

1 U.S. COMMODITY FUTURES TRADING COMMISSION (CFTC)

2

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5

6 Commodity Futures Trading Commission - CFTC

7 Open Meeting

8

9 Three Lafayette Centre

10 Office of Secretariat

11 1155 21st Street, N.W.

12 Washington, DC 20581

13

14 BEFORE:

15 Heath P. Tarbert, Chairman

16 Brian D. Quintenz, Commissioner

17 Rostin Behnam, Commissioner

18 Dawn DeBerry Stump, Commissioner

19 Dan M. Berkovitz, Commissioner

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1 P R O C E E D I N G S

2 CHAIRMAN TARBERT: Good morning. This
3 meeting will come to order. This is a public meeting
4 of the U.S. Commodity Futures Trading Commission. I
5 would like to welcome members of the public and market
6 participants as well as those on the phone or watching
7 our webcast. I would also like to welcome my fellow
8 commissioners: Commissioner Quintenz, Commissioner
9 Behnam, Commissioner Stump, and Commissioner
10 Berkovitz.

11 As always, we will begin with the Pledge of
12 Allegiance. Today, General Counsel Dan Davis will
13 lead us in the pledge. And I will want to let
14 everybody know that last week, Dan received the
15 Chairman's Award for Excellence. That is the highest
16 award the agency bestows on a member of our staff.
17 So, Dan, why don't you please come up and -- our
18 general counsel does not appear to be here. Is there
19 anyone from the General Counsel's Office that can ably
20 represent our general counsel? There we go.
21 Herminio, thank you very much.

22 [Pledge of Allegiance]

1 CHAIRMAN TARBERT: Thank you. Well, there
2 is an old saying in leadership that you are as good as
3 your people are. And so one of the reasons the
4 General Counsel's Office has done such a fabulous job
5 is because it is staffed so well.

6 On today's agenda on the open meeting, we
7 have got three items. First, we will vote to finalize
8 Part 13 of the Commission's regulations. And that
9 will ensure that our rulemaking process is fully
10 consistent with the Administrative Procedure Act.

11 Second, the Commission will vote on whether
12 to reopen the comment period and request additional
13 comments on proposed regulations and amendments
14 relating to capital requirements for swap dealers.
15 Proposed regulations were previously proposed in 2011
16 and then re-proposed in 2016.

17 And then, third, we will vote on proposed
18 amendments to the swap clearing requirement exemption
19 for inter-affiliate swaps. This proposal would revise
20 the Commission regulation that exempts certain
21 affiliated entities within a corporate group from a
22 swap clearing requirement under our section 2(h)(1) of

1 the Commodity Exchange Act.

2 So now we will start with opening
3 statements. I will go first, followed by my fellow
4 commissioners in order of seniority. And I have been
5 told some of them will actually split up their
6 statements during the course of the rulemaking as we
7 discuss particular items. For me, I am actually going
8 to combine my opening and closing statements into a
9 single statement. And my statement is entitled,
10 "Tripling Down on Transparency."

11 As regulators, we must be mindful not only
12 of what we do but how we do it. Our shared vision for
13 the CFTC is to be the global standard for sound
14 derivatives regulation. Soundness is built on
15 transparency. Public input and dialogue help us serve
16 our markets. We owe it to those who rely on our
17 derivatives markets to regulate in the open.

18 I have long thought that the CFTC is the
19 most important regulator most Americans have never
20 heard of. We are working to change that. By the end
21 of next week, we will have held, this Commission, all
22 5 of us, 6 open meetings in the last few months of

1 2019. That is the same number of open meetings the
2 Commission held during 2015, 2016, 2017, and 2018
3 combined. With the help of my fellow commissioners --
4 and it is a lot of work -- as well as the staff, I
5 intend to continue this trend of open meetings in
6 2020.

7 While transparency is important for all
8 regulators, it is especially critical for us. The
9 Dodd-Frank Act gave us jurisdiction over the \$400
10 trillion notional swaps market. That is a humbling
11 level of responsibility, and it demands we give the
12 public visibility into what we are doing. We simply
13 won't regulate from behind a curtain. Reaffirming the
14 value of transparency is, therefore, vital.

15 In 2010, this agency faced immense pressures
16 in the wake of the Dodd-Frank Act. And the need to
17 "get things done" didn't always lead to getting them
18 done in the right way. Some have criticized the CFTC
19 for stumbling in its commitment to transparency
20 earlier in this decade. The agency from time to time
21 used staff no-action letters, policy statements, and
22 enforcement actions, rather than notice-and-comment

1 rulemakings. While our predecessors on the Commission
2 surely didn't make opacity the goal, it was sometimes
3 the result.

4 As we approach 2020 and beyond, I am pleased
5 to announce the CFTC will triple down on transparency
6 by focusing on three areas: number one, how we make
7 regulations; number two, how we apply them; and,
8 number three, how we enforce them.

9 The first area is transparency in
10 rulemaking. We will reaffirm the importance of
11 notice-and-comment rulemaking under the APA. Today,
12 as I mentioned, the Commission is voting on amendments
13 to Part 13 of our regulations. The amendments will
14 clarify how we receive, process, and respond to
15 petitions for rulemaking. Part 13 also retains
16 section 13.2, which permits any person from the public
17 to petition the Commission for a rulemaking. Now,
18 that is actually a unique feature of the CFTC
19 framework that reinforces transparency and the
20 public's ability to participate. More importantly, we
21 will publish those petitions from the public for
22 rulemakings on our website. That will further

1 encourage public engagement with our rulemaking
2 process.

3 Because of the help of my fellow
4 commissioners and our staff, we are also going to be
5 publishing a summary of our rulemaking process on our
6 website written in plain English so everybody
7 understands it.

8 The second area is transparency in staff and
9 other types of relief; in other words, how we apply
10 our rules. Wherever possible, we should regulate with
11 public notice-and-comment rulemakings. Staff relief
12 should be a supplement, not a substitute, for APA
13 rulemakings. Today I am pleased to announce that the
14 CFTC is finalizing guidance to ensure staff no-action,
15 interpretive, and exemptive relief letters are limited
16 to appropriate situations. Examples will include
17 unique circumstances that don't give rise or are not
18 suitable for a general rulemaking or only where
19 temporary relief is contemplated.

20 We must also increase transparency, even
21 where staff relief is appropriate. Today, I am also
22 announcing that as of January 1, 2020, the CFTC will

1 publish all requests for staff relief on our website
2 when our staff grants that relief. This harmonizes
3 our approach with that of the other Federal financial
4 regulators. And it also provides greater public
5 visibility into the issues before us.

6 The third, and final, area of transparency
7 is in enforcement actions. We have got to be
8 transparent in how we enforce the law. A key goal of
9 enforcement is to deter misconduct before it happens.
10 Deterrence requires clarity about how our laws work.
11 Long gone are the days when kings posted edicts high
12 on columns to make the law harder to read and easier
13 to violate. Our founders, instead, adopted a system
14 in which the law is king. And it has been said that
15 in our American system, the rule of law is the law of
16 rules.

17 As a result, our Enforcement Division will
18 soon be providing an updated enforcement manual. This
19 will inform the public of a number of changes designed
20 to increase transparency.

21 In addition, the Commission and its staff
22 must be able to speak publicly about enforcement

1 matters. Beginning on January 1, 2020, I will not
2 present this Commission with any proposed settlement
3 that restricts the Commission or our staff from
4 publicly stating their views. Affirming this right to
5 speak ensures the CFTC can inform the public about our
6 enforcement priorities. It also advances customer
7 protection. The facts of past cases can serve as
8 early warning signs of new types of fraudulent and
9 manipulative activity.

10 But genuine transparency in the enforcement
11 area can't be one-sided. Just as the Commission
12 should be able to speak freely about enforcement
13 actions, so, too, should defendants. Also beginning
14 on January 1, 2020, I won't put before the Commission
15 any settlement agreement that unduly restricts a
16 defendant's ability to speak publicly. While we will
17 still expect defendants the Commission will continue
18 to require that defendants not to deny facts or
19 statements that both they and the CFTC have agreed on,
20 we won't stand in the way of comments or criticism.
21 This approach is good for both transparency and
22 accountability. Defendants can speak freely, but they

1 also can't avoid tough questions by hiding behind
2 settlement language.

3 Transparency is sometimes avoided,
4 particularly here in Washington, because it opens the
5 door to criticism. But, as Aristotle reminds us,
6 criticism is something we can avoid easily by saying
7 nothing, doing nothing, and being nothing. Well, that
8 has never been of the path of the CFTC during our
9 nearly 45 years of regulating the U.S. derivatives
10 markets. Nor will it ever be. Just as we won't
11 shrink from calling out wrongdoing, so, too, will the
12 public have insight into what we are doing.

13 Criticism isn't always pleasant, but it is a
14 core facet of democracy. This Commission is an agency
15 of the United States Government. The CFTC should be
16 scrutinized when we act.

17 In 1787, Benjamin Franklin was leaving
18 Independence Hall in Philadelphia at the close of the
19 Constitutional Convention. As the story goes, a woman
20 came up to him and asked, "Dr. Franklin, what kind of
21 government will we have?"

22 He answered, "A republic if you can keep

1 it." Rest assured our Commission will do its part.

2 Thank you very much.

3 Commissioner Quintenz, the floor is yours.

4 COMMISSIONER QUINTENZ: Thank you, Mr.

5 Chairman. First, let me just take a minute to applaud
6 your statement and your eloquence and comprehensive
7 commitment to transparency through not only the open
8 meeting process that we have but important reforms to
9 the Commission to ensure that what we do is
10 transparent to the public. There is another saying
11 that sunshine is the best disinfectant. It is hard to
12 have accountability without transparency. And I for
13 one am a strong believer in accountability for all of
14 us to ensure that the public and our overseers on
15 Capitol Hill know exactly what we are doing and how we
16 are doing it. So bravo.

17 I am going to save my comprehensive
18 statements on these rules for their discrete
19 consideration during the open meeting, but let me just
20 cut to the chase and say that I am going to support
21 all three of them. And I really appreciate the
22 staff's work from all of the divisions and the Chief

1 Economist's Office and all the conversations that you
2 have had with my staff to help us understand and also
3 interpret and accept some of our points of view.

4 So thank you again.

5 CHAIRMAN TARBERT: Thank you very much,
6 Commissioner Quintenz.

7 Commissioner Behnam?

8 COMMISSIONER BEHNAM: Good morning. Thank
9 you, Mr. Chairman, for having the meeting. Thank you
10 for your statement.

11 And, like Commissioner Quintenz, I will
12 reserve statements as we consider each of the rules.
13 Quick thanks to all of the staff for all of their work
14 in working with both myself and my office to get to
15 today.

16 So I look forward to the meeting. And
17 thanks again for holding it.

18 CHAIRMAN TARBERT: Thank you very much.

19 Commissioner Stump?

20 COMMISSIONER STUMP: I am going to reserve
21 my comments for a bit later, but I did want to applaud
22 you. I wholeheartedly support us having a more

1 transparent and open process going forward with regard
2 to the many things we do. I think it is particularly
3 incumbent upon this Commission given that we, unlike
4 10 years ago, have the benefit of experience based
5 upon the things, the lessons we have learned as a
6 result of the rules that were put in place post-
7 crisis. And so it is very important for us to have
8 that ongoing dialogue with the public to ensure that
9 we have the right rules and the right modifications
10 and the right calibration as we move forward.

11 And I also would like to say we should never
12 shy away from criticism. Some of the best policies I
13 have ever worked on came as a result of having
14 somewhat critical conversations with people who even
15 sit on this dais today. And I appreciate that their
16 opinions made the work product all that much better at
17 the end.

18 Thank you.

19 CHAIRMAN TARBERT: Thank you very much.

20 Commissioner Berkovitz?

21 COMMISSIONER BERKOVITZ: Thank you, Mr.

22 Chairman.

1 I, too, fully support all your measures for
2 transparency. You have been transparent in your
3 support for transparency all along. And I am a big
4 proponent of that. I applaud your leadership in that
5 effort.

6 I am going to talk about some specific
7 things that you mentioned. We are talking about
8 transparency, I feel compelled to respond to some of
9 the statements that have previously been made, such
10 as, "We are going to be transparent, unlike what they
11 did previously," "unlike what the Commission did in
12 2010" and "They did it wrong back then, and we are
13 going to get it right now." And I feel compelled to
14 do this for the CFTC staff that is here as well as my
15 own involvement.

16 In the Dodd-Frank years from 2010 to 2013,
17 this agency did -- it depends on how you count it --
18 approximately 65 rulemakings. I haven't looked at the
19 website recently, but I believe we had between 45 and
20 50 open Commission meetings on those rulemakings. And
21 it was all the Commission rulemakings. We published
22 notices of proposed rulemakings. And we had final

1 rulemakings. People were complaining about all the
2 meetings we were having. We were having too many
3 meetings. We were going too fast. It was too much,
4 too much being made public.

5 I also want to say that it is a record that
6 I am particularly proud of. I feel somewhat
7 uncomfortable sitting up here today saying this, but
8 if I don't say it, it is not going to be said. And I
9 can't leave the record as it is. Not a single rule,
10 not a single of those 65 rules, was overturned or
11 successfully challenged on procedural grounds. There
12 wasn't a single violation of the Administrative
13 Procedure Act in any of those rulemakings. The only
14 rule that the court invalidated was the rule on
15 position limits. And it was a substantive
16 interpretation of the statute where there was a
17 mandate to issue position limits.

18 I see our deputy for litigation was part of
19 that team. We were up against the best lawyers that
20 private industry threw at us to overturn our rules on
21 cost-benefit analysis. The Securities and Exchange
22 Commission lost six times in the U.S. Court of Appeals

1 on cost-benefit analysis

2 Frankly, when we came in 2010, the cost-
3 benefit analyses that the agency was doing were
4 substandard. And we were challenged on it. The
5 inspector general issued a report saying we needed to
6 up our game.

7 When we upped our game on cost-benefit
8 analysis, the Office of General Counsel, the Office of
9 Chief Economist, and the CFTC staff all worked
10 together to make those cost-benefit analyses robust
11 and survive challenge in the Court of Appeals.

12 We have a very strong opinion from the U.S.
13 Court of Appeals affirming the way this agency did
14 cost-benefit analyses. We were up against the same
15 lawyers that defeated the SEC six times on cost-
16 benefit analysis. Okay? We did it right. We didn't
17 cut corners. We were transparent. We were upheld in
18 the U.S. Court of Appeals.

19 SIFMA challenged us on what we did. ISDA
20 challenged us on what we did. They challenged our
21 cross-border interpretation. They were unsuccessful.
22 They said, "Oh, you can't issue guidance. You have

1 got to do a final rule." The U.S. courts, the Federal
2 courts agreed with us.

3 I think we have a lot to be proud of in
4 those years. Now, we got those rules done in three
5 and a half years without a single procedural,
6 successful procedural, challenge. I think this agency
7 has a lot to be proud of for that record. And those
8 rules have held up over the years. Okay? One reason
9 those rules have held up over the years is because no-
10 action relief that was granted. Literally, there were
11 about 100 no-action letters granted in each of 2012
12 and 2013. That is a lot.

