I think the banks have little option but to take is to explore every avenue as to which may wind up that they have to do something that is unexpected. So they are having to ready themselves for every outcome and that is an expensive exercise.

Mrs. ELLMERS. Sure. That is very difficult to do.

And I have a little more time so, Mr. Vice, do you anticipate that the U.S. rules governing clearinghouses will be comparable to the

regulations in foreign jurisdictions and what is the risk if they are not?

Mr. VICE. I think we are very concerned about that. The United States is pretty far out in front of the rest of the world, we operate a large clearinghouse in the UK, clearing CDS, commodities, and so, as managers of those businesses, we are trying to plan—we are looking at Dodd-Frank capital requirements for members, all of the other implications there. That clearinghouse is also a U.S. DCO, which means that it is registered with the CFTC and capable of clearing U.S. swaps businesses as well as U.S. futures. So that kind of dual registry, which is important for serving global markets like commodities, like FX, it is going to be critical that those rules are harmonized and that they are as close as possible. Otherwise, it is going to be pretty messy quite honestly.

I think there is a good history between the CFTC and the FSA in terms of mutual recognition, cooperation, information sharing, recognition of comparable regulation not exactly the same regulation, and so our hope is that as the rulemaking continues that there will be some harmonization there.

Mrs. ELLMERS. Great, thank you.

Mr. Chairman, I yield back the remainder of my time.

The CHAIRMAN. The gentlelady's time has expired. Mr. Boswell for 5 minutes.

Mr. BOSWELL. Well, thank you, Mr. Chairman.

A couple of questions and we have had several Members arrive, so I want them to have some time.

The whole panel, those supporting H.R. 3283, in the past our regulators and foreign regulators have worked together to respect each other's respective jurisdictions and, in the words of Mr. Vice, lead to greater harmonization of regulation yet allow foreign regulators to oversee their institutions. Is there anything in the law that prevents the regulators from continuing this approach? The language of concern that you cite has not been interpreted yet by the CFTC and the SEC. Can they not read the language in a manner consistent with this past cooperative approach of foreign regulators? We will just go across. I would like for all to comment if you care to. Mr. Vice?

Mr. VICE. Is the question is there anything preventing regulators from cooperating in the future as they have in the past? Not to my knowledge.

Mr. BOSWELL. Can they?

Mr. VICE. Can they? I think they can. I think from a practical standpoint as we sit here today, regulators—certainly the FSA and the CFTC—are struggling with staffing. There is a lot of attrition in those agencies. They are struggling with budget challenges while they are trying to write rules, anticipate unintended consequences, and then probably last on the list is harmonizing with international regulators. So it is an enormous amount of work that they are having to do in a very short amount of time.

Mr. SALTZMAN. Several agencies are involved in the picture. It is the SEC, the CFTC, the Fed. Obviously, we have been focusing an awful lot on the UK regulators but the derivatives market is a global marketplace, and as we indicated, legal certainty is critically important. So even if you could get to that normative goal of per-

fect harmonization, you have a sequencing and timing issue where the United States is readily apace at appropriately adopting many of the implementing regulations that provide the protections that we support, but you do have complexities as a result of that timing. So legal certainty at a statutory level would bring together the agencies and provide clarity to the marketplace.

Mr. BAILEY. And as you know, the provision in the statute requires that the regulators reach out and try to reach harmonization with the international regulators. I think that they are attempting to do that. It is a challenging issue which is accentuated by the timing differences that are arising between the U.S. rules and the rules that are coming into play in Europe and Asia, but there is absolutely a requirement that they do so and we believe that that is an achievable objective.

Mr. BODSON. I think it is more H.R. 4235. I think the uncertainty that has been created for the indemnification and the plenary access issues breach this trust to a certain extent and puts up barriers to global cooperation. And the issue of data fragmentation is very much about everybody being able to see the data or the information they should see as a regulator, while also providing global systemic risk management. But when there are rules that appear to allow U.S. regulators to have a farther reach than their global colleagues may have, cooperation starts to fail.

Mr. BOSWELL. Thank you, Mr. Chairman. I yield back.

The CHAIRMAN. The gentleman yields back.

Mr. Huelskamp, 5 minutes.

Mr. HUELSKAMP. Thank you, Mr. Chairman.

A question for all the members of the panel, we have been hearing about increased risk that foreign countries are threatening to potentially retaliate for U.S. actions on financial reform they may view as an overreach. In your opinion, do these threats in fact exist and how and where would you think the risk is the greatest, and what could be a potential response on our side to avoid that? I open that to anyone who would like to answer that question.

