



**AMERICANS  
FOR FINANCIAL REFORM**  
ACCOUNTABILITY \* FAIRNESS \* SECURITY

**Americans for Financial Reform**  
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Dear Representative,

On behalf of Americans for Financial Reform (AFR), we are writing to express our opposition to several of the bills under consideration in today's subcommittee hearing, as well as our support for HR 1847, the "Swaps Data Repository and Clearinghouse Indemnification Act".<sup>1</sup>

AFR opposes HR 686, the "Small Business Mergers, Acquisitions, Sales, and Brokerage Simplification Act of 2015", HR 1317, "A bill to amend the Commodity Exchange Act and the Securities Exchange Act of 1934 to specify how clearing requirements apply to certain affiliate transactions", and HR 1965, "The Small Company Disclosure Simplification Act". Due to the number of bills included in today's hearing, we have not completed our review of all items of legislation being considered. We may after further review express additional views on the other proposed bills under discussion today.

**HR 1317** would expand the exemption to Dodd-Frank clearing requirements by making it easier for financial entities with commercial affiliates to take advantage of the exemption from Dodd-Frank clearing requirements. The requirement that standardized derivatives transactions be cleared through a central counterparty is a fundamental financial system safeguard established by the Dodd-Frank Act, and by loosening it HR 1317 would create additional risks to the financial system.

The Dodd-Frank Act already clearly exempts commercial entities using derivatives to hedge legitimate commercial risk from clearing requirements. However, financial entities can only qualify if they are hedging risk on behalf of an affiliated commercial company and are acting as the agent of the commercial affiliate. HR 1317 would remove these limitations and leave in place only a requirement that the financial entity is somehow hedging or mitigating the risks of a commercial affiliate. As many purely financial trades can be interpreted to somehow 'mitigate the risks' of the broader corporate group, including commercial affiliates, this limitation is vague and non-specific.

This seemingly technical change could have far-reaching implications. As the non-partisan Congressional Research Service stated in an analysis of this bill, it "could potentially allow large banks to trade swaps with other large banks and not be subject to the clearing or exchange-

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<sup>1</sup> Americans for Financial Reform is a coalition of more than 200 national, state and local groups who have come together to reform the financial industry. Members of our coalition include consumer, civil rights, investor, retiree, community, labor, faith based and business groups. A list of AFR member groups is available at <http://ourfinancialsecurity.org/about/our-coalition/>

trading requirements as long as one of the banks had a nonfinancial affiliate.”<sup>2</sup> There are numerous major financial entities that have commercial affiliates and could claim that there was some relationship between their derivatives activities and mitigating risk for some commercial affiliate. For example, the Senate Permanent Subcommittee on Investigations has recently documented that the major Wall Street banks often combine commodity production and trading activities, and that these “financial companies often traded in both the physical and financial markets at the same time, with respect to the same commodities, frequently using the same traders on the same trading desk.”<sup>3</sup> HR 1317 would significantly reduce the ability of the CFTC to police risk management for this kind of co-mingling of commercial and financial activities.

There are cases in which financial affiliates of commercial entities may genuinely be hedging the production-related risks of commercial affiliates but may not in a narrow sense be acting ‘as an agent’ of the commercial affiliate. Through administrative action, the CFTC has already permitted such affiliated ‘central treasury units’ (CTUs) to make use of the clearing exemption in a wide range of cases.<sup>4</sup> The agency has thus made clear that it is taking a broad interpretation of what it means to hedge ‘on behalf of the [commercial affiliate] and as an agent’, and is eager to accommodate legitimate hedging needs. But if this restriction were eliminated entirely, as this legislation would do, then the CFTC would be dramatically limited in its ability to address attempts by financial entities to evade risk management requirements by claiming that they were mitigating the risk of commercial affiliates, an evasion that would be invited by this legislation.

We oppose this legislation and believe statutory change is unnecessary. If Congress wishes to make some statutory change in this area, it should be limited to clarifying the CFTC’s discretionary authority to accommodate the CTU model on a carefully controlled basis, and should incorporate the various controls that have been included in the CFTC’s administrative actions in this area. There should be no general reduction in CFTC authority to manage this complex area of derivatives regulation.

**HR 686** would eliminate SEC broker-dealer registration requirements for merger and acquisition brokers. While a much narrower version of this legislation could be acceptable, we believe that this legislation poses risks to investors and to the fair conduct of our financial markets.

As currently drafted, HR 686 has multiple flaws:

- It lacks needed investor protections such as provisions to prevent bad actors from taking advantage of exemptions from registration to evade enforcement of securities laws.<sup>5</sup>

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<sup>2</sup> Congressional Research Service, “CRS In Focus: HR 37 Derivatives Provision May Create Broader Exemption”, January 26, 2015.

<sup>3</sup> United States Permanent Subcommittee on Investigations, “[Wall Street Bank Involvement With Physical Commodities, Majority and Minority Staff Report](#)”, Permanent Subcommittee on Investigations, United States Senate, November 20, 2014.