13 Fundamentally, what those enabled us to do
14 was get those regulations in place with a safety valve
15 so people could operate under those regulations
16 successfully. Okay? We weren't rigid. If people
17 needed more time, they got more time. If you needed
18 to adjust this condition, we adjusted that condition.
19 The very fact that today and the next meetings and the
20 previous meetings, we are essentially going to be
21 codifying that relief because we have now the
22 experience, the relief worked. We were able to put

1 that in place temporarily, see how it worked, say,
2 "Okay. Well, maybe the rule needs to be adjusted here
3 or there." It worked.

4 Now today we have the confidence that we can
5 make that permanent. Rather than saying, "Okay. We
6 are going to make this permanent. We are never going
7 to change it. This is it. You know, we are going to
8 make it really hard to adjust to fine-tune the dial,"
9 we made it possible to fine-tune that dial and then
10 have the confidence for -- the entire Commission can
11 sit and have the confidence that that is the
12 appropriate way of doing business. Then we modify the
13 regulations and make it permanent.

14 So I think the no-action letters, while I
15 agree that if you can put it in regulation, do. I
16 think the no-action letters do serve a valuable
17 purpose, and we need that relief valve. I
18 wholeheartedly support the approach. I do think it is
19 a big improvement that we are going to put the no-
20 action letters, the requests on, make those public
21 when we grant the relief. I do think that would be a
22 big improvement.

1 Finally, on enforcement actions, I know the
2 Defense Bar has been complaining all of the time about
3 making policy through enforcement actions. I wasn't
4 here for a lot of the times they were complaining, but
5 I have been on the outside. And I think that is a
6 Defense Bar objection. I don't think that is really
7 what the agency is doing. We have a statute to
8 implement.

9 Things like manipulation and fraud, as the
10 courts have said, the methods of manipulation are
11 limited only by the ingenuity of man. As more
12 ingenious methods of manipulation are presented to the
13 Commission, the enforcement staff in this Commission
14 has addressed those. That requires an evolution of
15 the law. Sometimes you apply new interpretations and
16 new factual situations. I know the Defense Bar
17 complains that that is making law as you go, but that
18 is what you do in enforcement cases. You have to be
19 able to have the flexibility to address.

20 So I applaud the transparency. I fully
21 support where you are going with that. You have been
22 a strong proponent of transparency. But I just feel I

1 have to correct the record as to what happened
2 previously in this agency's performance in the Dodd-
3 Frank years. We were transparent. We were effective.
4 Your statement, Mr. Chairman, about the best little
5 known agency, it is because of that. That is why we
6 have the reputation.

7 My colleagues here who were on the Hill at
8 that time -- the other thing, we were looked and this
9 agency was looked and it still is looked at as a
10 resource for Congress and an objective resource. Part
11 of the reputation was from those years, and part of it
12 has been carried on by predecessors and successors.
13 So it is a long tradition of this agency.

14 Finally, along the lines of transparency, I
15 want to really strongly support your statement that
16 you are not going to put before the Commission any
17 settlement agreement that constrains the Commission,
18 individual commissioners, or Commission staff from
19 making public statements about that matter. You have
20 been steadfast in your views on that matter. I have
21 appreciated it all along, and I appreciate it here
22 today. I am, however, disappointed. Those of you who

1 have been watching the agenda now will notice that we
2 actually had -- a proposed rule was on the agenda, but
3 it is not on the agenda, that would essentially codify
4 that practice. I am disappointed that we are not
5 ready to go to a proposed rule on that today.

6 Ensuring the transparency and accountability of the
7 Commission's operations and enforcement actions should
8 be a high priority for this Commission. It certainly
9 is a priority for me.

10 During my tenure as a commissioner, I will
11 never agree, I will never agree, to any gag clause
12 with any party settling an enforcement matter with the
13 Commission. I will continue to exercise my right to
14 speak on all matters before the Commission, a right
15 that was recently affirmed by the United States Court
16 of Appeals and is written in section 2(a)(10)(C) of
17 the Commodity Exchange Act. Neither a majority of the
18 Commission nor any consent order can take away that
19 right. Under no circumstance will I agree or will I
20 agree to be silenced or agree to let the Commission be
21 silenced or the staff by any person that the
22 Commission believes has violated the Commodity

1 Exchange Act.

2 Thank you, Mr. Chairman, and I look forward
3 to discussing today's rules.

4 CHAIRMAN TARBERT: Thank you very much.

5 For each of the items on today's agenda, the
6 staff will make presentations to the Commission.
7 After each staff presentation, the floor will be open
8 for questions and comments from each commissioner.

9 Following the close of discussion on each
10 matter, the Commission will vote on the
11 recommendation. All final votes conducted in this
12 public meeting will be recorded votes. The results of
13 the votes approving the issuance of rulemaking
14 documents will be included with those documents in the
15 Federal Register.

16 To facilitate the preparation of approved
17 documents for publication in the Federal Register, I
18 now ask the Commission to grant unanimous consent for
19 staff to make necessary technical corrections prior to
20 submitting them to the Federal Register.

21 Without objection, so ordered.

22 At this time, I would like to welcome the

1 following staff for their presentations on the final
2 rules amending Part 13. From the Office of General
3 Counsel, we have our general counsel, Dan Davis; and
4 senior special counsel Herminio Castro. The floor is
5 yours. Thank you.

6 MR. DAVIS: Thank you, Mr. Chairman. And
7 thank you, commissioners, for the opportunity to
8 present on Part 13. I appreciate all of the input
9 that we have gotten from your respective offices,
10 which I think has made an excellent final rule here.

11 Without further ado, I will turn it over to
12 Herminio Castro. And I wanted to thank Herminio and
13 Dhaval Patel, who put in the effort from OGC on this
14 rule.

15 MR. CASTRO: Good morning. My name is
16 Herminio Castro, senior special counsel with the
17 Office of the General Counsel.

18 Today, staff recommends that the Commission
19 adopt the final rule to amend Part 13 of the
20 Commission's regulations. The staff also recommends
21 that the Commission adopt the summary of the
22 rulemaking process for placement on the Commission's

1 website.

2 Part 13 of the Commission's regulations was
3 originally promulgated in 1976. It has not been
4 updated since that time. It sets forth the rulemaking
5 procedures for formulation, amendment, or repeal of
6 rules that directly affect the public. The final rule
7 would eliminate the provisions in Part 13 that set
8 forth the process for issuing rulemakings. As
9 originally adopted, Part 13 was intended to track the
10 rulemaking process set forth in the Administrative
11 Procedure Act, or APA. Because the APA governs the
12 rulemaking process, it is unnecessary to maintain this
13 process in a Commission regulation.

14 Also, in its current form, Part 13 does not
15 fully conform to the APA, which may create ambiguity
16 and confusion about procedures to be followed by the
17 Commission in rulemakings. Accordingly, the final
18 rule eliminates the provisions that set forth the
19 process for promulgating rulemakings. Part 13, as
20 amended, would, however, retain regulation 13.2,
21 renumbered as 13.1, which describes the process for
22 filing a petition for rulemaking, which the APA does

1 not specifically address.

2 The proposal was published on September
3 20th, 2019. And the comment period closed on October
4 21st, 2019. We received two comments on the proposal
5 from Better Markets, Inc. and the Administrative
6 Conference of the United States, or ACUS. The ACUS
7 asked the Commission to consider conforming the final
8 rule to ACUS' recommendation on petitions for
9 rulemaking issued in 2014. Better Markets recommended
10 the Commission implement ACUS recommendations
11 concerning ex parte communications, also issued in
12 2014.

13 In light of the comments we received, we
14 modified the proposal to allow the electronic
15 submission of petitions for rulemaking. And it will
16 be the Commission's policy going forward to post the
17 petitions on the Commission's website.

18 We also note in the preamble that the
19 Commission will decide on a case-by-case basis whether
20 to solicit public comment on petitions for rulemaking.

21 With regards to ex parte communications,
22 while the APA does not prohibit ex parte

1 communications, we noted in the preamble that it is
2 the Commission's policy to make public on the
3 Commission's website substantive ex parte
4 communications, both written and oral, that provide
5 significant material information addressed to the
6 merits of the proposed rule. It is also the
7 Commission's practice to make public on its website
8 all ex parte meetings held on proposed rules,
9 including the names and affiliations of attendees.

10 Finally, the summary of the Commission's
11 rulemaking process explains in plain English the
12 Commission's process for promulgating rulemaking by
13 the Commission. It also explains the Commission's
14 policy and practice on ex parte communications.

15 I would like to thank Dhaval Patel, counsel
16 with OGC, for her assistance drafting this rule. I am
17 now happy to take questions.

18 CHAIRMAN TARBERT: Thank you very much for
19 that informative presentation.

20 To begin the Commission's discussion and
21 consideration of these rulemakings, I will now
22 entertain a motion to adopt the final rules amending

1 Part 13.

2 COMMISSIONER QUINTENZ: So moved.

3 COMMISSIONER BERKOVITZ: Second.

4 CHAIRMAN TARBERT: Thank you.

5 I would now like to open the floor for
6 commissioners to ask any questions or make comments.
7 Since I have already explained why I am supporting
8 this rule, I will turn to Commissioner Quintenz.

9 COMMISSIONER QUINTENZ: Thank you, Mr.
10 Chairman.

11 I don't have any questions. I would just
12 like to compliment you on your work. It wasn't that
13 long ago that you were here with the proposal in front
14 of us. And I know that it takes a significant amount
15 of effort to turn something around that quickly. So
16 thank you, Herminio and Dan, for your work on this. I
17 think it is an important rule for us to finish. Thank
18 you.

19 CHAIRMAN TARBERT: Thank you.

20 Commissioner Behnam?

21 COMMISSIONER BEHNAM: I will echo
22 Commissioner Quintenz's statements. Herminio, thank

1 you for your work. And Dhaval as well I know is not
2 here. Mr. General Counsel, thanks for your support.
3 I do want to especially thank the chairman and the
4 staff for working with my office to put the webpage
5 up, which I think in the spirit of transparency is
6 going to be a really nice step for the public to
7 understand. In the absence of this more prescriptive
8 language, which I know is outdated, the webpage will
9 be a sort of user-friendly tool for the public to
10 understand the rulemaking process within this agency.

11 So thank you again for your work. And I
12 look forward to seeing the website.

13 CHAIRMAN TARBERT: Thank you.

14 Commissioner Stump?

15 COMMISSIONER STUMP: I have no questions.
16 Thank you all.

17 CHAIRMAN TARBERT: Commissioner Berkovitz?

18 COMMISSIONER BERKOVITZ: Thank you, Mr.
19 Chairman. Thank you, Herminio and Dhaval. I
20 appreciate your working with my office on this rule
21 and working to address the comments. I just want to
22 discuss one of the comments we received from Better

1 Markets regarding ex parte communications. Although
2 that is not part of the rule, my understanding and my
3 reading of the preamble is we are reaffirming our
4 practice and policy in that respect. Can you just
5 briefly summarize that policy and practice on ex parte
6 communications that we are reaffirming?

7 MR. CASTRO: Yes. Again, the Commission's
8 policy is to include all ex parte communications
9 involving oral or written communications that provide
10 significant material information. And it is the
11 Commission's policy then to place that on the record.
12 Also, it is the practice of the Commission to post ex
13 parte communications meetings on proposed rules. So
14 we are going to place those also on the Commission's
15 website.

16 COMMISSIONER BERKOVITZ: So if there is a
17 meeting or any other type of communication where new
18 information is provided, that new information would be
19 put on the comment part of the website?

20 MR. CASTRO: Yes as long as that information
21 pertains to the proposed rulemaking and provides
22 significant and material information.

1 COMMISSIONER BERKOVITZ: And this will be
2 explained as part of that posting on the website about
3 our rulemaking --

4 MR. CASTRO: Correct. We added that
5 particular -- policy and practice, we added that to
6 the rulemaking explanation.

7 COMMISSIONER BERKOVITZ: Okay. Again I
8 thank you very much. I think this is part of the
9 transparency that the chairman has been referring to
10 and supporting. So I appreciate your responsiveness
11 and your clarity in which we are making public these
12 policies and practices. Thank you again very much.

13 CHAIRMAN TARBERT: Thank you, Commissioner
14 Berkovitz.

15 Well, if there are no other questions or
16 comments, are my fellow commissioners prepared to
17 vote? Okay. It appears so. So, Mr. Kirkpatrick,
18 will you please call the roll?

19 MR. KIRKPATRICK: Thank you, Mr. Chairman.

20 The motion now before the Commission is on
21 the adoption of the final rule amending Part 13 of the
22 Commission's regulations. Commissioner Berkovitz?

1 COMMISSIONER BERKOVITZ: Aye.

2 MR. KIRKPATRICK: Commissioner Berkovitz
3 votes aye.

4 Commissioner Stump?

5 COMMISSIONER STUMP: Aye.

6 MR. KIRKPATRICK: Commissioner Stump votes
7 aye.

8 Commissioner Behnam?

9 COMMISSIONER BEHNAM: Aye.

10 MR. KIRKPATRICK: Commissioner Behnam votes
11 aye.

12 Commissioner Quintenz?

13 COMMISSIONER QUINTENZ: Aye.

14 MR. KIRKPATRICK: Commissioner Quintenz
15 votes aye.

16 Chairman Tarbert?

17 CHAIRMAN TARBERT: Aye.

18 MR. KIRKPATRICK: Chairman Tarbert votes
19 aye.

20 Mr. Chairman, on this matter, the ayes have
21 five, the noes have zero.

22 CHAIRMAN TARBERT: Thank you very much, Mr.

1 Secretary. The ayes have it, and the motion to adopt
2 the final rule is hereby approved. Okay. Thank you
3 very much.

4 At this time, I would like to invite a
5 second presentation on a proposal that would reopen
6 the comment period and request additional comment on
7 the Commission's proposed capital requirements for
8 swap dealers and major swap participants.
9 Specifically, we have DSIO Director Josh Sterling,
10 Deputy Director Tom Smith, Associate Director Josh
11 Beale, Special Counsel Jennifer Bauer, and Senior
12 Financial Risk Analyst Rafael Martinez. From the
13 Office of General Counsel, we have Associate General
14 Counsel Paul Schlichting.

15 I will go ahead and give the floor open to
16 you, Josh. Thank you.

17 MR. STERLING: Good morning, Mr. Chairman.
18 And, commissioners, good morning to you as well.
19 Again it is a pleasure to be before you with
20 representatives of my world-class staff to talk to you
21 about a very important step in our regulation of swap
22 dealers. We are putting before you and recommending

1 that you vote for reopening the comment period on our
2 2016 capital proposal. Just a few quick highlights on
3 that.

4 Capital is the last substantive rule we
5 would adopt with respect to swap dealers before our
6 swap dealer rule set is complete, the effect of which
7 is that swap dealers would transition from being
8 considered provisionally registered with us and
9 provisional members of the National Futures
10 Association to having a full registration. So in some
11 respects, this will be when it is finally brought
12 forward to a final rule a capstone event and a
13 regulation of swap dealers under Dodd-Frank. And I
14 think the Commission as a whole can take great pride
15 in moving forward in that regard.

16 I would say that we are reopening the
17 comment period because we think it is appropriate to
18 take notice of events that have transpired since the
19 2016 proposal went out for consideration by the
20 public.