Mr. BODSON. Well, we saw in the European draft and your legislation that when they saw the indemnification and the plenary access issues, they were putting similar wording into their legislation. They have since pulled back from that. Other countries have followed suit such as Singapore, but that possibility of it arising again could always be out there. We have seen Hong Kong for a variety of reasons but one of which is the indemnification issue choose to go with a local repository and again starts the process of data fragmentation. Now we are working with them to get feeds of information in so there is a global view when there are global products involved. But you see the instance is already there, so we are working with legislators to get the wording out, but they are retaliating. And rather than taking an offensive stance on this, I think this is one where by fixing the issues here in legislation we avoid having the retaliation, or the issue come up at all.

Mr. HEULSKAMP. Okay.

Mr. BAILEY. I agree with that. I would also note that in the earlier legislation that was recently agreed in Europe which deals principally with the clearing issue and the market infrastructure issues, at the last minute they introduced a provision which is ex-

tremely comparable to the Dodd-Frank extraterritorial provision, that the language is very slightly different but it deals with direct and foreseeable impact on the EU. It allows another regulatory body to impose a clearing in uncleared margin of requirements on transactions that are outside the EU, which meet that standard and are having a direct and foreseeable impact on the EU. Our understanding is that was inserted as a cautionary available tool to allow them to take essentially whatever action the United States—at least the interpretation of Dodd-Frank may choose to direct towards Europe. It is a very real risk that the Europeans will take a corresponding view on wherever the United States lands on this issue.

Mr. HEULSKAMP. Yes. Mr. Bodson?

Mr. BODSON. Just prudentially, there are appropriate theories for the jurisdictional nexus and it really requires some nexus to the United States. And, as we hear from some of the domestic regulators, they really are breaking new ground, possibly regulating overseas activities that will undoubtedly result in retaliatory measures. It is literally breaking ground by regulating activities that have no foreseeable nexus to the United States. I think it should be a source of concern for everyone.

Mr. HEULSKAMP. I yield back. Thank you, Mr. Chairman.

Mr. BAILEY. Maybe just one more point. In relation to the Volcker Rule, which is obviously a very different context, I think you have seen a sense of the regulatory response from the offshore regulators as to the potential impact that that will have on their shores and on their markets. And last, it is a different context. I think it sets the tone.

Mr. HEULSKAMP. Okay. Thank you.

The CHAIRMAN. I thank the gentleman.

Ms. Sewell for 5 minutes.

Ms. SEWELL. First, I would like to thank the Chairman Conaway as well as Ranking Member Boswell for having this hearing today and to our witnesses for testifying before us.

This hearing has given us the opportunity to really hear from practitioners in the area of swaps and understand better why modifications to the confidentiality in the swap jurisdiction requirements in Dodd-Frank need to be made. As we continue to move forward with the rulemaking and implementation process provisions of Dodd-Frank, we must be mindful of the original purpose and intent behind the passage of such legislation. Dodd-Frank was intended to provide more transparency and oversight to our financial markets and to ensure that another financial crisis and meltdown does not occur.

I want to applaud the diligent work of both the CFTC as well as the SEC in drafting and implementing critical new regulations. And I also would like to remind Members of Congress that we must continue to make sure that we hone and refine and clarify any provisions that may be unintended consequences of such regulation.

Having said that, as a former practitioner in the securities industry—I was a lawyer at Davis Polk & Wardwell for over 7 years—and as a practitioner myself drafting swap contracts as well as derivatives, I understand fully the implications of the unintended consequences with respect to especially the indemnification provi-

sions that are currently being required by Dodd-Frank. And that is why I am a cosponsor of H.R. 4235.

My comments or questions are really directed to Mr. Bodson. I want you to talk a little bit more about the systemic risks involved in not correcting the indemnification provisions as well as helping to eliminate data fragmentation, and talk a little bit more about the data fragmentation that would occur if we don't correct that provision.

Mr. BODSON. Sure. Thank you very much. Transparency of accurate and comprehensive data is a very powerful tool for the markets and for regulators. Uncertainty over that data breeds risks and breeds inappropriate actions. So let's roll the clock back a little bit and go back to the Lehman event and that weekend when the markets obviously were in a state of flux and high anxiety. There were market rumors about what was going to be happening with Lehman, whether Barclays was going to buy portions of the business and the debt.

And if you think back to that weekend in September of 2008, you had *The Washington Post* and *The Financial Times* and *The New York Times* started speculating about what would the level of payments that were going to be made on credit default swaps on Lehman debt. And the numbers started going from $50 billion to $100 billion to $200 billion and it culminated with a $400 billion number. You could see the markets starting to quiver saying, where is everybody going to come up with $400 billion given what was going on in the marketplace? At that point, Federal Reserve Bank of New York President Geithner was asking, what is the real number? As a result of a trade information warehouse we have for credit default swaps, we knew with a pretty high level of certainty that the actual number was $6 billion. We knew because we had a comprehensive database of global positions. It was clean data, it was active data, and we knew the number was a very accurate number so we issued a press release. And you could see the tension going down immediately.