<sup>4</sup> Commodity Futures Trading Commission, Division of Clearing And Risk, “[No-Action Relief For Swaps Entered Into By Eligible Treasury Affiliates](#)”, CFTC No-Action Letter 13-22, June 14, 2013; Commodity Futures Trading Commission, Division of Clearing And Risk, “[Further No-Action Relief For Swaps Entered Into By Eligible Treasury Affiliates](#)”, CFTC No-Action Letter 14-44, November 26, 2014.

<sup>5</sup> North American Securities Administrators Association, “[NASAA Letter to Senators Manchin and Vitter Re S. 1923](#)”, September 8, 2014

- The legislation applies the M&A broker exemption far too broadly, to any acquisition of a company with gross revenues of \$250 million or less. This goes far beyond transactions involving the purchase of local small businesses, and would permit numerous deals involving companies of significant size to avoid broker-dealer oversight.
- The lack of an effective provision to prevent transfer to a shell company means that the broker could effectively also take control of the transferred company in a private-equity type transaction.

The potential application to private equity is concerning, as the exemption from broker-dealer registration would restrict the SEC in policing this complex area and interfere with ongoing SEC investigation of potential abuses in private equity involving unregistered broker-dealer activities.<sup>6</sup>

This legislation is also unnecessary, as the SEC has already taken administrative action to exempt merger and acquisition brokers from broker-dealer registration, while preserving capacity to enforce needed investor protections.<sup>7</sup>

Finally, we would also point out that numerous registered broker-dealers who comply fully with SEC broker-dealer conduct requirements are active in arranging deals to sell companies, and this overly broad legislation would expose them to competition from unregulated entities that would not have to comply with important investor protection requirements such as suitability standards. We believe this is inappropriate.

**HR 1965** would exempt over 60% of publicly traded companies from requirements to file machine-readable financial statements. AFR opposes this legislation. By banning the SEC from requiring most companies in the market to file computer-readable financial data, this legislation would strike a serious blow against progress in bringing financial reporting into the 21<sup>st</sup> century. The legislation also directly contradicts recommendations from SEC staff and the SEC's Investor Advisory Committee which call on the agency to move to an open data disclosure system in order to benefit investors, issuers, and the public.<sup>8</sup>

Should Congress wish to address issues in the SEC's implementation of open data requirements, the answer is not to simply exempt the bulk of the market from any requirement to provide machine-readable data to investors. Instead, Congress should take steps that assist the SEC and the issuer community in moving data disclosure forward into the modern era of computerized,

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<sup>6</sup> Buccacio, Katherine, "[Republicans Look to Ease PE Regulatory Burden](#)", Private Equity Manager, January 13, 2015; Morgenson, Gretchen, "[Private Equity's Free Pass](#)", New York Times, September 27, 2014.

<sup>7</sup> Securities and Exchange Commission, "[No-Action Letter Re M&A Brokers](#)", January 31, 2014 [Revised February 4, 2014].

<sup>8</sup> Securities and Exchange Commission, "[21<sup>st</sup> Century Disclosure Initiative, Toward Greater Transparency: Modernizing the Securities and Exchange Commission's Disclosure System](#)", January 2009; Securities and Exchange Commission Investor Advisory Committee, "[Recommendations of the Investor as Owner Subcommittee Regarding the SEC and the Need for the Cost Effective Retrieval of Information by Investors](#)", July 25, 2013.

machine-readable information. Such steps could significantly improve financial sector transparency.

**HR 1847** would eliminate Dodd-Frank requirements that derivatives clearinghouses and data repositories indemnify the government for any litigation costs resulting from information sharing arrangements. AFR supports this legislation.

For some years AFR has been concerned with the slow pace at which domestic and international regulators are implementing derivatives data reporting mandates under the Dodd-Frank Act. The requirement that derivatives data be reported to regulators in a form that can be aggregated and used to measure total risk exposures across the financial system is an important part of the improved capacity to monitor systemic risk that should be created by new financial regulations. Clear, consistent, and usable derivatives data would be extremely beneficial to both banking and market regulators in controlling risk, and could create important indirect benefits for financial institutions themselves, many of which still face issues in their own internal systems for aggregating risk exposures.

Unfortunately, progress in derivatives data reporting has been slow, and some of the data collected does not appear to be in a form that can be aggregated. There are many reasons for this slow progress, but it is clear that the ability to share derivatives data between different national regulators and data repositories is crucial for effective data reporting. It appears that the indemnification requirements in Dodd-Frank are creating a barrier to such information sharing. The replacement of these indemnification requirements with a simpler confidentiality agreement, as proposed in HR 1847, would be beneficial in encouraging needed sharing of derivatives data between different jurisdictions and entities. We thus favor this legislation.

Thank you for the opportunity to express our views on this legislation. Should you have additional questions on this issue, please contact Marcus Stanley, AFR's Policy Director, at [marcus@ourfinancialsecurity.org](mailto:marcus@ourfinancialsecurity.org) or 202-466-3672.

Sincerely,  
Americans for Financial Reform