21 First of all, we received a number of
22 important public comments. It gave us an opportunity

1 to think about our approach.

2 We also said at the time that we anticipated
3 the SEC would move forward and ultimately adopt their
4 capital rules for security-based swap dealers. And,
5 indeed, they have. We think that, inasmuch as section
6 4s(E) of the Commodity Exchange Act requires
7 essentially collaboration amongst financial regulators
8 in getting the final rules, we should take fair notice
9 of what the SEC has done and consider those
10 developments in light of what is appropriate for our
11 registrants and our markets.

12 The last thing I would say, by way of a
13 highlight, is that we are affording a 75-day
14 opportunity to comment on the release. Now, we have
15 asked for comments in 16, 17, or so specific areas.
16 The entire 2016 proposal is, of course, open for
17 comment by interested members of the public. We look
18 forward to having their comments. So we feel like a
19 75-day period to effectively comment again on the 2016
20 proposal was a very measured and thoughtful way for us
21 to get good feedback to come to you soon thereafter
22 with a recommendation on what a final rule set for

1 capital would look like.

2 Now, before I hand it over to the team, I
3 just want to thank them all for their hard work. We,
4 of course, have Tom Smith, Josh Beale, Jennifer Bauer,
5 and Rafael Martinez before us today. I would also
6 like to thank the General Counsel's Office, Dan Davis,
7 Paul Schlichting, and Carlene Kim, in particular.
8 And, of course, the Chief Economist's Office was quite
9 helpful as well. Bruce Tuckman worked closely with us
10 as Lihong McPhail. And I think, in particular, Matt
11 Daigler in your office, Mr. Chairman, should be
12 thanked for his involvement and input as well. It was
13 indeed vital.

14 So, with that, I will turn it over to Tom or
15 Josh.

16 MR. BEALE: Thank you, Josh.

17 Mr. Chairman, commissioners, staff requests
18 Commission approval to publish in the Federal Register
19 a notice to reopen the comment period of the 2016 swap
20 dealer capital proposal for 75 days. Consistent with
21 the statutory requirements in the Dodd-Frank Act,
22 division staff provided each of the Prudential

1 Regulators and the SEC an opportunity to review and
2 comment on the proposed notice to reopen the comment
3 period. The 2016 proposal would implement provisions
4 of section 731 of the Dodd-Frank Act that direct the
5 Commission to adopt regulations imposing capital
6 requirements and financial condition reporting on swap
7 dealers and major swap participants.

8 The Dodd-Frank Act applies a bifurcated
9 approach that requires each swap dealer and major swap
10 participant for which there is a Prudential Regulator
11 to meet the capital requirements established by the
12 applicable Prudential Regulator, each swap dealer and
13 major swap participant for which there is no
14 Prudential Regulator, including nonbank subsidiaries
15 of bank holding companies, to meet the capital
16 requirements adopted by the Commission.

17 To date, there are 107 provisionally
18 registered swap dealers with the Commission. Of those
19 107, 54 are subject to the capital and margin rules of
20 the Commission while the remaining 53 are subject to
21 the rules of a Prudential Regulator.

22 The 54 provisionally registered swap dealers

1 for which the Commission is primarily responsible for
2 establishing their capital requirements represent a
3 diverse set of swap dealer registrants. Based on our
4 analysis, four of these firms are large alternative
5 net capital broker-dealers already duly registered
6 with the SEC. Twenty-two represent foreign domiciled
7 entities, likely subject to existing comparable
8 capital requirements of a foreign regulator while
9 several of the remaining are nonbank subsidiaries of
10 existing bank holding companies or standalone
11 commercial entities or subsidiaries thereof. For
12 these reasons, the 2016 proposal was flexible in its
13 design and permitted compliance with the Commission's
14 minimum capital requirements by leveraging off of
15 already existing capital regimes.

16 That proposal offered swap dealer
17 registrants a choice of one of three methods to
18 calculate their capital under the Commission rules:
19 the first, a Basel-based method which incorporated by
20 reference certain capital adequacy rules of the
21 Federal Reserve Board as if that swap dealer itself
22 was a bank holding company; the second, a net liquid

1 assets method, which incorporated by reference the
2 SEC's proposed and now finalized rules applicable to
3 security-based swap dealers and is based off the
4 capital requirements traditionally imposed on futures
5 commission merchants and broker-dealers; and, third, a
6 tangible net worth method designed for swap dealers or
7 major swap participants that are predominantly engaged
8 in nonfinancial activities.

9 The 2016 proposal also included a capital
10 comparability determination process wherein foreign
11 domiciled swap dealers could apply to the Commission
12 to utilize a capital regime of a foreign regulator
13 subject to certain conditions. For those swap dealers
14 duly registered as futures commission merchants, the
15 2016 proposal required these registrants to comply
16 with existing FCM net capital rules. And several
17 amendments to those rules were proposed to better
18 reflect swap activities.

19 Finally, the 2016 proposal also included
20 reporting, recordkeeping, and notification
21 requirements. These requirements are comparable to
22 already existing reporting, recordkeeping, and

1 notification requirements for futures commission
2 merchants and, to the extent practicable, with the
3 SEC's requirements for security-based swap dealers.

4 I am now going to turn the presentation over
5 to Jennifer Bauer to discuss the specific components
6 of the 2016 proposal, which have been incorporated
7 into the reopening document before you today.

8 MS. BAUER: Thank you, Josh.

9 Following the 2016 proposal, Commission
10 staff analyzed the substantive comments and met with
11 commenters. Staff also met several times with SEC
12 staff in the finalization of their capital rules as
13 well as consulted the Prudential Regulators for
14 comment.

15 The matters this notice specifically
16 highlights for further comment are a result of these
17 efforts as well as consideration of the SEC's final
18 capital rules for security-based swap dealers. This
19 notice of reopening addresses the 8 percent minimum
20 capital floor calibration. Commenters noted concerns
21 with the 8 percent risk margin calculation, with
22 several suggesting the Commission consider lowering

1 the percentage. One commenter suggested that the 8
2 percent calculation was appropriate and necessary in
3 light of permitting the use of models to calculate
4 market and credit risk capital charges. Some
5 commenters also suggested that the calculation should
6 only be applied to a lesser subset of the derivatives
7 positions of the swap dealer.

8 This notice for reopening contains several
9 questions to obtain additional information for the
10 Commission to consider with respect to this aspect of
11 the risk margin calculation, including how the 2016
12 proposal calculation would be quantified under swap
13 dealers electing each approach. Specifically, the
14 notice requests commenters, wherever possible, to also
15 provide data for the Commission's consideration.

16 This notice of reopening addresses how the
17 2016 proposal impacts FCMs, including and adopting
18 standardized market charges for swaps. Commenters
19 raised concerns with the 2016 proposal's impact on
20 FCMs specific to the addition of proprietary cleared
21 swaps to the FCM net capital floor given the
22 proprietary cleared swaps' positions are subject to

1 existing FCM net capital charges. The notice requests
2 further comment on not adopting the proposed additions
3 to the risk margin floor for standalone FCMs. Also,
4 the notice requests further comment on the proposal's
5 addition of FCM standardized market risk charges for
6 swaps, which are incorporated by reference in the
7 standardized swap dealer market risk charges. This
8 notice asks for comment on technical changes to the
9 2016 proposal grid for credit default swap market risk
10 charges and on a change to the standardized market
11 risk charge for uncleared interest rate swaps, from a
12 half percent to one-eighth of 1 percent in order to
13 maintain alignment to the standardized charges with
14 the SEC.

15 Further, the notice requests comments
16 regarding the inclusion of some types of offsetting
17 for the standardized market charges applicable to
18 commodity and currency or other swaps where there is
19 existing offsetting permitted in the application of
20 net capital charges on the underlying instruments,
21 also as aligned with the SEC.

22 This notice of reopening addresses the

1 composition of capital. Based on suggestions of
2 commenters, this notice asks additional questions
3 regarding potentially modifying the bank-based
4 approach, including the advisability of adding more
5 layers than only common equity tier 1 capital to the
6 calculation; for example, to permit the consideration
7 of qualifying subordinated debt to count as capital.
8 This notice also addresses the suggestions of other
9 commenters that asked whether the tangible net worth
10 approach should be adjusted to consider swap dealers
11 organized under a parent organization that is
12 predominantly engaged in nonfinancial activities.
13 Accordingly, this notice asks additional questions
14 concerning the qualifications necessary for the use of
15 the tangible net worth approach.

16 This notice of reopening addresses model
17 approval. Many commenters, anticipating a model
18 approval backlog, raised issues concerning the
19 logistics of model approval in the 2016 proposal and
20 emphasized the importance of being able to use models
21 to compute market and credit risk net capital charges
22 on swaps. The notice asks additional questions on

1 possible revisions to the model approval process,
2 including specifically highlighting and asking for
3 additional comment on one commenter's suggestion for
4 revised rule text.

5 The notice of reopening addresses liquidity
6 requirements. The 2016 proposal provides swap dealers
7 electing the bank-based capital approach also comply
8 with liquidity requirement based on high-quality
9 liquid assets as if the bank holding company liquidity
10 coverage ratio were applicable specific to the swap
11 dealer entity. A separate liquidity requirement was
12 proposed for swap dealers using the net liquid assets
13 capital approach based on monthly liquidity stress
14 tests. When the SEC finalized its capital rules, it
15 declined to finalize its proposed liquidity
16 requirements. Commenters suggested with regards to
17 the liquidity requirements that any swap dealer be
18 able to elect either method of a liquidity
19 requirement, regardless of the chosen capital approach
20 employed. So the notice contains further questions in
21 light of those comments and in light of the SEC's
22 deferral of adopting liquidity requirements.

1 Finally, this notice of reopening addresses
2 financial reporting for swap dealers. Several
3 commenters asked that the Commission consider changes
4 to specific aspects of the financial reporting and
5 notification rules contained in the 2016 proposal.
6 The notice, therefore, asks questions regarding those
7 specific requests, including expanding the use of
8 international financial reporting standards, extending
9 the time period of routine financial reports, and the
10 advisability of changes to certain public disclosure
11 requirements. So the notice asks questions regarding
12 these technical amendments to the financial statement
13 rules to ensure harmonization in financial reporting.

14 That concludes our presentation of this
15 notice of reopening. Thank you. And we would be
16 happy to answer your questions.

17 CHAIRMAN TARBERT: Thank you very much for
18 that presentation, very informative.

19 At this point, I will entertain a motion to
20 approve the division's proposal for the notice of
21 reopening and request for comment related to the
22 capital requirements for swap dealers.

1 COMMISSIONER QUINTENZ: So moved.

2 COMMISSIONER BEHNAM: Second.

3 CHAIRMAN TARBERT: Thank you.

4 I would now like to open up the floor for
5 commissioners to ask questions and make comments.
6 This time, why don't we start with you, Commissioner
7 Berkovitz.

8 COMMISSIONER BERKOVITZ: Thank you, Mr.
9 Chairman.

10 First of all, this is a very complex rule,
11 as evidenced by highly qualified and numerous staff at
12 the table. I want to thank the staff again for their
13 interactions with my office in responsiveness to a
14 number of our comments in a very short period of time,
15 very responsive in our discussions. I want to say at
16 the outset that I do appreciate that.

17 I have some fundamental concerns with the
18 proposal, nonetheless, in the simply insufficient time
19 that we had with this proposal to become comfortable
20 with. And one of the things, Josh, I think you said
21 is that you intend this to be the basis for a final
22 rule, this document?

1 MR. STERLING: Mr. Commissioner, thank you
2 for your question. The short answer is yes. The
3 slightly longer answer is this proposal and the
4 comments from it will inform the 2016 proposal. So it
5 is, rather, on a continuum.

6 COMMISSIONER BERKOVITZ: Okay. So the 2016
7 proposal actually made a specific proposal in terms of
8 rule, text, and what the various capital requirements
9 should be and the alternative methods of calculation,
10 correct?

11 MR. STERLING: Yes, sir, that is right.

12 COMMISSIONER BERKOVITZ: And we got a large
13 number of comments negative towards those specific
14 proposals of 2016.

15 MR. STERLING: We received a number of
16 informative comments. I don't think that they all
17 agreed with the approach we initially articulated.

18 COMMISSIONER BERKOVITZ: And I think,
19 Jennifer, you stated that one of the things that is
20 done here in this document suggests some alternative
21 approaches; for example, the SEC's approach and other
22 potential suggestions, and asks for comments on those

1 other potential approaches or modifications.

2 MS. BAUER: Thanks, Rafael.

3 The structure of the 2016 proposal has not
4 changed. And we received what I would view as
5 comments informing aspects of that. And what we are
6 reopening is the same proposal with further
7 information provided by commenters, commenters to
8 alert other commenters to the universe of comments.
9 We have tried to summarize some of their thoughts here
10 where appropriate. And we think that in the few
11 places rule text was suggested, we have put that in to
12 alert the whole universe of commenters as to what
13 those potentially could be.

14 COMMISSIONER BERKOVITZ: Okay.

15 MR. SMITH: I will just add something,
16 Commissioner. In the 2016 proposal, yes, there was
17 specific rule text and language as to what the
18 Commission was looking for with a capital rule. But
19 it also requested specific comment on such things as
20 the 8 percent and the common equity tier 1 capital.
21 Questions were asked, "Was it too high? Was it too
22 low? How should it be adjusted? Should there be

1 changes to the products that are included in that?"

2 So those are the types of things that the
3 commenters did provide feedback on during the comment
4 process, which we are highlighting here now to say
5 what would be beneficial to the Commission in going
6 final is if we could quantify some of these
7 differences, to come up with an appropriately
8 calibrated approach to the capital.

9 COMMISSIONER BERKOVITZ: Okay. I appreciate
10 that. And that is actually consistent with the
11 example that I am going to use here. I will just read
12 from the proposal that we are going to be voting on.
13 It is consistent, Tom, with what you just stated.
14 This is one of -- and it depends on what you count as
15 a question. I counted when I went through the
16 document 140 questions. So there are a lot of
17 questions, and there are a lot of alternatives. They
18 go one way on this, and they go one way on that. If
19 it were just binary, it was just, "Yes" or "No," of
20 the 140 questions, you could have, what, 200-140 of
21 potential rules coming out of this document, a lot.
22 There's a lot of ways to go on this.

1 But let me read you on this 8 percent
2 question here some of the questions or statements.
3 The Commission requests comment on whether the
4 proposed 8 percent risk margin amount should be
5 modified for SDs electing the bank-based capital
6 approach, the net liquid assets capital approach, or
7 the targeted net work capital approach to a lower
8 percentage requirement, such as 4 percent. So we are
9 asking about 4 percent in addition to about 8 percent.
10 If so, is 4 percent risk margin properly calibrated to
11 the inherent risk of SD and activities that it engages
12 in? If not, 4 percent, what percentage of the risk
13 margin should the Commission consider? Okay?

14 And then it goes on. 1(c), the Commission
15 requests comment on whether the proposed 8 percent
16 risk margin amount should be modified to be harmonized
17 with the approach adopted by the SEC for SBSDs in the
18 SEC final capital rule. Specifically, should the
19 Commission modify the regulation to lower the risk
20 margin amount percentage from 8 percent to 2 percent?
21 So we are asking 8 percent, 4 percent, 2 percent,
22 right?