It is just an example of what happens when you know you have a certainty over a number that you can provide the markets and the regulators with a clear picture of what is happening. If that $400 billion number had continued to float out there, the Asian markets would have melted down and it would have just exacerbated what was already a horrible situation in the marketplace. So comprehensive global data gives regulators the ability to manage systemic risk. They still have the access to the underlying data for their constituents or their parties of interest, but having that global view allows things to be put into context. If it starts fragmenting, putting the pieces together again; it is Humpty Dumpty revisited.

Ms. SEWELL. Thank you for that. I understand that your company is currently operating a trade repository for credit default swaps. Can you please explain the impact of the indemnification and plenary access requirements on how your company shares information with global regulators?

Mr. BODSON. Sure. There has been a great level of global cooperation through the OTC Derivative Regulators Forum, this group of 40 regulators who have come together to create a protocol

and the CFTC, SEC, and the Fed have all been involved in creating that protocol to allow regulators to come in and to get comprehensive data on credit default swaps. They go to one place. They come in through what we call a regulatory portal. They can do their inquiries as to the parties of interest and get that information back immediately. If we did not have the trade information warehouse, they would not be able to do that. They would have to go to repositories around the world, pull the information together, get rid of duplicative transactions, try to standardize the data schemas. They would never be able to get a comprehensive view on a regular day much less during a period of stress. Right now, they get it.

Ms. SEWELL. Thank you so much for your testimony.

Mr. BODSON. Thank you.

The CHAIRMAN. I recognize Mr. Neugebauer for 5 minutes.

Mr. NEUGEBAUER. Thank you, Mr. Chairman. This is a question for Mr. Bailey and Mr. Saltzman. You know, commodity swaps particularly for agricultural products are very important to producers in my Congressional District and other Members, and it would be interesting to see what your perspective on Section 716 and what its effects if any it would have on hedging opportunities for the farmers and ranchers?

Mr. BAILEY. Section 716 as you know would require the push-out of the commodity business into a subsidiary, which is not having access to discount window. And the cost of doing that is multiple. That decision would have to be independently capitalized. And that isn't a zero-sum game. That isn't simply a matter of moving capital from the exiting bank and putting it into the subsidiary. It is an additive requirement. That subsidiary would have to meet basic creditworthiness in order to be a sustainable counterparty to the agricultural community. It is unfavorable in terms of the risk management treatment both on the client side and the bank side. It requires additional dedicated risk management people. And we see this is a very real concern in terms of its translation into higher costs.

I can certainly speak for Barclays, who is a meaningful player in the space in the commodities markets. We are quite concerned about that issue in terms of what it would do to our ability to provide the kinds of prices that we do currently to our customers. And obviously that isn't simply a matter of the trading customers or investment banking clients for whom we transact significant deals where the kind of larger hedges that attain to those and are important to be able to be done. Otherwise, the transaction really is at risk of failing to achieve completion.

So we think that your question is very pertinent and it is something that will translate to significant increased costs for those banks that are having to move down that subsidiary route. It is possible that others will find that it is simply too expensive a proposition to do that and may in fact find themselves with little options but to withdraw from the marketplace which gives the customers less ability to clear as market participants.

Mr. NEUGEBAUER. Mr. Saltzman?

Mr. SALTZMAN. I would just add a few thoughts. Clients lose the benefit of setoff and netting, which is likely to artificially increase collateral and margin requirements to the benefit of no one. You

also have various operational risks associated with the segregation of both—as Mr. Bailey said—from a bank's perspective as well as from the end-user's perspective. A whole new set of documentation, a whole new set of parameters around that really to no advantage. You are really creating just a completely duplicative architecture that in and of itself is likely to increase costs substantially to the end-user, and in some cases obviously crowd out those who are at the edge in terms of the price and cost-benefit.

Mr. NEUGEBAUER. So I wanted to kind of say back, what I heard: there are really two costs. One probably would increase the transactional cost because you have to go and duplicate the capital structure and the architecture in another entity, but second, that some current market participants may just decide not to make a market or to be involved in those activities. Is that a possibility?

Mr. SALTZMAN. Very much so. I would also add from the swap dealer's perspective, you are materially increasing operational risks, and as Mr. Bailey said, risk management, risks which in and of itself would also translate into credit appetite, which in and of itself could have an inhibiting impact on providing the investing and hedging activities that swap dealers do need to provide to commodity end-users.

Mr. NEUGEBAUER. Mr. Bailey, do you want to amplify on that?

Mr. BAILEY. I agree with your assessment.

Mr. NEUGEBAUER. Thank you very much, Mr. Chairman. I yield back.

The CHAIRMAN. The gentleman yields back. Mr. Scott for 5 minutes.

Mr. SCOTT. Thank you very much, Mr. Chairman. You know, no legislation is ever perfect, especially one that is as large and as complex in scope as Dodd-Frank is, and as such, we shouldn't be afraid to revisit the issue, make changes and alterations where they are due. And the bills before us do just that on swap jurisdiction, repeal of Section 716, and the swap data repository clearinghouse indemnification. They are, in large part, just clarifications and revisions that do not undermine the letter or the spirit of this historic financial reform bill that was passed by this body and of which I am a cosponsor.

I also think it is worth noting that the manner in which these bills were evolved, this is very important. The sponsors of these bills and their staff, both on the Majority and the Minority side of the aisle in this Committee and in the Committee on Financial Services, both of which I serve on, worked very closely together and with great consideration to one another's concerns to ensure that these bills were narrow, that they were targeted and addressed real problems. And that is why we have seen these bills move with strong bipartisan support, including mine through the Committee on Financial Services, and it is my hope, Mr. Chairman, that the same spirit of cooperation will reign in our Agriculture Committee as well and that we continue to see these bills progress smoothly through the legislative process.

So let it be noted, Mr. Chairman, that in spite of what many may say, bipartisanship and cooperation is alive and well as demonstrated by our work on this bill.

Now, let me turn to you, Mr. Vice, to discuss H.R. 3283 and some of the concerns you mentioned in your testimony with respect to the extraterritorial reach of certain provisions of Dodd-Frank. It is my understanding that you are already experiencing potentially duplicative regulation on your activities conducted at your clearinghouse in Europe. Perhaps you could elaborate for us on what you think the SEC is attempting to accomplish by venturing into territory—that is to say your energy swaps activity which is already, as I understand, regulated by the CFTC here in the United States and the FSA in the UK. How would H.R. 3283 address or remedy this situation?

Mr. VICE. Well, just for background there, we have a London-based clearinghouse. We started about 5 years ago and of course it is regulated by the FSA clearing commodities swaps. A couple years after that we began clearing credit default swaps including index and single name. Excuse me. Prior to that, we registered as a U.S. DCO in preparation for Dodd-Frank to be able to clear U.S. OTC swaps and potentially even U.S. futures. So with that we were essentially dually regulated by the CFTC and the FSA.

Subsequent to that, we did begin clearing credit default swaps, which for the single-name CDS brought in SEC oversight, appropriately so——

Mr. SCOTT. Yes.

Mr. VICE.—and so we have been in that business we have been overseen by three regulators. Some of the obscure language, an artifact of Dodd-Frank, gives the SEC some oversight of commodity swaps, believe it or not. In informal discussions with SEC staff, everyone can look at that and conclude that wasn't really the intent, but at the same time, they have proceeded on with essentially regulating our commodity swaps business. And we clear hundreds of commodity swaps in that clearinghouse and we add new swaps all the time. We are at a point now where each time we want to clear an additional swap that is already existing, is traded bilaterally on a global basis in some cases not even with any nexus to the United States, maybe traded largely in Asia, we are required to get FSA approval, CFTC approval, and now SEC approval. So it has dramatically slowed down our process there.

Mr. SCOTT. There are some concerns that because of technology and because of electronic transactions that this business is highly mobile and it will naturally shift overseas to less regulated markets. What are your opinions on whether or not this is a real risk? And are there ways we can strengthen the language in this bill to prevent this from occurring while still accomplishing our goals?

Mr. VICE. Yes, it is definitely a real risk. In fact, the primary reason we built our own clearinghouse in 2008—we were clearing at the London clearinghouse at the time—and the speed with which they could clear additional products for us was costing us business and was going to put us out of business eventually, so we needed to be in control of that part of our service, which includes getting regulatory approval for those products. So we have seen firsthand it is a very competitive environment out there between clearinghouses globally. All of these markets, whether it is FX, commodities, interest rates, they are global markets and so I guess the good news there, there is healthy competition among exchanges

and clearinghouses and so we are very sensitive to unlevel playing field things like this. So this is again much like the indemnification issue which seemed like an obvious technical fix. I don't think anyone in Washington intended for the SEC to regulate commodities laws.

Mr. SCOTT. Thank you, Mr. Vice.