1 MR. STERLING: Yes.

2 COMMISSIONER BERKOVITZ: So there is no data
3 in this rule. Let me ask this question. We are
4 asking if you think, the commenters, we are asking if
5 you think, it should be 4 percent, tell us why and
6 give us data. Correct?

7 MR. STERLING: Yes, sir.

8 COMMISSIONER BERKOVITZ: If it should be 2
9 percent, tell us why, and give us data?

10 MR. STERLING: Yes.

11 COMMISSIONER BERKOVITZ: Okay. But we do
12 not have the data right now. And we are not proposing
13 data. We are asking for it, whether to go with 4
14 percent or 2 percent. Is that correct?

15 MR. STERLING: That is correct, Mr.
16 Commissioner, in a sense that we are asking members of
17 the public to provide us with information sufficient
18 for us to consider those possibilities and recommend a
19 choice that would be good. In fairness, I believe
20 that a lot of the information that would be required
21 to be provided to articulate what they believe an
22 acceptable standard would be, there are significant

1 privacy interests in the retention of that
2 information. And so we are trying to design a process
3 where we can have conversations about that, receive
4 information about that, information from the public,
5 by giving them specific choices to look at within a
6 range from 2 to 8 percent.

7 COMMISSIONER BERKOVITZ: Sure. But we do
8 not have the information currently now to propose a 4
9 percent or a 2 percent. That is the whole purpose of
10 this. We want to comment to be able to potentially
11 depending on what the data shows us -- we will look at
12 it. Some people will say, "We like 8 percent." Some
13 people will say, "4 percent." Some people will say,
14 "2 percent." Some people will say, "0 percent." Some
15 people will say, "Go with the Prudential Regulators at
16 their numbers, at 6 and a half percent, or whatever."
17 So there is a whole range of possibilities. There is
18 a whole range of data that might come on. And our job
19 as a commission is to choose which one of those based
20 on the data that we don't have. And then we would
21 decide. You come to us with a recommendation,
22 correct? If we had it, why aren't we making the

1 decision, you coming to us now, instead of asking them
2 for it?

3 MR. STERLING: Right. Well, Mr.
4 Commissioner, I take the point. I believe that -- I
5 mean, we could be here today coming to you with a
6 final rule set for the Commission to consider for
7 action, wherein we would have made a choice that we
8 thought was right and then we could deal with it
9 substantively going forward, but the decision would
10 have been procedurally found. We thought the better
11 approach would be to ask the public, "Well, what do
12 you think based on the information you have got?"

13 And I think that going between 2 and 8
14 percent is an exercise that the SEC recently
15 experienced. We think that asking within that range
16 will get us a lot of valid input from the public. But
17 you are fundamentally correct, sir. We do need to
18 ask. So we are.

19 COMMISSIONER BERKOVITZ: Okay. And I also
20 want to make it clear that I support and I have always
21 supported and I continue to support data-based
22 rulemaking. I think it is good that we are asking for

1 data. If the commenters don't like 8 percent, I think
2 it is the proper approach to say, "If you don't like 8
3 percent, tell us why you want 4 percent" or if people
4 say, "You should harmonize with the SEC," back it up
5 with data and arguments, not just the argument,
6 "Harmonization for harmonization's sake." But is it
7 substantively correct?

8 So we need the data to adopt an alternative.
9 We are not proposing an alternative. We are thinking
10 about alternatives. And we want data to be able to
11 justify a final rule, which we don't have yet. There
12 is nothing out there that the public can comment on as
13 to going to 4 percent. There is no notice and comment
14 on a proposal for 4 percent. There is no data to
15 justify it that we are putting out.

16 MR. STERLING: Sir, we are not putting
17 forward 4 percent. We are suggesting and asking
18 questions, as you have read into the record, sir, to
19 ask what the right amount would be supported by data.
20 I think that the 2016 proposal if I have it right --
21 please correct me, team, if I am wrong -- put out a
22 percentage for risk margin and now are asking whether

1 we got that right. So I think when we get to a final
2 rule recommendation for you, we will have a percentage
3 that is backed up by data in our assessment of it.
4 And I don't think that whatever number we were to
5 decide between a range of 2 and 8 percent, let's say,
6 will leave the public somehow guessing or not knowing
7 our thoughts or our intentions. I think we are being
8 quite deliberate about that.

9 COMMISSIONER BERKOVITZ: Oh, exactly.

10 Jennifer, did you want to add?

11 MS. BAUER: I just want to clarify one thing
12 because you had spoken about the 6 and a half percent.
13 That is not a risk margin. That is a separate bank-
14 based approach off of risk-weighted assets. That is
15 not changing. The floor of risk margin percentage was
16 something that we proposed in the 2016 proposal
17 applicable across the board. And we received a lot of
18 comments about the floor, but we aren't proposing
19 changing the concept. Really, the questions for
20 additional comment are about calibrating the
21 percentage. The SEC's final rule discussed the
22 iterative process of getting this right is sort of you

1 need data and to implement. And over time, you will
2 focus in on the exact right percentage. And we ask
3 questions about whether we should follow what the SEC
4 did. They also proposed 8 percent and adopted a final
5 rule, asked questions then in a reopening, and then
6 adopted a final rule that has a 2 percent with a
7 possibility of ratcheting up to 4 and 8 over time.

8 Similar to what you said about the no-action
9 process, trying to get things right but also get to
10 implementation, I think the questions we are asking
11 about the 8 percent risk margin amount are an attempt
12 to ask the public to give us this data as much as
13 possible, but it may be in the final rulemaking that
14 it is something that may take iterations for this
15 Commission to get right. I don't think anyone has any
16 intention of doing anything other than getting as much
17 information as possible from the public about this
18 amount.

19 However, the approach is how to count
20 capital, what qualifies as capital, the ability to use
21 these, depending on the type of swap dealer being able
22 to use these, different flexible approaches that are

1 consistent with the SEC, are consistent with the
2 Prudential Regulators.

3 All of that rule text is in the 2016
4 proposal and is not changing. And we are not
5 proposing to change it. On these things that
6 commenters have raised, we want to make it public to
7 the other commenters. What are the things that are
8 the main concerns? What are the things that could be
9 tweaked? Give us more information about that. And
10 where it was an actual change to rule text, we
11 included that. But it is very minimal in
12 consideration of the entire package of rule text from
13 the 2016 proposal.

14 COMMISSIONER BERKOVITZ: And I appreciate
15 that. Let me just get to the heart of my concern. If
16 we are asking commenters for reasons to support an
17 alternative approach to what we propose and that
18 approach that they suggest provides us with new
19 important data that would justify a different approach
20 from the original proposal and we are relying on that
21 information from the commenters to go a different way,
22 that we can't just go to final, that that information

1 has to be put out we have to re-propose. That is the
2 thrust of where I am getting at with this, that in the
3 APA notice-and-comment rulemaking, the commenters have
4 to have an opportunity to comment on critical data
5 relied on by the agency, important data relied on by
6 the agency. If we want to get different data to
7 support a different rule or the data the Commission
8 concludes it wanted to go in a different direction,
9 then that is fine.

10 It should be data-driven. But we can't ask
11 the commenters, say, "Well, what rule do you like?
12 Give us the data" and then pick the best rule and data
13 from what the commenters provide us. We have to
14 subject that different approach if we are going to
15 deviate from 8 percent and go to 4 percent or 2
16 percent. And we are asking for data to justify it.
17 And we get that data and say, "We believe we should go
18 in this different direction."

19 That has to be subject to public comment.
20 There is a whole bunch of case law on that. We can
21 talk to the lawyers about it. But that is I believe
22 the law.

1 So that is my point. If we are going to get
2 the significant new data, it is a big data call in
3 this thing that this does not support going to a final
4 right away. We have to re-propose.

5 MR. STERLING: Thank you, Mr. Commissioner.
6 We understand the point and take due note of it.
7 Thank you.

8 CHAIRMAN TARBERT: Good. Okay. Are you all
9 right?

10 COMMISSIONER BERKOVITZ: Well, I have --

11 CHAIRMAN TARBERT: Do you want to do one
12 more?

13 COMMISSIONER BERKOVITZ: The other point
14 that I would raise is more in the substance. And it
15 is in my written statement, but I have used up a lot
16 of time on the process. But I would emphasize what I
17 have said before. Harmonization for harmonization's
18 sake is not a sufficient reason to do something. Just
19 because the SEC has gone to a certain level doesn't
20 mean we should do it just because they have done it.
21 It has to be independently supported.

22 I am also concerned that every place in this

1 thing, in this re-proposal, the tendency is
2 encouraging sort of a backing off from where we were
3 in 2018. So I have that overall concern, and I have
4 that procedural concern.

5 So thank you, Mr. Chairman.

6 CHAIRMAN TARBERT: Thank you, Commissioner
7 Berkovitz.

8 Commissioner Stump?

9 COMMISSIONER STUMP: Thank you, Mr.
10 Chairman. And thanks to the team and the Office of
11 the General Counsel and the Office of the Chief
12 Economist. You all have spent considerable time with
13 us working on this, and I really appreciate it. Just
14 based upon the number of questions my team had, I can
15 only imagine how many meetings you had to have to help
16 us better understand this very complex rule.

17 Relative to reopening the comment period and
18 asking additional questions, I am extremely
19 supportive. Building upon something Commissioner
20 Berkovitz said, I do so with an open mind. I am not
21 pre-assuming what the outcome is going to be. I, in
22 fact, had a question about offering these different

1 options but preserving the ability to consider them as
2 a non-exhaustive list of just that: options. The
3 questions that are very specific with these specific
4 numbers may, in fact, not be where we land.

5 Whether or not that requires us to
6 re-propose or go to final is actually not the question
7 we should be asking. The bottom line is, it is time
8 to get this right. If we have to re-propose it, we
9 have to re-propose it.

10 Any information -- and I applaud you all for
11 asking for data-driven information -- is going to help
12 us get this rule to the place it needs to be. But the
13 reality is that the reason it has taken us so long to
14 do this rule is because it is extremely complicated.
15 And the market participants that this agency deals
16 with in this context are quite diverse. Some of the
17 other regulators didn't have that type of diversity
18 when they attempted to finalize these rules.

19 So it is complicated. It has taken us a
20 while. It is time to finish it, but we have to finish
21 it correctly.

22 So I thank you all for all of your time and

1 energy and the many hours you spent just with my team
2 alone. So thank you. I am very supportive of
3 reopening the comment period, hearing from the public,
4 and getting this right.

5 CHAIRMAN TARBERT: Thank you very much.

6 Commissioner Behnam?

7 COMMISSIONER BEHNAM: Thank you, Mr.
8 Chairman. Thank you to all the staff. I appreciate
9 your time in doing all of this hard work with your
10 discussions with me in the past few weeks and my
11 staff.

12 A few questions I had are similar to
13 Commissioner Berkovitz's. So I will try to work
14 around them and avoid duplicative question-and-answer
15 scenarios.

16 So I will try to get a few things about the
17 core of the rule itself and then a little bit about
18 some of the additional questions, which in my mind
19 stray a little bit from the original '16 proposal.

20 And then, Mr. Chairman, after I conclude
21 hopefully a quick Q&A session, I will read my
22 statement as well.

1 Josh Beale, you mentioned the three
2 methodologies. And I believe we talked about this,
3 but I think it is good for the public to understand
4 and also for us to just maybe unpack a few more
5 things. We have the Basel method, FCM BD method, and
6 the tangible net worth method. And something that, as
7 I read the document, what I thought about was, are we
8 trying to get to the same place using three different
9 methods? And I know clearly with a tangible net worth
10 method, as you pointed out, it is specifically focused
11 on commercial end-users because of the type of
12 businesses they run, the organizational setup, and the
13 physical assets they have as compared to a traditional
14 banking organization.

15 But, just as a broad matter, using these
16 three different methods depending on what the entity
17 chooses, what methodology they choose, from a
18 regulatory standpoint, are you trying to get, are we
19 trying to get to the same place on the back end or do
20 the three methods sort of serve different purposes
21 that will allow us to assess risk individually and in
22 more of a bespoke manner, based on the organization?

1 MR. BEALE: My personal view is that each of
2 the methods requires capital at the end of the day.
3 How you get there is obviously very different. So in
4 my mind, it is better to have something than nothing.
5 But we acknowledged in the 2016 release that we needed
6 diversity because of the large number of diverse
7 registrants that we had. And we knew that several of
8 them were already maybe subject to a capital rule or
9 by the effect of their parent organizations. So each
10 of the methodologies will likely result in different
11 conclusions as to what their specific quantitative
12 capital will be. But I think, as a whole, all of that
13 is intended on achieving the regulatory purpose behind
14 capital, which is to have something there at the end
15 of the day for wind-down of operations and cover
16 holistically entry-level risk at the organization.

17 COMMISSIONER BEHNAM: Great. Thanks.

18 Jennifer, you discussed -- I believe it was
19 you -- briefly about internal modeling. That was a
20 question and a comment that had come up, and it has
21 been an issue I know from a policy perspective for a
22 number of years. And I think the commenters focused

1 on the challenge of getting model approvals from the
2 regulators. Can we talk a little bit about maybe what
3 the process is in terms of model when an entity
4 chooses a specific type of model methodology and then
5 what the relationship is and what the conversations
6 are with the regulator? And given the sort of vast
7 pool of regulators that some of these organizations
8 have to deal with -- they have different methodologies
9 for Prudential Regulators versus different market
10 regulators and how this sort of all comes together.

11 MS. BAUER: Sure. And I may include Rafael
12 here.

13 COMMISSIONER BEHNAM: Sure.

14 MS. BAUER: But, to start, the proposal, the
15 2016 proposal, provides that the swap dealers can
16 apply for approval to use models to calculate market
17 risk and credit risk charges. And those would VAR
18 models. And we included a very substantial amount of
19 qualitative and quantitative requirements for those
20 models. So the models that they submit have to meet
21 those qualitative and quantitative requirements. And
22 then they would be verified to meeting those by the

1 NFA. And then once that process is completed, they
2 would be approved to use those models.

3 So the concerns of commenters were, "That is
4 going to be quite a process. It is going to take some
5 time." In the meanwhile, if they had to use
6 standardized charges, that may be a competitive
7 disadvantage because those were perceived to be a much
8 higher and onerous capital charge. So that is
9 essentially what we are -- the submitted language that
10 was asked for by a commenter was to attempt to
11 leverage off of existing reviewed, approved models
12 from other regulators so that NFA wouldn't have those
13 also in the pipeline to approve.

14 If it is a Basel-based model, it has been
15 approved by a Basel-type regulator or the SEC. That
16 would be considered to be good for the purposes of
17 starting to use those same model processes.

18 And the qualitative and quantitative
19 requirements that govern these models that we have
20 imported are very consistent with those same types of
21 reviews of other regulators. So that I think was the
22 reason for that suggestion to the Commission to

1 consider.

2 And I will let Rafael talk about what he
3 thinks the model approval process for NFA would
4 actually consist of.

5 MR. MARTINEZ: Thank you, Commissioner
6 Behnam.

7 So, first, I want to just mention in
8 response to a prior question you had about the
9 objective of the rule, are we trying to get to the
10 same place, and we definitely are. We are trying to
11 get to the safety and soundness of these swap dealers
12 ultimately.