Thank you, Mr. Chairman.

The CHAIRMAN. The gentleman yields back.

Mr. Crawford for 5 minutes.

Mr. CRAWFORD. Thank you, Mr. Chairman.

Mr. Bodson, I just have a couple questions for you. Can you cite a specific example of when your trade repository has been able to provide regulators with accurate, timely information during a time of crisis?

Mr. BODSON. I think, too, of the scenario I explained before during the Lehman Brothers crisis. There was obviously a lot of misinformation in the marketplace, which created uncertainty which created risk, and could have had a snowballing effect into the Asian marketplace providing that certainty over the exposure of its Lehman Brothers to the anxiety out.

The other most recent event really is the Greek default situation where we were able to provide regulators throughout Europe primarily insight just to exactly what the exposures were for their financial institutions. And again, by coming in they were able to get a complete view not only of the positions but the counterparty risk that was involved, and that allowed them to focus their efforts on where the exposure would be. So again, without a global view, they would be having to go through regulators or SDRs around the world, try to get that information, try to normalize it, and try to get a view. In times of crisis, that is not the approach you want to take. So those are two instances where the regulators were able to do their job effectively by having a comprehensive global view.

Mr. CRAWFORD. Okay. If the indemnification provision is not removed from Dodd-Frank, in your opinion would it hurt regulators' ability to oversee global systemic risk?

Mr. BODSON. Most definitely. I think the key is that being able to rely on a comprehensive data set that shows the full content and allows a full understanding of what is happening in the marketplace, allows for regulators to pinpoint their focus on where areas of risk may be arising, is critical. When you don't have that comprehensive view, when you have inaccurate data, you have inaccurate information, you are going to have the wrong actions. You are going to be focused on the wrong issues. Very simply, I mean the case that has been pointed out is AIG. If regulators had a sense of what was going on at AIG, would the issue have arisen to the level? You know, you are not going to be able to see it just by looking at an SDR but it will give you the telltale signs that I should be going in there, I should be looking at what is going on, I should be able to understand where that exposure is on a global basis. Without that information, when you start fragmenting it, you are never going to get that full view.

It doesn't stop regulators from going into the firms or looking at specific transactions for market manipulation. They have those rights under their jurisdictions for the areas of interest. But by

having that global comprehensive view also gives them a context they wouldn't have otherwise.

Mr. CRAWFORD. I understand these two issues indemnification and plenary access are separate and distinct. Can you explain why Congress should legislate a resolution of both indemnification and plenary access, and are both of those issues adequately addressed in H.R. 4235?

Mr. BODSON. They are addressed in H.R. 4235. You can almost view them as two sides of the same coin. I mean in one case you are asking overseas regulators to provide an indemnification, which is not a concept they are used to; it is a U.S. tort law issue. And they really are not going to be willing to give an indemnification to a private entity such as the SDRs. That will cause the fragmentation. The plenary access issue is one where there is concern that confidentiality will be breached. You know, under the ODRF, as I mentioned before, there are great levels of global cooperation and trust in terms of respecting each other's boundaries in terms of what information will be accessed, who has the supervisory rights. If that trust is broken, you will see the same issue as indemnification. Regulators will not feel comfortable putting information into global trade repository. They will start pulling the information back to local repositories and you will get data fragmentation. Back to my previous answer, systemic risk therefore becomes that much more difficult.

Mr. CRAWFORD. Thank you, Mr. Bodson. I appreciate all of you being here today.

I yield back.

The CHAIRMAN. The gentleman yields back.

Mrs. Hartzler for 5 minutes.

Mrs. HARTZLER. Thank you, Mr. Chairman.

Thank you, gentlemen. I apologize for my tardiness as well, I had another committee meet at the same time so it is kind of frustrating.

But I was just wanting to ask the panel a couple of questions and then another one specifically if we have time to Mr. Saltzman. But the first question, where do you see the greatest diversions between the United States and other countries implementing derivatives reforms? Mr. Bailey?

Mr. BAILEY. If I could just take that. And I speak principally in relation to Europe. There are very different approaches to a number of issues between the United States and the European regulators, but within the foundation of it, the broad commitments that were made as to derivatives. So it is all within the context of a requirement to clear appropriate transactions, who should be exempt, and a requirement to transact on regulated venues. While in the clearing space there is, in large part, a parity and we are very optimistic that there will be a position where regulators can mutually recognize clearinghouses in other jurisdictions because the protections are adequate.

But, one of the more difficult areas may be in the execution space, the requirement that was in Dodd-Frank, of course, to trade certain products on SEFs is narrowed in the current negotiations of the documents around the market and financial instruments directly, which is the upgrade for the current regulations pertaining

to execution in Europe. But the approach may be a little different there and it is still at an earlier stage. We haven't seen anything yet in the sense of rulemaking from ESMA (European Securities and Markets Authority). That is clearly a risk for some divergence and that would create some clear difficulties if Dodd-Frank were to have extraterritorial application into Europe where for the same transaction you would be obliged to execute all and that obviously means that the trade wouldn't happen. So we think that is an area of concern.

As to reporting again we are hopeful that even real-time reporting of transactions to the market, we think that there will be sufficient consensus there, not to be too problematic. And as to issues around code of conduct, there are instances where you can see real conflicts, but in most cases it is a matter of avoiding duplication and layering of different requirements. Clearly, if we are transacting out of London to the Italian customer as it relates to the Investor Protection Rules, we principally think the Italians would hold sway on that, and secondary would be the London FSA because of where we are situated if we are transacting out of London. Whether the CFTC should be engaged in the matter in which that trade is executed we think is highly questionable. So it is really in execution that I think we have the concerns.

Mrs. HARTZLER. Can I follow up on that? And then I want to hear Mr. Saltzman. So are the execution concerns dealing with proposed regulations, concerns you think that might come down from Dodd-Frank, or are there already concerns in the legislation that you think clearly are going to be problematic?

Mr. BAILEY. It is at the regulation stage so it is not yet certain that it is problematic. It is potentially problematic.

Mrs. HARTZLER. So is there any legislation in the works to try to address those concerns right now, that aspect, proactively——

Mr. BAILEY. Well, the legislation that is before this Committee which would limit the jurisdiction of the United States imposing a particular execution requirement for transactions outside the United States would obviate that, so yes.

Mrs. HARTZLER. Very good. So it does address that.

Mr. BAILEY. Yes.

Mrs. HARTZLER. Perfect. Yes, Mr. Saltzman?

Mr. SALTZMAN. Just very briefly I would also add no other jurisdiction is contemplating the push-out of swaps as we have in Section 716 and that is confirmed by Governor Tarullo, who I believe spoke before the Senate Banking Committee this week where he indicated that we are a loner in that respect. I think that is obviously a material structural difference between our approach to these issues and other jurisdictions.

Mrs. HARTZLER. Okay. One of the principal goals of Dodd-Frank is to reduce systemic risk, so could you please discuss how the bills that we are considering today, how they would impact regulators' ability to monitor and to mitigate systemic risks?

Mr. VICE. I will speak on the indemnification piece. I will let the banks respond to the extraterritoriality bill. ICE operates a repository much like DTCC. We are also in full agreement and support of this bill to address the indemnification issue, the full access issue for all the reasons that I think DTCC articulately laid out.

I think we probably have a little different—it is important to differentiate some of the reasoning that DTCC has given for that. I mean Dodd-Frank allowed—the CFTC promulgated rules to allow multiple repositories, in other words, much like the clearing business or the exchange business allow that to be a competitive landscape. That means that by default there will be some aggregation of data across repositories. Regulators, particularly the CFTC, are very adept at doing this. They already aggregate data across exchanges and across clearinghouses. So SDR can readily be done as well.

I think the unique problem that these issues bring up where we are in agreement with DTCC is it gives rise to the possibility that a trade could actually end up in two different repositories. So until you had a foreign exchange trade, a Euro-dollar trade with a U.S. bank and a UK bank, if those provisions are allowed to stand, the U.S. bank to be compliant or the set that it is trading on to be compliant may have to get that trade to a U.S.-registered SDR, which EU doesn't have access to, and similarly, it may go to any U.S. SDR. So you can see that type of duplication or data integrity that you would want to try to avoid. But, the more operational issue of aggregating data is, I mean that is the business we are all in, running computer systems. That is not rocket science.

Mrs. HARTZLER. Okay. Thank you very much, gentlemen, I appreciate it. I think my time has expired.

The CHAIRMAN. The gentlelady's time has expired.

Staying on that same theme, could each of you comment quickly or briefly on what the costs to you will be if we don't pass these corrections bills today, or if they don't get the President's signature relatively quickly?

Mr. VICE. Again, I will say on the indemnification issue we are assuming it doesn't go away. We are hopeful it does but we will be registering separate entities with their own staff and resources and overhead. Certainly for starters we already have an application in with the CFTC for a U.S.-registered SDR and once the rules are out on the EU we would be registering as an SDR there. We will have to have what presumably will be all of the physical plant and chief compliance officers and people on the ground, essentially, duplicating what we are doing in the United States, and then I assume probably in other jurisdictions as well outside the EU.

The CHAIRMAN. Mr. Saltzman?