13 There are the three alternative methods.
14 And they are structured differently. So there is the
15 banking approach, the broker-dealer FCM approach, and
16 the tangible net worth. And they are structured
17 differently, but whenever they use models, the models
18 are used only to try to estimate the risk of the
19 portfolio over all the market risk and then the risk
20 of the specific relationship with a counterparty, and
21 that is a credit risk. And in all cases, they are
22 using at the moment the same underlying model, which

1 is the Basel-based model. That may change. It has
2 been changing for I think forever. They are just
3 always changing. There were changes after the crisis,
4 and there are some that have not been fully adopted.
5 But do we intend to use those same models?

6 So there is really just one style of model,
7 which is the one that these globally followed and
8 established by Basel. And I think there are over 90
9 countries that are represented in Basel. So it is
10 really the global standard. That is what we plan to
11 use.

12 One disadvantage of this is that there might
13 be calibrations of the specific parameters that had
14 been made by the people that participate in Basel,
15 which are generally the central banks of countries
16 that might put more emphasis and more detail in
17 certain parts of the financial world that may not be
18 exactly the ones that our dealers follow. So there
19 might be a need for recalibration of some parameters
20 possibly. We will have to learn with experience. By
21 the way, that is a way I think about the -- whether 8,
22 6, or 4, there is no change of structure, no change of

1 the proposal. It is a question of recalibrating some
2 parameters. And I think that that just is
3 appropriate.

4 Then, finally, the advantage of having these
5 Basel models is that there is generally -- we have a
6 lot more people looking at how they perform. We can
7 get informed by the global experience. It is very
8 difficult to find people that can do the examinations
9 and the approvals and the governance of these models
10 and the examination and all of this of these models.
11 So following the global standard allows us to tap into
12 a pool of experts and specialists that we don't need
13 to have somebody who knows the CFTC way, but, you
14 know, it follows that process. It is more generic.

15 We do think it is going to be a big
16 challenge to do the approval and the ongoing
17 monitoring of this. We are going to be relying like
18 we have. In the case of, for example, the uncleared
19 margin, we are going to be relying heavily on the NFA.
20 And we are going to have to have a program in how we
21 work with the NFA to ensure that the oversight is
22 appropriate. And it is a challenge, and we will be

1 looking for help from the Commission in developing
2 that program.

3 MR. STERLING: Just to add briefly -- sorry,
4 Mr. Commissioner -- we are indeed actively working
5 with the National Futures Association to design that
6 very kind of process when, indeed, we do get a final
7 rule to implement.

8 COMMISSIONER BEHNAM: Thank you.

9 Two final things. And then I am going to
10 get through my statement. I associate myself with
11 Commissioner Berkovitz about the comment about
12 harmonization. I know, Director Sterling, you pointed
13 out 4s(e). And harmonization is an absolute key
14 priority for the agency and has been for decades, as
15 long as we have existed. It is good from a regulatory
16 perspective. It is good from a market participant
17 perspective. But certainly, having read the document,
18 there is a lot of mention of harmonizing with the SEC,
19 which has recently finalized some of its capital
20 rules. But I caution a full-on sort of head-first
21 approach to harmonization given the fact that we have
22 unique markets; different risk perspectives; and, of

1 course, as Commissioner Stump pointed out, a very
2 diverse participant pool.

3 I will end off on just a note. I don't even
4 need to make this a question and answer, but this is
5 really the reason that I am, unfortunately, not going
6 to be able to support the rule proposal. Yes, the
7 core of it is opening up the comment period again from
8 the 2016 rule. But there are a number of questions,
9 additional questions. And I will just point out the
10 leverage ratio question. If I am correct, that was
11 not in the 2016 or the 2011 document and also the
12 alternative compliance mechanism, which is an SEC rule
13 and is also not in our 2016 proposal.

14 I understand the thrust of the document is
15 focused on the 2016 proposal, which I think is
16 important. I applaud both the chairman and you for
17 working on this, but given the fact that we are adding
18 new questions, which are proposing new ideas, which
19 require new data and new different ways of thinking
20 about the capital rule writ large, there is too much
21 risk in my mind for going astray from what we are
22 presenting to the public, which is just at its core a

1 reopening of the comment period. So I am going to
2 stop there and read my statement, and then I will be
3 all finished up, Mr. Chair.

4 I respectfully dissent from the CFTC's
5 decision today to reopen the comment period and
6 request additional comment on proposed regulations and
7 amendments to implement section 731 of the Wall Street
8 Reform and Consumer Protection Act, which requires the
9 CFTC to establish capital rules for all registered
10 swap dealers and major swap participants that are not
11 banks, including nonbank subs of bank holding
12 companies, as well as associated financial
13 recordkeeping and reporting requirements. While I
14 would have been comfortable supporting the reopening
15 as a matter of moving this critical Dodd-Frank rule
16 forward to finalization, to the extent it introduces
17 supplementary avenues for future rulemaking, such as a
18 leverage ratio requirement, it is a deception.

19 Impulsively inviting comment on matters
20 tangential to the 2016 capital proposal, but perhaps
21 relevant to determining appropriate capital standards
22 and methodologies, as opposed to a thoughtful

1 re-proposal, sacrifices discipline for expediency, and
2 runs afoul of proper process for notice and comment.
3 I will not be complicit in supporting Commission
4 action that I believe could invite backdoor
5 rationalization when finalization is before us. The
6 public deserves and our integrity demands that we play
7 by the rules.

8 Today's action is a reopening of the comment
9 period and a request for comment, rather than a true
10 proposal. And, thus, the 2016 capital proposal
11 remains the only concrete indicator to the public of
12 the Commission's intentions. If the 2016 proposal is
13 an extreme overshoot, the appropriate way to provide
14 the public with an opportunity to comment is to issue
15 a re-proposal. Asking further questions without a
16 clear signal as to where the Commission is going, at
17 the minimum, risks further slowing this nearly 10-year
18 effort to finalize a capital rule by adding an
19 unnecessary step to the process in the form of a
20 re-proposal at some time in the future and, at worst,
21 incites the agency towards an exercise in creative
22 reasoning outside the bounds of process.

1 Too often over the last couple of years, I
2 believe this agency has slowed its own progress by
3 snaking outside clear Administrative Procedure Act
4 trajectories and adding unnecessary steps to the
5 rulemaking process. In part, I fear that we are doing
6 the same thing today. The competing threads
7 throughout the reopening make it harder for the public
8 to discern what the Commission is proposing to do and
9 will make it more difficult to effectively comment on
10 the existing proposal from 2016. This creates undue
11 risk under the APA and, arguably, poisons the well in
12 regard to the reachable goals of this new request for
13 comment.

14 To reiterate sentiments made in my first
15 speech as a CFTC commissioner, capital is a
16 cornerstone financial crisis reform that is critical
17 to protecting our financial institutions and the
18 financial system as a whole, specifically from
19 systemic risk and contagion but also from unintended
20 consequences if capital and margin levels are applied
21 and set without due regard to the uniqueness of our
22 financial markets and market participants. I

1 appreciate that in moving forward, we must heed our
2 directive to establish capital standards appropriately
3 and in due consideration of other activities engaged
4 in by swap dealers and major swap participants such
5 that we ensure that we do not penalize commercial end-
6 users who need choices and benefit from competition in
7 our markets.

8 The reopening's overarching premise is that
9 the chosen response to certain uncertainties at the
10 time of the Commission's prior proposals resulted in
11 recommending standards that, in application, could in
12 no way be justified as appropriate to offset the
13 greater risk to swap dealers and major swap
14 participants and the financial system such that the
15 only solution for the potentially extreme overshoot is
16 to dial it back. With the passage of time comes a
17 nagging amnesia to the pain that the crisis brought on
18 American households and the global economy. We cannot
19 forget that undercapitalization was at the heart of
20 the crisis.

21 The overall changes to the derivatives
22 market over the last several years, the Commission's

1 adoption and implementation of margin rules for
2 uncleared swaps and growing knowledge and experience
3 with swap dealers and recent movement by the
4 Securities and Exchange Commission in finalizing
5 capital, margin, and segregation requirements as well
6 as financial reporting requirements for security-based
7 swap dealers and major security-based swap
8 participants provides a reasonable basis for affording
9 the public an opportunity to reevaluate the 2016
10 proposal. However, to the extent the reopening seeks
11 additional comment on both broader issues of
12 harmonization and more targeted proposals regarding
13 what amount of capital is appropriate and what
14 methodology is used, its focus on solidifying a data-
15 driven approach should send a strong signal that the
16 Commission must justify its final determinations with
17 respect to capital standards.

18 To reiterate, I would have liked to support
19 today's Commission's action. To the extent it would
20 move us toward a final rule on a matter that is
21 critical to the safety and resiliency of our markets,
22 the supplemental concepts for consideration and

1 overarching premise that we overshot the mark badly in
2 2016 raises concerns. If the '16 proposal is an
3 extreme overshoot and if there are alternative
4 methodologies and concepts to consider because of new
5 market data since then, the appropriate way in my view
6 to provide the public with an opportunity to comment
7 is to issue a re-proposal.

8 While I would have liked to stand with my
9 fellow commissioners today in supporting this first
10 step towards a final capital rule, I cannot justify it
11 under these circumstances.

12 Again I would like to thank the staff for
13 all of your hard work. I really appreciate the time
14 you have given me and my staff. And I certainly look
15 forward to working with you and the chairman in the
16 future to get this rule done in an appropriate way.

17 CHAIRMAN TARBERT: Thank you very much,
18 Commissioner Behnam.

19 Commissioner Quintenz?

20 COMMISSIONER QUINTENZ: Thank you, Mr.
21 Chairman.

22 I think what I am going to do is read my

1 statement on the rule first and then maybe ask some
2 follow-up questions from it because, with all due
3 respect to my colleagues, I significantly disagree
4 with a number of the characterizations of this, as
5 well as what constitutes a recollection of what
6 occurred. And I would like to either set the record
7 straight on that or at least provide my opinion. I
8 have long said that finalizing capital requirements
9 for FCMs and swap dealers is perhaps the most
10 consequential rulemaking of the post-crisis reforms to
11 get right.

12 The financial crisis exposed serious
13 vulnerabilities in the financial system -
14 uncollateralized, opaque, bilateral exposures, which
15 under the right circumstances could have and
16 ultimately, did cause a panic and liquidity freeze due
17 to concerns around that counterparty credit risk.
18 This panic in my opinion transformed a significant
19 recessionary event into the crisis as we know it.
20 Importantly, since the financial crisis, global
21 regulators, and certainly those in the U.S., have
22 implemented many policy reforms, like central clearing

1 and margin for uncleared swaps, designed to bring
2 transparency to those exposures.

3 I have long lamented prior regulators'
4 implementation of important swaps market regulatory
5 reforms by viewing them in isolation of each other,
6 trying to calibrate each of them in a way that it
7 alone could have prevented the crisis. In fact, I
8 think the elegance of the reforms is that they work
9 together and build upon each other.

10 Therefore, in my view, it is wrong to think
11 of capital in terms of what levels should have existed
12 during the financial crisis that could have prevented
13 it from occurring. Very few capital regimes, in my
14 opinion, could have provided the market with enough
15 certainty given the size, nature, and the opacity of
16 those exposures, to have removed the possibility of
17 the panic. And those regimes that could have done
18 that would have rendered the swaps market obsolete or
19 uneconomic. Therefore, regulatory capital regimes
20 implemented to respond to the last crisis need to
21 respect the increased transparency and the certainty,
22 which other reforms have already brought to the

1 market. I believe we are asking the right questions
2 in this reopening to respect that progress in
3 calibrating our own capital regime appropriately.

4 The final pillar of our Dodd-Frank Act
5 reforms, capital, ensures that firms are able to
6 continue to operate during times of economic and
7 financial stress by providing an adequate cushion to
8 protect them from losses. Just as important as the
9 safety and soundness of individual firms, capital is
10 designed to give the marketplace as a whole confidence
11 that any one firm has a high probability of surviving
12 the next crisis.

13 Capital requirements also create important
14 incentives that drive market behavior. The cost of
15 capital may be the most determinative factor in a
16 firm's decision to remain or become a swap dealer or
17 to continue to provide clearing services to clients in
18 the case of an FCM. If capital costs are too
19 expensive or too inappropriately calibrated, firms
20 will restrict certain business activities, end
21 unprofitable business lines, or in some cases exit the
22 swaps or futures markets altogether, which we have

1 already seen. As a result, over time, the swaps and
2 futures markets would become less liquid, less
3 accessible to end users, more heavily concentrated,
4 and less competitive. These are not the hallmarks of
5 a healthy financial system. And, in fact, I think
6 they are all things that a lot of us on this dais have
7 expressed concern about.

8 Therefore, appropriate capital levels are
9 directly linked to both the health and the vibrancy of
10 the derivatives markets and to the sustainability of
11 the entire financial system more broadly. To promote
12 a vibrant derivatives market, I believe it is
13 critically important that the CFTC finalize a capital
14 rule that is appropriately calibrated to the true
15 risks posed by an swap dealer's or FCM's business.

16 So I am pleased to support the reopening and
17 the request for comment before us today. This
18 document solicits comment on key issues that the
19 Commission must get right in the final rule to ensure
20 that capital requirements are appropriate and
21 commensurate to a firm's risk.

22 I appreciate that market participants have

1 commented on two prior capital proposals already and
2 the Commission will continue to consider all past
3 comments in moving forward with any final rule.
4 Nevertheless, I hope commenters use this opportunity
5 to provide the Commission with much-needed data and
6 quantitative analysis demonstrating the impact that
7 various choices contemplated would have on a firm's
8 minimum capital level and, by extension, on that
9 firm's ability to participate in the market and
10 adequately service its clients. Data is going to be
11 vital, and should always be vital, to the Commission's
12 ability to evaluate various capital alternatives and
13 identify those alternatives that would render certain
14 business lines uneconomic.

15 Let me talk just briefly about the 8 percent
16 risk margin amount. We heard from many commenters
17 that of all of the alternatives, the 8 percent risk
18 margin amount would act not as a capital floor, as
19 intended, but, rather, be the primary driver of a
20 firm's capital allocation and as a potential binding
21 constraint across their business. And, whereas, FCMS
22 are currently required to include in their minimum

1 capital requirement 8 percent of the margin required
2 for their futures and cleared swaps customer
3 positions, the 2016 proposal expanded the 8 percent
4 risk margin amount to include proprietary futures,
5 swaps, and security-based swap positions for FCMs and
6 swap dealers electing the net liquid asset approach.

7 In addition to these proprietary positions
8 being included in the risk margin amount, these FCMs
9 and SDs would also be subject to capital charges on
10 these proprietary positions. I hope commenters can
11 provide us with data showing the capital costs of
12 including proprietary positions for the first time in
13 an FCM's risk margin amount. To the extent possible,
14 it would also be helpful to see how different risk
15 margin percentages or a different scope of products
16 included in the margin amount impacts the minimum
17 capital requirements for an actual or hypothetical
18 portfolio of positions.

19 I have more that I will release in my full
20 statement, but let me stop there and maybe just ask a
21 couple of quick questions. Director Sterling, do you
22 agree that it is important to have data to finalize

1 this rule?