Mr. SALTZMAN. I think certainly with respect to H.R. 1838, the costs of running duplicative derivatives activity out of two separate legal entities and the ensuing risk management, collateral management, pricing, costs will be Draconian, including, as indicated earlier, many market participants on both sides of the transaction potentially leaving the business, thereby creating more systemic risk. I think Chairman Bernanke and former FDIC chair Sheila Bair during the course of the debate recognized the systemic risk associated with pushing the derivatives out to a less regulated, less well capitalized legal entity. And I would say with respect to the H.R. 3283, extraterritoriality, the tremendous legal uncertainty that continues to hang over the marketplace. It is very easy to quantify hard costs, but it is very difficult to quantify the soft costs of really not knowing how your business is going to be structured. It is al-

most proving the negative, what businesses are you not entering into, what business are you not doing because of that legal uncertainty.

So we would urge the Chairman and the rest of the Members of the Committee to promptly and swiftly pass both bills. But thank you very much.

The CHAIRMAN. Mr. Bailey, quickly?

Mr. BAILEY. I totally agree with Mr. Saltzman's comments in relation to the push-out bill which we have kind of covered before as well, highly expensive and likely to involve additional cost to customers of all segments of the marketplace.

Just make one comment additionally on the extraterritorial bill, to the extent that there are conflicts that arise because or irreconcilable rules applying either here or in Europe or in Asia, that will result in transactions not occurring. Even if those are merely duplicative rules, it is creating an acquiring expense to make sure you are compliant with the higher standard and they may itself be sufficient to cause a firm to feel that they have to move their businesses to a "subsidiary-ized" structure in order to have only one set of those rules apply. And so you get the cost increment through that process.

The CHAIRMAN. And Mr. Bodson?

Mr. BODSON. It is hard to identify pure cost of what happens when you have repositories popping up all over. We are creating five asset class repositories, three data centers. It is about $¼ billion spending in the next 5 years. But that is the hard dollar cost. That is easy to kind of estimate. Really it is what is the cost to the financial system of the uncertainty of not having comprehensive overview of what is happening in the marketplace? What happens in the next crisis when regulators or market participants are reacting inappropriately because they don't have a full view? That is the cost that is almost impossible to gauge.

I do want to clarify by the way H.R. 4235, this deal with the indemnification and not the plenary access when we spoke before. I think that is the harder number to quantify is what happens when you don't have a full comprehensive view of what is happening in the marketplace? The SEC and CFTC can answer that better.

The CHAIRMAN. The SEC has actually come and encouraged Congress—speaking of the indemnification—pass this fix. Yet the CFTC is saying they can actually just do that by some sort of an interpretive guidance. Mr. Bodson, your comments on which approach you would prefer? That is a leading question.

Mr. BODSON. Yes. Well, let me see if I can swing and not miss this one. As I said before, it is a legislative issue and legislation fix it. I think while guidance may provide some comfort, at the end of the day, foreign regulators are very focused on what is the rule of the law, what does the legislation say and not what guidance says. So fixing this through legislation will provide the certainty that regulators want to have.

The CHAIRMAN. Well, thank you. It would be helpful as we continue to build a case as to why this is important. If you could provide the Committee—this is a request, not any kind of a requirement—your thoughts on those hard costs of what you see occurring in your organizations if we don't do these things and do them on

a timely basis, and as well as some thoughts on those soft costs no one really can quantify is what impact does it have from your intuition on the markets on people either entering businesses or not entering businesses. If you could provide that to the Committee over the next several days, we would most appreciate it. If you don't want to do that, that is fine as well because I do appreciate all four of you coming today to visit with our Committee and help add more momentum. Obviously, these came out of Financial Services yesterday afternoon. We will have a markup on them I am told in the Agriculture Committee and move these to the floor.

So again, gentlemen, thank you for coming here to help us with that process.

Under the rules of the Committee, the record of today's hearing will remain open for 10 calendar days to receive additional material and supplementary written responses from the witnesses to any questions posed by a Member.

This hearing of the Subcommittee on General Farm Commodities and Risk Management is adjourned.

[Whereupon, at 11:48 a.m., the Subcommittee was adjourned.]

[Material submitted for inclusion in the record follows:]

LETTER SUBMITTED BY MICHAEL C. BODSON, CHIEF OPERATING OFFICER, DEPOSITORY TRUST & CLEARING CORPORATION

April 10, 2012

Hon. K. MICHAEL CONAWAY,
Chairman,
Subcommittee on General Farm Commodities and Risk Management,
House Committee on Agriculture
Washington, D.C.