2 MR. STERLING: Wholeheartedly, Mr.
3 Commissioner.

4 COMMISSIONER QUINTENZ: Do you feel as
5 though we have that data currently?

6 MR. STERLING: No.

7 COMMISSIONER QUINTENZ: Let me speak to Tom
8 for a second. I feel like we have been having a
9 capital conversation for about 10 straight months now.
10 And I appreciate all of the hard work that you have
11 put into helping our office understand the different
12 regimes that are out there, as well as work with the
13 SEC to make sure that the impact of various choices
14 was well understood. And I think we can take a small
15 amount of credit for what I think turned out to be a
16 very good proposal from the SEC's perspective in terms
17 of how it impacted a very broad part of our
18 marketplace.

19 Maybe, Tom, I can ask you a kind of a direct
20 question that -- in the 2016 proposal, we did suggest
21 8 percent. Was that number heavily data-driven or was
22 it referenced through some other concept?

1 MR. SMITH: It was not heavily data-driven.
2 It was based on the existing, as you just mentioned,
3 the existing, FCM requirement of 8 percent of the
4 customer transactions. And it was incorporated into
5 this approach. That is correct.

6 COMMISSIONER QUINTENZ: Okay. And I would
7 like to point out that it is easy to kind of focus and
8 ridicule or badmouth certain percentages that may seem
9 large or small. But I think the fact of the matter
10 is, we all understand math. And we have to realize
11 that number is a percentage of a base. And that
12 percentage may be large or small depending on the
13 equation of what it multiplies. And in the scenario
14 of the 2016 proposal, the base seems to be very large.
15 It grosses up all counterparty net margin amounts
16 across proprietary positions, as well as swaps and
17 security-based swaps. Is that correct?

18 MR. SMITH: That is correct.

19 COMMISSIONER QUINTENZ: And there has also
20 been a lot of conversation around harmonization
21 issues. I would like to point out that if we were
22 harmonizing for harmonization's sake, then the only

1 base that we would include would be security-based
2 swaps. Is that correct?

3 MR. SMITH: That is correct

4 COMMISSIONER QUINTENZ: Okay. So maybe we
5 should set that record straight. And we can talk
6 about whether or not we should harmonize for
7 harmonization's sake in that context.

8 I would also like to note that the proposal
9 asked questions about a number of different
10 percentages, or any percentage that seems to be
11 appropriate to the safety and soundness of the firm
12 and the economic benefit they should derive from
13 dealing in these products. It also asks about
14 eliminating this concept specifically. And I know it
15 is not because we don't think there should be any
16 minimum capital requirements. But it is because we
17 are asking whether or not it may be a very difficult
18 thing to actually calibrate appropriately to the
19 different businesses and the different portfolios and
20 the books that they have - that it may be better,
21 which we will ask about, to rely on the minimum
22 capital standards that are already in place through

1 other approaches. Is that correct?

2 MR. STERLING: That is correct. I think
3 that we do ask about that. And it is in the context,
4 Mr. Commissioner, if I may, of sort of recognizing
5 that a certain portion of capital is consensual in the
6 sense that a firm knows best its risk exposures, we
7 had to provide a framework of choice for them. And
8 they have to design something consistent with
9 standards that works for them and works for us. So it
10 will be difficult and data-driven. And that is why,
11 among other reasons, we ask that question.

12 COMMISSIONER QUINTENZ: Okay. Thank you.

13 And just maybe two final points. One is
14 thank you for a long comment period. I think 75 days
15 is a really robust amount of time to get the data that
16 I think is necessary to ensure that we appropriately
17 calibrate this regime.

18 I would also like to note, I applaud your
19 inclusion of questions around the tangible net worth
20 approach and how or if we can recognize various forms
21 of collateral that end-users have better access to
22 than maybe the cash collateral that is normally

1 thought of in the bank regulators' recent final rule
2 on SA-CCR. They eliminated the alpha surcharge on
3 positions with commercial end-user firms in
4 recognition of the benefits that some of that
5 collateral can provide. And I am interested to hear
6 commenters' perspectives of that. And I applaud you
7 for including that question.

8 Thank you all very much for your hard and
9 diligent work and your communication with my office.
10 Thank you, Mr. Chairman.

11 CHAIRMAN TARBERT: Thank you very much,
12 Commissioner Quintenz. I am also pleased to support
13 the reopening. So let me just make sure I totally get
14 this straight because I am the new guy here. We have
15 no capital requirement right now for swap dealers on
16 the books here. Is that right?

17 MR. STERLING: Yes, sir.

18 CHAIRMAN TARBERT: So it has been a nine-
19 year rulemaking period. All right.

20 MR. STERLING: Yes.

21 CHAIRMAN TARBERT: And, then, on the point
22 -- at a later time, I think I will say something about

1 capital because this is an area that -- I actually
2 happened to write a doctoral dissertation on the Basel
3 capital requirement. But I am not going to -- our job
4 is to help educate the public, not punish you. So I
5 will not say any more about that, but there are
6 different capital requirements for different
7 objectives. Right?

8 So the capital requirements, this goes to a
9 good question that Commissioner Behnam had about, you
10 know, what is the end goal. I do think there are
11 different strategies. The Basel capital requirements
12 in my view should generally be more conservative
13 because they are dealing with insured depository
14 institutions, institutions that have access to the
15 discount window. I think when we look at broker-
16 dealers; swap dealers; and, particularly, FCMS, the
17 goal has always been focused on customer funds and
18 making sure that -- not to prevent insolvency but,
19 rather, to ensure there is enough capital to make sure
20 customers are made whole in the event of a insolvency.
21 So we will have to sort of think about, you know,
22 those various strains, but I think you see that in our

1 FCM regime. We have had a capital requirement there
2 for decades.

3 On the issue about the leverage ratio, I
4 just want to make sure I am reading the question
5 right. My understanding is that in no way does this
6 contemplate that if we went to final, there would be a
7 leverage ratio. Is that right?

8 MR. STERLING: That is correct, Mr.
9 Chairman.

10 CHAIRMAN TARBERT: So it is just a question
11 about down the line. The 8 percent or the margin-
12 based capital requirement that Commissioner Quintenz
13 was speaking about, the question is, down the line, at
14 a future rulemaking, is that something the Commission
15 should consider in lieu of the margin-based
16 requirement? Right?

17 MR. STERLING: Yes, sir. That is right.

18 CHAIRMAN TARBERT: All right. Okay. Well,
19 I think I will ask whether the commissioners are
20 prepared to vote. Okay. Mr. Kirkpatrick, would you
21 please call the roll?

22 MR. KIRKPATRICK: Thank you, Mr. Chairman.

1 The motion now before the Commission is on
2 the approval of the proposal reopening the comment
3 period and requesting additional comment with respect
4 to capital requirements for swap dealers and major
5 swap participants. Commissioner Berkovitz?

6 COMMISSIONER BERKOVITZ: No.

7 MR. KIRKPATRICK: Commissioner Berkovitz
8 votes no.

9 Commissioner Stump?

10 COMMISSIONER STUMP: Aye.

11 MR. KIRKPATRICK: Commissioner Stump votes
12 aye.

13 Commissioner Behnam?

14 COMMISSIONER BEHNAM: No.

15 MR. KIRKPATRICK: Commissioner Behnam votes
16 no.

17 Commissioner Quintenz?

18 COMMISSIONER QUINTENZ: Aye.

19 MR. KIRKPATRICK: Commissioner Quintenz
20 votes aye.

21 Chairman Tarbert?

22 CHAIRMAN TARBERT: Aye.

1 MR. KIRKPATRICK: Chairman Tarbert votes
2 aye.

3 Mr. Chairman, on this matter, the ayes have
4 three, the noes have two.

5 CHAIRMAN TARBERT: Thank you very much. The
6 ayes have it, and the motion to reopen the comment
7 period carries.

8 At this time, I would now like to invite our
9 third and final presentation. In this case, it is on
10 the proposed rule that would amend the swap clearing
11 requirement exemption for inter-affiliate swaps.
12 Specifically from our Division of Clearing and Risk,
13 we have director Clark Hutchison, Special Counsel
14 Melissa D'Arcy, and Deputy Director Sarah Josephson.
15 So Clark, Melissa, and Sarah, the floor is yours.
16 Thank you.

17 MR. HUTCHISON: Good morning, Mr. Chairman,
18 commissioners, fellow staff. This is my first
19 appearance at an open meeting of the Commission. I
20 would like to take this opportunity to briefly
21 introduce myself. My name is Clark Hutchison. And I
22 am the director of the Division of Clearing and Risk.

1 Prior to joining the Commission in July, I spent over
2 three decades working for a number of large financial
3 institutions in the area of clearing and risk
4 management.

5 This morning, my staff and I will be
6 presenting a proposal to amend the Commission
7 regulation 50.52, the inter-affiliate exemption from
8 the Commission's swap clearing requirement.

9 When the Commission adopted the inter-
10 affiliate exemption, it established conditions that
11 affiliated entities must satisfy when electing the
12 inter-affiliate exemption in relation to cross-border
13 swap activity. Of those conditions, the alternative
14 compliance provisions were time-limited and expired in
15 2014. Since that date, DCR staff provided targeted
16 relief to allow eligible affiliates to continue using
17 the expired compliance frameworks.

18 Today's proposed amendments would reinstate
19 the alternative compliance provisions with minor
20 modifications to align with the staff no-action relief
21 that is currently in place.

22 I would like to recognize this morning Sarah

1 Josephson, a deputy director; and Melissa D'Arcy, a
2 special counsel from DCR, for their hard work on this
3 rulemaking proposal. In addition, I would like to
4 thank our colleagues in the Office of the General
5 Counsel Carlene Kim, Paul Schlichting, and Mark Fajfar
6 and our colleagues in the Office of the Chief
7 Economist Scott Mixon and Steve Kane for their time,
8 effort, and helpful assistance in preparing this
9 rulemaking. Thank you all.

10 I will now ask Melissa to introduce the rule
11 proposal the Commission will be considering this
12 morning.

13 MS. D'ARCY: Good morning, Mr. Chairman and
14 commissioners. I would like to thank you for this
15 opportunity to present the rule proposal this morning.

16 The proposed amendments would update
17 Commission regulation 50.52 to reflect current market
18 practices with respect to a specific condition of the
19 inter-affiliate exemption from the swap clearing
20 requirement.

21 The proposed edits accomplish three things.
22 First, the proposal would eliminate the expiration

1 date of March 11, 2014 and reinstate the alternative
2 compliance provisions.

3 Second, the proposal would expand the number
4 of jurisdictions in which affiliated entities could be
5 located and not be constrained by a limit on the
6 aggregate notional value of swaps eligible for the
7 exemption.

8 And, third, the proposal would streamline
9 the provisions under Commission regulation 50.52 to
10 delete any unnecessary or unused provisions.

11 The proposal seeks comments from the public
12 regarding all of these changes. Particularly, if any
13 market participants rely on a provision that would be
14 deleted, we would request that people inform us of
15 that.

16 Overall, this proposal is intended to
17 reflect the Commission's dedication to promoting sound
18 regulation and improving clarity in its rules. Before
19 discussing the specifics of the outward-facing swaps
20 condition that is the subject of this proposal, I
21 would like to briefly outline the general structure of
22 the Commission's inter-affiliate exemption from the

1 swap clearing requirement.

2 In 2013, soon after the Commission issued
3 its first clearing requirement for certain interest
4 rate swaps and credit default swaps, the Commission
5 adopted an inter-affiliate exemption as well. Under
6 section 4(c), "Public Interest Exemption Authority,"
7 in the Commodity Exchange Act, the Commission is
8 permitted to exempt certain transactions or persons
9 entering into transactions from requirements or
10 provisions of the act in order to promote responsible
11 economic or financial innovation and fair competition.
12 The Commission determined that inter-affiliate
13 transactions provide an important risk management role
14 within corporate groups and that such swaps, if
15 properly risk-managed, may be beneficial to the entity
16 as a whole.

17 The Commission recognized these benefits and
18 adopted the exemption for eligible affiliated entities
19 subject to certain conditions. For example, these
20 conditions include the requirement to maintain a
21 centralized risk management program and to report
22 certain information to a swap data repository.

1 There is one more tailored condition to the
2 inter-affiliate exemption, the outward-facing swaps
3 condition that is the focus today. The outward-facing
4 swaps condition was adopted in order to address the
5 potential risk that eligible affiliated entities would
6 evade the Commission's clearing requirement through
7 third party trades with foreign affiliates that are
8 not subject to a domestic clearing regime that covers
9 analogous counterparties or products. As part of its
10 rationale for adding an outward-facing swaps
11 condition, the Commission explained that it would not
12 prejudge the potential incentives or ways of evading
13 or complying with the Commission's clearing
14 requirement and the inter-affiliate exemption from
15 clearing. The Commission viewed the requirements
16 under Commission regulation 50.52(b)(4) as a
17 transparent way to mitigate the risk that affiliates
18 would use the inter-affiliate exemption to evade the
19 clearing requirement.

20 Now that the Commission has had some
21 experience monitoring the election of the inter-
22 affiliate exemption and we have heard feedback from

1 market participants using the exemption, we feel it is
2 an appropriate time to reconsider the conditions.

3 The Commission established five mechanisms
4 through which counterparties could comply with the
5 outward-facing swaps condition. One, counterparties
6 could elect to clear the swaps through a registered or
7 exempt DCO (derivatives clearing organization). Two,
8 counterparties could comply with the requirements of a
9 non-U.S. clearing regime that the Commission has
10 determined to be comparable and comprehensive but not
11 necessarily identical to the Commission's clearing
12 regime. Three, counterparties could comply with an
13 exception or exemption from the clearing requirement.
14 Four, counterparties could comply with an exception or
15 exemption under a foreign jurisdiction's clearing
16 requirement. Or, five, counterparties could clear the
17 swap through a clearing organization that is not
18 registered with the Commission as a DCO but is subject
19 to supervision and has been assessed to be in
20 compliance with the principles for financial market
21 infrastructures.

22 Based on concerns that non-U.S. clearing

1 regimes might not be implemented quickly enough to
2 permit market participants to use some of these
3 outward-facing compliance mechanisms, the Commission
4 adopted a set of time-limited alternative compliance
5 frameworks. A number of the outward-facing swap
6 provisions would require the Commission to issue
7 comparability determinations with respect to the
8 clearing requirement.

9 To provide additional flexibility in the
10 absence of this determination, the Commission adopted
11 the alternative compliance frameworks. The
12 alternative compliance frameworks to the outward-
13 facing swaps condition generally permit counterparties
14 to enter into affiliated swaps without clearing the
15 outward-facing swap so long as variation margin
16 requirements are satisfied.

17 When the Commission adopted the alternative
18 compliance frameworks in 2013, it believed the
19 clearing requirement regimes were under development in
20 a number of other non-U.S. jurisdictions. The
21 Commission intended for the alternative compliance
22 frameworks to assist market participants' transition

1 to broadly similar clearing requirements around the
2 globe. In the absence of broadly similar non-U.S.
3 clearing requirements, eligible affiliates could enter
4 into uncleared swaps with an unaffiliated counterparty
5 outside of the U.S. and then enter into uncleared
6 swaps on a back-to-back basis using the inter-
7 affiliate exemption that could transfer risk back into
8 the United States.

9 The approach to adopting and implementing
10 clearing requirements around the globe was less
11 coordinated. Some jurisdictions took longer than
12 expected to implement their own clearing regimes. In
13 response to requests from counterparties concerned
14 about complying with the outward-facing swaps
15 condition, DCR staff issued a no-action letter to
16 permit counterparties to continue using the
17 alternative compliance frameworks.

18 DCR subsequently extended its no-action
19 relief in five additional letters. The most recent
20 letter, dated December 14th, 2017, provides relief to
21 eligible affiliates that comply with the alternative
22 compliance frameworks, as described in the letter,

1 until the earlier of December 31st, 2020 or the
2 effective date of any amendments to Commission
3 regulation 50.52. Eliminating the expiration date in
4 Commission regulation 50.52 would reinstate the
5 alternative compliance frameworks and allow eligible
6 affiliates to continue using these frameworks with the
7 additional certainty of Commission regulation, rather
8 than relying on DCR staff to continue issuing no-
9 action relief.

10 The second proposed edits to Commission
11 regulation 50.52 would expand the list of jurisdiction
12 in which an eligible affiliate may be located and
13 still take advantage of an alternative compliance
14 framework without subjecting the swap to a 5 percent
15 test limit.

16 The Commission originally adopted the
17 alternative compliance frameworks with no limits on
18 the number or percentage of inter-affiliate swaps that
19 could be entered into with an eligible affiliate
20 counterparty for those located in the European Union,
21 Japan, or Singapore only, so long as the variation
22 margin requirements were satisfied.

1 After the Commission expanded its interest
2 rate swap clearing requirement in 2016, DCR
3 anticipated that eligible affiliates would enter into
4 more swaps in jurisdictions within which the official
5 domestic currency was subject to the Commission's
6 clearing requirement. For example, the Commission
7 expanded its fixed-to-floating interest rate swap
8 clearing requirement to include the Mexican peso. And
9 we anticipated that eligible affiliates would conduct
10 additional swaps with entities in Mexico.

11 As a result, DCR issued no-action relief to
12 eligible affiliates if one of the counterparties is
13 located in an expanded list of jurisdictions, to
14 include five additional countries: Australia, Canada,
15 Hong Kong, Mexico, Switzerland, and the United
16 Kingdom.

17 The DCR relief in line with Commission
18 regulation 50.52(b)(4) limits the amount of uncleared
19 inter-affiliate swaps that an eligible affiliated
20 counterparty located in the U.S. may enter into with
21 affiliate counterparties in jurisdictions other than
22 Australia, Canada, the European Union, Hong Kong,

1 Japan, Mexico, Singapore, Switzerland, the United
2 Kingdom, or the United States.

3 An eligible affiliate located in the U.S.
4 may not enter into swaps that are valued at more than
5 5 percent of the aggregate notional value of all of
6 its swaps, which are subject to the Commission's
7 clearing requirement with an affiliate located in a
8 jurisdiction other than those countries. This
9 limitation is intended to prevent concentrations of
10 uncleared inter-affiliate swaps from building up in
11 jurisdictions that do not have established clearing
12 regimes. In both alternative compliance frameworks,
13 the proposal is modifying the set of jurisdictions
14 that are subject to the 5 percent notional amount
15 limit, to include fewer jurisdictions, and is
16 increasing the set of jurisdictions in which eligible
17 affiliate swaps are not limited.

18 In addition, this proposal makes one change
19 that is different from the current no-action relief
20 provided by DCR. The proposal expands the list of
21 jurisdictions to add the United Kingdom as a separate
22 jurisdiction from the European Union in the event of

1 Brexit.

2 Third, the proposed edits to Commission
3 regulation 50.52 would streamline the provisions and
4 alternatives offered so that any unnecessary or unused
5 provisions offering relief would be deleted. The
6 proposal does not include a separate set of compliance
7 instructions for eligible affiliate counterparties if
8 one of the affiliates is a non-financial entity and
9 neither of the affiliates is affiliated with a swap
10 dealer or major swap participant. This alternative
11 would be deleted because we do not believe that non-
12 financial entities that are not affiliated with swap
13 dealers are electing the inter-affiliate exemption
14 currently. The proposal invites commenters to discuss
15 whether or not the deletion is appropriate.

16 The proposal also deletes the option given
17 to eligible affiliates to pay and collect full
18 variation margin daily on all swaps entered into
19 between the eligible affiliate counterparty and
20 unaffiliated counterparties. Staff believes that all
21 eligible affiliates choose to pay and collect
22 variation margin with their own affiliates now, and

1 there is no reason to preserve the option to pay and
2 collect variation margin with the unaffiliated
3 counterparties if that is not being used.

4 The revisions also propose to include a new
5 definition of the term "United States" in order to
6 clarify which eligible affiliates will qualify for the
7 alternative compliance frameworks.

8 Overall, the proposed changes to Commission
9 regulation 50.52 reflect an effort to reevaluate and
10 update the outward-facing swaps condition. Staff has
11 been monitoring the swaps transaction-level data to
12 gain additional information about the types of
13 entities that are electing the inter-affiliate
14 exemption and, more specifically, the eligible
15 affiliates that are electing the inter-affiliate
16 exemption and complying with the outward-facing swaps
17 condition through one of the alternative compliance
18 frameworks.

19 Staff has identified roughly 60 financial
20 entities that are located outside of the U.S. and it
21 believes to be complying with the outward-facing swaps
22 condition using the alternative compliance frameworks.

1 Based on reviews of swap data repository information,
2 these types of entities electing the inter-affiliate
3 exemption are almost exclusively financial and
4 affiliated with a registered swap dealer. While we
5 note that the entities electing the exemption may
6 change over time based on entity structures and
7 business needs, the number of entities electing it and
8 the locations of the entities around the globe have
9 remained relatively stable over the past few years.

10 There also appears to be an increase in the
11 number of entities electing the inter-affiliate
12 exemption from jurisdictions that were added through
13 no-action relief in 2016 and 2017, such as Australia,
14 Canada, and Mexico. This slight shift is consistent
15 with the expectation that additional entities would
16 elect the inter-affiliate exemption as it became
17 available in additional jurisdictions without a 5
18 percent test limitation.

19 Again, the proposed changes are intended to
20 codify the current no-action relief, which provides
21 that eligible affiliates may continue to use the
22 alternative compliance frameworks, as modified, to

1 comply with the outward-facing swaps condition. The
2 goal of this rulemaking is to clarify and streamline
3 the conditions required for eligible affiliates.

4 We hope this information is helpful and will
5 be glad to answer any questions this morning.

6 CHAIRMAN TARBERT: Thank you very much for
7 that great and very detailed presentation,
8 particularly to you, Melissa.

9 At this point, I will entertain a motion to
10 approve the division's proposed rulemaking relating to
11 the clearing exemption.

12 COMMISSIONER QUINTENZ: So moved.

13 COMMISSIONER BEHNAM: Second.

14 CHAIRMAN TARBERT: Thank you.

15 I would now like to open the floor for
16 commissioners to ask any questions or make any
17 comments. I don't have any questions. All I will say
18 is, you know, I like to see these instances where we
19 have a codification of no-action letters, in this case
20 a temporary no-action letter. You know, once we
21 figure out, you know, what the right answer is, to
22 codify it I think is very important. So it is not

1 only good policy. It is also good government.

2 Commissioner Quintenz?

3 COMMISSIONER QUINTENZ: Thank you, Mr.

4 Chairman. Just a couple of quick questions.

5 And thank you for the presentation, Melissa.

6 I think you covered this, but I just wanted to be a
7 little more clear. What are the types of entities
8 that typically elect this exemption? Are they
9 unregistered commercial firms or are they more
10 registered firms in our space?

11 MS. D'ARCY: Yes. They tend to be financial
12 entities that that are generally registered with the
13 Commission or affiliates of registrants. And we have
14 seen them be fairly consistent over the years.

15 COMMISSIONER QUINTENZ: Okay. I wanted to
16 ask -- again, you brought this up a number of times,
17 but I just wanted to raise it and see if I understand
18 it. The rationale for preserving the 5 percent
19 limitation on affiliates' variation margining their
20 swaps when that affiliate is located outside of one of
21 the 9 jurisdictions that has an adopted a swap
22 clearing requirement. Can you just tell me that

1 explanation again in terms of where you think risk can
2 come into the system, versus the protections that we
3 have in place right now for those entities and these
4 affiliates from a variation margining perspective?

5 MS. D'ARCY: Sure. So we think it is
6 important to preserve the 5 percent limit because not
7 all jurisdictions have adopted a robust clearing
8 regime. And not all have an uncleared margin
9 requirement. So for those jurisdictions where
10 somebody is entering into an uncleared swap, the risk
11 is that they could pool concentrations of risk in
12 those jurisdictions that have less domestic oversight
13 and are subject to fewer requirements on that side.
14 And then there is always the risk of the back-to-back
15 transfers back to the U.S. And that is why we have
16 the variation margin requirements, to kind of prevent
17 that.

18 COMMISSIONER QUINTENZ: Okay. Thank you.

19 And the final question, which I know the
20 answer to. Maybe I will just say it. I am correct
21 that this exemption from the clearing requirement
22 doesn't provide relief from the trade execution

1 requirement. Is that correct?

2 MS. D'ARCY: That is correct. That is being
3 considered separately.

4 COMMISSIONER QUINTENZ: Okay. I would like
5 to preemptively express my support for considering
6 that. So thank you very much for your hard work.

7 CHAIRMAN TARBERT: Thank you.

8 Commissioner Behnam?

9 COMMISSIONER BEHNAM: Thanks, Mr. Chairman.
10 And thank you, Melissa and Sarah, for your work. And
11 thanks for taking your time to talk with me and my
12 staff a few days ago. I do have a statement, which I
13 will post on the CFTC website, but just I will
14 highlight some questions and some of the themes in my
15 statement within the questions.

16 In the 2013 preamble and then also in this
17 draft, there is a statement which I think is worth
18 discussing because it is a little bit
19 counterintuitive, but I do believe, Melissa, you
20 pointed it out, why we are moving forward and the
21 rationale, despite the statement. But the statement,
22 by and large, recognizes the fact that paying and

1 collecting variation margin does not mitigate
2 counterparty credit risk to the same extent that
3 central clearing does. So we are sort of taking a
4 step in a direction where we recognize it is not a
5 safe and resilient sort of mitigant against risk
6 versus central clearing. Can you just talk a little
7 bit about the rationale that we are moving forward?

8 I know it is embedded in the statement you
9 made, Melissa, but I think it is important since we
10 are recognizing the fact that this is not the most
11 robust risk mitigant. Yet, we are going forward with
12 it. I think it would be helpful.

13 MS. D'ARCY: Sure. I think that the
14 Commission made efforts to recognize that clearing is
15 the best protection in this instance. And, yet, it is
16 not necessarily workable for these affiliated entities
17 that are going to be operating outside of the U.S. in
18 jurisdictions that have not reached that level of
19 regulation that the CFTC has, for example. We don't
20 necessarily want to put affiliated entities at a
21 market disadvantage or to impose requirements on them
22 when we do feel that the variation margin protects

1 against any of that outside risk coming back into the
2 United States, not only does it force the
3 counterparties to mark-to-market; it also creates an
4 inhibition to taking outsized risk.

5 COMMISSIONER BEHNAM: Thank you.

6 Dovetailing off of that, which is I think -- and we
7 discussed this a little bit. This is why I feel
8 comfortable supporting this proposal. Despite VM not
9 necessarily being the best risk mitigant -- and I am
10 sort of making that term up here, but we do have a
11 number of sort of powers within the CFTC within 50.52
12 to identify those who are electing this exemption and
13 then, beyond that, having some lens into the scope and
14 the size of the individuals and the depth of the
15 market. Can you talk a little bit about that? I
16 know, Melissa, you pointed it out but also some of the
17 special call, antifraud, and anti-evasion authorities
18 that we retain. Just for me personally as a measure
19 of getting comfortable with what we are doing, what we
20 are proposing, despite VM not being the best
21 methodology, we do as an agency, both from a
22 surveillance standpoint and ultimately needed from an

1 enforcement standpoint, the ability to identify the
2 risk, see where the pockets of risk might be forming
3 and then do whatever due diligence and action we need
4 to resolve that.

5 MS. D'ARCY: Sure. I think it is important
6 to note that in both the initial adopting release, the
7 Commission noted that it was very intent on preventing
8 evasion of the clearing requirement when it adopted
9 this exemption. We tried to make that point today as
10 well. So one of the ways that we can do that is by,
11 as you said, monitoring the entities that are electing
12 it, monitoring how they are electing it, and making
13 sure that, for example, they are complying with the
14 alternative compliance frameworks, that the notional
15 value of their swaps complies with the 5 percent test
16 if that is applicable, and then we also have separate
17 anti-evasion authority under 50.10 that exists and we
18 use to monitor and prevent evasion of the clearing
19 requirement.

20 COMMISSIONER BEHNAM: Thanks. Lastly, and
21 talking about methodology a little bit earlier with
22 the DSIO team. Do we have any lens into the

1 methodologies that the entities will use in
2 calculating VM?

3 MS. D'ARCY: So that is not something that
4 we have prescribed in the rules. So they are free to
5 select and choose their own variation margin regimes
6 internally between the counterparties. And we do not
7 necessarily have a lot of insight into how they are
8 doing that.

9 COMMISSIONER BEHNAM: Okay. Thank you.
10 Again, thanks for your work on this and your time with
11 me. And I think with respect to some of these
12 questions, I look forward to the comments from the
13 public so that we can move forward with this.

14 Like you said, Mr. Chairman, I think it is
15 an efficient and timely and necessary thing to
16 finalize these legacy no-action letters that have been
17 around for a number of years.

18 Thank you.

19 CHAIRMAN TARBERT: Thank you.

20 Commissioner Stump?

21 COMMISSIONER STUMP: I don't have any
22 questions specifically, but I would like to say I

1 think this is exactly what the no-action relief is
2 designed to achieve. Oftentimes, regulators around
3 the world go to finalization of rules at different
4 paces. We obviously went first. We are first movers
5 in many regards. And so it created an unbalanced
6 quagmire, frankly, for a lot of affiliated entities
7 who could not make sense of what their business model
8 would allow them to do given our mandates. And so I
9 think this was designed to encourage them to continue
10 to operate in this space in a way that made sense.
11 And I am very happy we are finalizing this in the form
12 of a rule.

13 Also, we talk about these things just
14 because I have some experience on the clearing side.
15 I am always struck by, you know, these are things --
16 when you think about clearing in its most fundamental
17 sense, it is designed to eliminate counterparty credit
18 risk. And so I am going to oversimplify what I think
19 we are doing here: The counterparties at the base of
20 this proposal are, in fact, affiliated. So to the
21 extent we built in protections to ensure that risk is
22 not brought back to the United States in a way that is

1 harmful to our system, that is great, but clearing is
2 more about counterparty credit risk than it is about
3 the system itself. Certainly it can help with that,
4 but I think this is something that we should all be
5 reminded of.

6 So thank you all so much for your efforts.
7 And thank you for the great presentation, Melissa.
8 And, Clark, welcome to the CFTC.