The CHAIRMAN. Well, thank you. It would be helpful as we continue to build a case as to why this is important. If you could provide the Committee—this is a request, not any kind of a requirement—your thoughts on those hard costs of what you see occurring in your organizations if we don't do these things and do them on a timely basis, and as well as some thoughts on those soft costs no one really can quantify is what impact does it have from your intuition on the markets on people either entering businesses or not entering businesses. If you could provide that to the Committee over the next several days, we would most appreciate it. If you don't want to do that, that is fine as well because I do appreciate all four of you coming today to visit with our Committee and help add more momentum. Obviously, these came out of Financial Services yesterday afternoon. We will have a markup on them I am told in the Agriculture Committee and move these to the floor.

Attn: Paul Balzano

Mr. Chairman,

In response to your question regarding the "hard" costs of establishing the Global Trade Repositories, the following is a high-level, thumbnail sketch of the challenges and costs to develop the infrastructure necessary to provide global regulators the transparency requisite for them to supervise the five major derivative asset classes (Credit, Interest Rates, Equities, FX and Commodities).

Estimating the financial costs of developing software and implementing necessary infrastructures to develop and aggregate global data sets involves many variables. While fixed costs can easily be estimated, it also necessitates that some broad assumptions be made to estimate the variable costs over time. More consequentially, the hard dollar cost to construct the GTR network is relative to the potential risk caused by the failure to modify the indemnification provision and the resultant diminishment in market oversight resulting from lack of transparency; that section of U.S. law will have a more critical impact on systemic risk than just adding up the infrastructure investment.

The hard cost investment of setting up a Trade Repository (TR or SDR), is between $20–$25 million per data center—just for physical facilities and core infrastructure. While the DTCC standard for infrastructure build-out is heavily focused on ensuring that appropriate safeguards are in place regarding issues such as resiliency, data protection, and redundancy, the range is a reasonable proxy for the cost of establishing one data center. Note however that in order to provide certainty over disaster recovery and continuous data access, DTCC is establishing three data-centers globally. This hard dollar estimate does not include the direct financial impact on member firms expected to report the data to the repository such as their connection costs to the resultant data reporting regiment(s) and other related regulatory obligations. Beyond the cost of establishing and maintaining multiple points of connectivity, the inevitable deterioration in common standards will add another layer of complexity and expense which firms will be required to deal with in order to meet regulatory reporting requirements. These costs are difficult to estimate but will increase over time.

It is difficult to estimate the software development costs associated with a *de novo* establishment of an SDR but DTCC will be incurring costs of approximately $50mm over 3 years to build the GTR system worldwide. In addition, on an ongoing basis, direct support costs for the datacenters will be approximately $9mm per site per year. The global business management team supporting the GTR will cost approximately $10mm. While the scale of the GTR system is much larger than that of a single national repository, DTCC also has the benefit of years of experience in the repository space which has been critical in designing the GTRs and in executing the global roll-out of them. No value to these capabilities has been estimated.

If the Indemnification provision remains in U.S. law, there is a high probability that derivative trade data will fragment into multiple local TRs in different jurisdictions globally. The decision by Hong Kong, and potentially other sovereigns, to have national repositories in order to meet both local needs and avoid the indemnification

issue will complicate global TR development. While cooperation with these jurisdictions should minimize their impact, having additional multiple national repositories will make the problem of aggregating data increasingly impossible to do, especially in times of stress.

But the real "hard" cost is the systemic risk of failing to provide aggregated and netted data to allow regulators to mitigate risk concentrations during times of financial bubbles and market downturns. That cost, as 2008 nearly proved, would be catastrophic. Once data is fragmented, timely "defragmentation" in times of crisis is a near impossible challenge that risks global financial markets to the luck of guesswork, rather than a reasoned response to market conditions.

Once data is fragmented, the further uncertainty created by the plenary access concerns further compounds the issue by making aggregation and netting of data impossible to do, especially for U.S. regulators. In order to aggregate data in the U.S., non-U.S. nexused data must be combined with U.S.-nexused data. However, the moment the data is brought into a U.S. domiciled repository, it could be subject to plenary access claims by U.S. regulators. In order to avoid this issue, non-U.S. based repositories would by necessity avoid sending data into the U.S. The end-result is an inability to aggregate data with the resultant lack of market transparency which Dodd-Frank sought to achieve in the first place.

Thank you for the opportunity to provide a more detailed and thoughtful answer to your question. Please do not hesitate to contact me, or Dan Cohen in Washington, D.C. [**Redacted**], for additional information.

Sincerely,

MICHAEL C. BODSON,
Chief Operating Officer,
President of DTC, NSCC and FICC,
Chairman, EuroCCP and MarkitSERV.

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