9 CHAIRMAN TARBERT: Thank you very much.
10 Commissioner Berkovitz?

11 COMMISSIONER BERKOVITZ: Thank you, Mr.
12 Chairman. You may be relieved that Commissioner Stump
13 just made a number of the remarks that I was going to
14 make. So that can cut some of my time off.

15 I totally agree that under the
16 circumstances, the expiration of the timeframe in the
17 original regulation of 2014 for the Europeans to get
18 their clearing requirement, the three jurisdictions,
19 necessitated the continuance of the provisions
20 necessary by no-action relief.

21 Now, at that point, the Commission could
22 have gone through a notice-and-comment rulemaking or

1 whatever as an alternative, but relief needed to
2 happen. Conditions were changing. And the no-action
3 relief enabled the status quo to basically continue
4 and the Commission to adjust the program to these
5 changing global market conditions. And then the other
6 jurisdictions as they were coming online, it enabled
7 the program, the non-U.S. affiliates, to continue
8 operating in those jurisdictions without a competitive
9 disadvantage at the same time exchanging variation
10 margin to protect the risk from coming back into the
11 U.S. It was necessary at the time. We have
12 experience with that. And we have the swap data. You
13 have cited the swap data statistics. Given that
14 experience and our comfort level, also I think it was
15 extremely informative that we were able to determine
16 which of the alternatives people were using and not
17 using and who was using it and, therefore, base a
18 final regulation on the actual utility to the
19 marketplace and that informs that final regulation.
20 So I think the no-action relief was appropriate at the
21 time. And now it is totally appropriate and the right
22 thing to do to codify it so people can see it in the

1 regulation.

2 I just have a couple of questions. Why was
3 there an expiration date? What was the thinking, if
4 any, if you are aware of, initially? And I confess I
5 was here at the time, but I don't remember that
6 specific of the expiration in the initial regulation
7 of 2014. What was the purpose of that?

8 MS. JOSEPHSON: The idea at the time was
9 that that would be when the foreign jurisdictions
10 would have their regimes in place, that it would move
11 that quickly.

12 COMMISSIONER BERKOVITZ: So the fact is that
13 reading the release, that there is no foreign
14 jurisdiction that has a comparable clearing
15 requirement? We don't really expect that to be the
16 case?

17 MS. JOSEPHSON: That is correct. There is
18 no other jurisdiction that is as consistent with the
19 CFTC's in terms of the scope of products that are
20 required to be cleared and the types of market
21 participants that are required to clear.

22 COMMISSIONER BERKOVITZ: These non-U.S.

1 affiliates in these foreign jurisdictions are still
2 subject to the noncomparable clearing requirement of
3 the foreign jurisdiction. Is that correct?

4 MS. JOSEPHSON: Yes.

5 COMMISSIONER BERKOVITZ: And there is some
6 overlap, presumably. They may not be comparable and
7 comprehensive. We may not be able to make a
8 comparability determination. But there is going to be
9 significant overlap between those two clearing
10 requirements.

11 MS. JOSEPHSON: There is. I mean, the one
12 that is the closest to the U.S. is the European
13 Union's clearing requirement, it gets, in terms of the
14 product scope, fairly close to where we are.

15 COMMISSIONER BERKOVITZ: So if there is a
16 delta between a certain class that we require to be
17 cleared and they don't require it to be cleared, there
18 is still a variation margin. This alternative
19 compliance framework requires the variation margin
20 between the non-U.S. affiliate and U.S. affiliate,
21 correct?

22 MS. JOSEPHSON: Yes.

1 COMMISSIONER BERKOVITZ: Would it be correct
2 still, though, that to take advantage of these
3 alternative compliance frameworks they have to do
4 variation margin on all of their swaps subject to the
5 U.S. clearing requirement?

6 MS. D'ARCY: It is all of their swaps with
7 the other eligible affiliates.

8 COMMISSIONER BERKOVITZ: Even if that
9 eligible affiliate is then subject to a clearing
10 requirement in that eligible affiliate's home
11 jurisdiction?

12 MS. D'ARCY: If they choose to clear the
13 outward-facing swap, that is one way to comply with
14 it. So if they are subject to the non-U.S. foreign
15 clearing requirement and then they comply with it,
16 then they have already satisfied the outward-facing
17 swaps condition.

18 COMMISSIONER BERKOVITZ: This does not
19 relieve the non-U.S. affiliate from complying with its
20 home jurisdiction's clearing requirement, does it?

21 MS. D'ARCY: No.

22 COMMISSIONER BERKOVITZ: Okay. So in many

1 instances, that non-U.S. affiliate will still be
2 required to clear their outward-facing swap?

3 MS. D'ARCY: That may be true.

4 COMMISSIONER BERKOVITZ: It is just the
5 delta between the foreign jurisdiction's clearing
6 requirement and our clearing requirement that is going
7 to be still subject to variation margin between
8 affiliates, right?

9 MS. D'ARCY: In a sense. We are trying to
10 protect our clearing requirement, exactly.

11 COMMISSIONER BERKOVITZ: Exactly. Okay.
12 Okay. And now we have nine jurisdictions that have a
13 clearing requirement. So today, the set of these
14 transactions where there is variation margin, rather
15 than the -- where the non-U.S. affiliate exchanges
16 variation margin, rather than clears the outward-
17 facing swap, has diminished as time has gone by as
18 these jurisdictions have established clearing
19 requirements?

20 MS. D'ARCY: We would expect that to be
21 true. We do not necessarily track whether or not they
22 are clearing under a non-U.S. clearing regime.

1 COMMISSIONER BERKOVITZ: Okay. So I think
2 that is a significant point, too, that there has been
3 substantial clearing by these non-U.S. affiliates
4 during this time. I am interested in any comments by
5 commenters what this delta still is, whether there is
6 residual risk of being imported. And I look forward
7 to those comments, but I think this is an example of
8 how regulation progresses in an ever-changing global
9 environment. We establish a regulation. We balance.
10 We have to protect our markets, but at the same time,
11 we have to enable our market participants to
12 participate in these global markets, ensuring that no
13 undue risk is imported back into the U.S. and
14 recognizing that competitiveness, and as jurisdictions
15 come online and as the global financial regulatory
16 framework changes, we can adjust. And I think this is
17 a good proposal and reflects that sensible adjustment.

18 So thank you. Thank you for your -- there
19 are a lot of chains of transactions and conditions in
20 this thing. And it is somewhat complicated to get
21 your head around, but, actually, when you do, it sort
22 of makes sense. It makes sense. So thank you. And

1 thank you for that explanation.

2 CHAIRMAN TARBERT: Thank you. And the key
3 for me here is just that we are talking about inter-
4 affiliate transactions. So these are related
5 companies. And there is that added incentive, you
6 know, not to let one another fail to pay back your
7 brother or your sister company. I think we still have
8 that variation margin requirement in there just in
9 case, you know, if the risks were to come back to the
10 United States. But I think that is a different
11 scenario than just in a sort of arm's-length
12 transaction with some third party saying no. In that
13 case, you need to go to the clearinghouse because
14 there is credit risk there that is of a different
15 kind.

16 So, with that, if there are no other
17 questions, are the commissioners prepared to vote?
18 Okay. Mr. Kirkpatrick, would you please call the
19 roll?

20 MR. KIRKPATRICK: Thank you, Mr. Chairman.

21 The motion now before the Commission is on
22 the approval of the proposed rule regarding amendments

1 to the swap clearing requirement exemption for inter-
2 affiliate swaps. Commissioner Berkovitz?

3 COMMISSIONER BERKOVITZ: Aye.

4 MR. KIRKPATRICK: Commissioner Berkovitz
5 votes aye.

6 Commissioner Stump?

7 COMMISSIONER STUMP: Aye.

8 MR. KIRKPATRICK: Commissioner Stump votes
9 aye.

10 Commissioner Behnam?

11 COMMISSIONER BEHNAM: Aye.

12 MR. KIRKPATRICK: Commissioner Behnam votes
13 aye.

14 Commissioner Quintenz?

15 COMMISSIONER QUINTENZ: Aye.

16 MR. KIRKPATRICK: Commissioner Quintenz
17 votes aye.

18 Chairman Tarbert?

19 CHAIRMAN TARBERT: Aye.

20 MR. KIRKPATRICK: Chairman Tarbert votes
21 aye.

22 Mr. Chairman, on this matter, the ayes have

1 five, the noes have zero.

2 CHAIRMAN TARBERT: Thank you very much. The
3 ayes have it, and the motion to approve the proposed
4 rule carries. Thank you very much to DCR for your
5 participation, Sarah, Melissa, and Clark.

6 Before we move to closing statements, if
7 there are any, is there any other Commission business?

8 [No response.]

9 CHAIRMAN TARBERT: We are going to be having
10 another open meeting next week. So we will have more
11 Commission business but not today.

12 I would like to go ahead now and give my
13 fellow commissioners an opportunity to make any
14 closing statements you might have. We will start with
15 Commissioner Berkovitz.

16 COMMISSIONER BERKOVITZ: Thank you, Mr.
17 Chairman.

18 I don't have any further comments. I will
19 note on the upcoming agenda, there are a number of
20 extremely complex matters that we will be dealing
21 with, a bankruptcy, position limits, cross-border
22 issues. I can tell you that I am committed. I know

1 you have established an ambitious agenda. I can tell
2 you I am committed to working diligently and my staff
3 is committed to working diligently, but these are
4 incredibly complex matters. And I want to make sure
5 the Commission has adequate time to thoroughly
6 consider the issue. Good regulations when we have
7 well-considered regulations. So we should just keep
8 that in mind.

9 Thank you.

10 CHAIRMAN TARBERT: And, just to be clear,
11 out of the things you mentioned, I think one will be
12 next week, one will be in January, and one will be in
13 February. So otherwise I would be leaving coal in
14 your stocking this holiday season. But I think only
15 the cross-border rule, among those very complex rules,
16 will be next week. Thank you.

17 Commissioner Stump?

18 COMMISSIONER STUMP: I just want to again
19 thank everyone. I know the demands on your time,
20 given what Commissioner Berkovitz just laid out, are
21 enormous. And we all appreciate all of your efforts.
22 I appreciate all of the efforts from all of the people

1 who are back here because they have spent evenings and
2 weekends working on things of late. And I think we
3 are all very well-served to have such a wonderful
4 staff.

5 I just wanted to hearken back to what I said
6 in my opening statement relative to this Commission's
7 mission is the same as the Commission -- our mission
8 is the same, but our objective is somewhat different
9 in that previous commissions were tasked with putting
10 together an enormous new market structure for these
11 markets. And our objective is somewhat different in
12 that we have the benefit of the information that we
13 have today. And it sometimes helps inform a better
14 path forward.

15 For example, I think that the capital
16 proposal that has been -- or the reopening of the
17 comment period -- is well-timed because much has
18 changed since 2011 and 2016. And we could all be
19 well-served by a more contemporary snapshot of the
20 issues, especially in light of the other rules we put
21 in place and the rules that other fellow regulators
22 have put in place.

1 And the same can be said for the
2 codification of no-action relief. We have the benefit
3 of other jurisdictions having implemented some of the
4 reforms and us being able to have a more holistic view
5 of things.

6 Relative to transparency, I wanted to say
7 just one quick thing. You know, the Commodity
8 Exchange Act says that whenever the Commission issues
9 for official publication any opinion, release, rule,
10 order, interpretation or other determination in a
11 matter, the Commission shall provide that any
12 dissenting, concurring, or separate opinion by any
13 commissioner on the matter be published in full along
14 with the Commission's opinion, release, rule, order,
15 or interpretation. For good or bad, the Seventh
16 Circuit recently reaffirmed that that is, in fact, our
17 right as individual commissioners. I anticipate that
18 several will be exercising that right after today's
19 meeting to maybe publish dissenting views.

20 And so I just wanted to say I think this is
21 very important. And I wanted to say that I am not in
22 any way, shape, or form opposed to individual

1 commissioners being able to issue their dissenting or
2 concurring viewpoints.

3 So thank you, Mr. Chairman.

4 CHAIRMAN TARBERT: Thank you very much.

5 Commissioner Behnam?

6 COMMISSIONER BEHNAM: Thanks, Mr. Chairman.
7 I appreciate you having this meeting today. A special
8 thanks to DSIO and DCR for your work in working with
9 my staff, as I mentioned earlier. Also thanks to the
10 general counsel and the chief economist for all your
11 work with these teams.

12 And a special thanks -- I would like to
13 reiterate what Commissioner Stump said -- to my staff.
14 It is a busy time of year at home with holiday parties
15 and getting ready for the holidays and the new year.
16 So the ambitious agenda has put us all on overtime,
17 and I want to thank them for their work because it has
18 been a long couple of weeks. And we are looking
19 forward to next week as well. Thanks.

20 CHAIRMAN TARBERT: Thank you.

21 Commissioner Quintenz?

22 COMMISSIONER QUINTENZ: Thank you, Mr.

1 Chairman.

2 Yes. I would like to just reiterate my
3 sincere thanks to the staff out here for all of your
4 hard work on the re-openings, proposals, and final
5 rules today, all of the staff back here for their
6 continued efforts and communication amongst our
7 offices. I am very pleased that we took some
8 important steps today to finalizing some of the
9 requirements of Dodd-Frank, which are important
10 reforms of the swaps market, to make sure that we
11 accomplish those in a thoughtful, rational, and data-
12 driven ways, and that we ensure that they are
13 appropriate to the risks that we seek to mitigate. So
14 I am looking forward to some of the next open meetings
15 to do the same.

16 Thank you, Mr. Chairman.

17 CHAIRMAN TARBERT: Thank you very much. And
18 let me also echo my appreciation for the staff, for
19 the tremendous amount of hard work I have seen in my
20 only few months on the job as well as the staff for
21 the commissioners.

22 I also commend, you know, the idea of

1 putting out concurring and dissenting and other
2 statements. I think that is really important. And I
3 think, you know, the public sees that, but what the
4 public doesn't see is the often interaction one-on-one
5 between the commissioners, between our staffs, between
6 our staffs and the agency staff as a whole to sort of
7 make these rules what they need to be. And if you
8 will notice today -- and we had three measures. Two
9 of them were unanimous. And they were unanimous
10 because there was a lot of back and forth between the
11 offices to improve them.

12 And I think someone said it earlier -- I
13 forget which commissioner -- that by virtue of us
14 being five individuals with some very diverse
15 backgrounds coming at this, I think I am a better
16 commissioner as a result of having my four colleagues.
17 And they have helped me I think try to focus the
18 agenda, try to make our rules and regulations and the
19 other things that we promote better. So that
20 interaction is critically important. And particularly
21 during this time in Washington, having a commission
22 that not only has divergent views in some cases but

1 has the collegiality that we do I think is very
2 commendable. And I am committed to keeping that.

3 So, with that, there being no further
4 business, I would entertain a motion to adjourn the
5 meeting.

6 COMMISSIONER BEHNAM: So moved.

7 CHAIRMAN TARBERT: Those in favor of
8 adjourning the meeting will say, "Aye."

9 [Chorus of "Ayes."]

10 CHAIRMAN TARBERT: Those opposed?

11 [No response.]

12 CHAIRMAN TARBERT: The ayes have it. And,
13 again, thanks so much for everyone being here today.
14 The meeting is hereby adjourned.

15 [Whereupon, at 11:21 a.m., the meeting was
16 adjourned.]

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