July 23, 2019

Secretary
Securities and Exchange Commission
100 F Street NW
Washington, DC 20549-1000

RE: Proposed Rule Amendments and Guidance Addressing Cross-Border Application of Certain Security Based Swap Requirements (RIN 3235-AM13, File No. S7-07-19)

To Whom It May Concern:

The Americans for Financial Reform Education Fund (AFR Ed Fund) appreciates the opportunity to comment on the above referenced Proposed Rules (the "Proposal") concerning the Security and Exchange Commission's (SEC or Commission) application of Dodd-Frank Title VII rules concerning security based swaps (SBS) to cross border transactions. Members of AFR Ed Fund include consumer, civil rights, investor, retiree, community, labor, faith based, and business groups.[1]

At the very beginning of this Proposal the Commission states the fundamental issue raised by weakening the "arranged, negotiated, and executed" (ANE) test as it applies to de minimis provisions for dealer designation:

> "The use of the ''arranged, negotiated, or executed'' test in the context of the security-based swap dealer de minimis counting provision particularly plays an important role in helping to prevent entities from using booking practices to avoid registering as security-based swap dealers, despite being engaged in security-based swap dealing activity in the United States."

Unfortunately, having stated the issue, the Commission then proceeds to outline exemptions to aggregation rules that will create precisely this problem.

The ANE test for de minimis positions – the requirement to count positions arranged, negotiated and executed in the United States toward the de minimis threshold for SBS dealer registration – was created exactly to ensure that SBS dealers conducting substantial business in the United States would have to register under U.S. law.

[1] A list of coalition members is available at: http://ourfinancialsecurity.org/about/our-coalition/

As the Commission stated in its original 2013 cross-border proposal:[2]

> "many of a non-U.S. person's transactions conducted within the United States that arise out of its dealing activity may also be transactions with U.S. persons, and thus would already be counted for purposes of the de minimis threshold. However, requiring non-U.S. persons to include in their de minimis calculations only transactions with U.S. person counterparties would enable such persons to engage in significant amounts of security-based swap dealing activity within the United States without Commission oversight as a security based swap dealer, so long as the dealing activity were limited to non U.S. persons. This would be the case if the potential dealer operated out of a branch, office, or affiliate, or utilized a third-party agent acting on its behalf within the United States, or merely directed its dealing activity to non-U.S. persons that themselves operate out of the United States, either through branches, office, or affiliates, or by utilizing third party agents"

In our comment on this original 2013 proposal, AFR opposed the overly restrictive definition of U.S. person under the proposal, specifically the exemption of foreign subsidiaries of U.S. persons that were not formally guaranteed by the U.S. parent.[3] We pointed out that despite the lack of a formal guarantee, credit and liquidity risks from non-guaranteed foreign subsidiaries of global U.S. banks would undoubtedly affect the U.S. entity as a whole, including its U.S. operations. For this reason, we opposed an exemption of foreign subsidiaries from the U.S. person definition. However, we also pointed out that given the narrow definition of U.S. person under the rule, the inclusion of ANE transactions in the de minimis count was an absolutely crucial protection to include in the rule.

The ANE test immediately came under fire from industry lobbyists and was revised to ease compliance. However, the Commission maintained the test in the 2016 Final Rule. It recognized that given the loose definition of "U.S. person" in the cross-border rules, it was absolutely crucial to include transactions that were ANE in the United States toward the de minimis threshold in order to ensure that SBS dealers active in the U.S. market were actually registered as such under U.S. law. As the Commission stated in the 2016 Final Rule covering cross border issues in the de minimis threshold:[4]

> "We believe that not requiring non-U.S. persons to count these [ANE] trades toward their de minimis thresholds would significantly impair the effectiveness of the Title VII dealer framework….even U.S.-based financial groups may opt to book their security-based swap transactions in non-U.S. persons in response to regulation or to competitive disparities between U.S. persons and non-U.S. persons. Given these dynamics, failure to require non-U.S. persons to count the transactions encompassed by the final rule toward the dealer de minimis thresholds…would permit financial groups that have a security-

[2] 78 FR 3100, https://www.govinfo.gov/content/pkg/FR-2013-05-23/pdf/2013-10835.pdf
[3] https://www.sec.gov/comments/s7-02-13/s70213-54.pdf
[4] https://www.govinfo.gov/content/pkg/FR-2016-02-19/pdf/2016-03178.pdf

based swap dealing business to avoid registering non-U.S. persons that engage in security-based swap dealing activity in the United States. As long as a non-U.S. person limited its dealing activity with U.S. persons to levels below the dealer de minimis thresholds, it could enter into an unlimited number of transactions connected with its dealing activity in the United States without being required to register as a security based swap dealer."

The 2016 Final Rule replied in exhaustive detail to the industry objections to being required to count ANE transactions toward the de minimis threshold. It also provided extensive analysis of the security-based swap market, analysis which demonstrated how it is a fully globalized market in which major SBS dealers, including those in U.S. based financial groups, could easily avoid swap dealer designation for large shares of their U.S.-related business if permitted to omit swaps that were booked in non-U.S. subsidiaries from being counted toward designation.

Yet the changes to Rule 3a71-3 in this Proposal would, by exempting swaps that were ANE in the United States but booked in non-U.S. subsidiaries from the de minimis threshold, create exactly the situation the Commissions own staff warned about in previous proposals and in the 2016 Final Rule. There has been no change in circumstances since 2016 warranting this complete reversal of the Commission's position:

- Since the Commission's SBS framework has not even been implemented, there is no new evidence introduced from concrete practical experience in implementing the regulations that would weight against the previous ANE framework.

- At several points in this Proposal the Commission refers to harmonizing cross-border rules with the Commodity Futures Trading Commission (CFTC). However, the CFTC's cross-border swaps rules are still essentially the same as they were in 2016. In any case the changes in this Proposal do not align the SEC and CFTC cross-border frameworks, since the CFTC rules force aggregation of cross-border swaps for de minimis purposes in order to prevent swap dealers with significant connections to the U.S. market from avoiding designation, which this Proposal would not do.[5]

- Some other jurisdictions, particularly in Europe, have moved forward with some swaps-related rules since 2016, for example by adopting regulatory technical standards under EMIR. But there is no analysis of these changes to demonstrate that they offer protections that were not available in 2016 and (more importantly) are equivalent to the protections offered in U.S. law. Further, the situation in the U.K. and major European jurisdictions has become more unstable since Brexit, which is nowhere mentioned in the Proposal.

[5] See CFTC Regulation 1.3(ggg)(4) which requires aggregation of the total notional value of swap dealing transactions entered into by all affiliates of the entity under common control when determining volumes to be compared to the de minimis threshold.

- The economic analysis in the Proposal does not offer any new evidence to overturn the findings in the 2016 Final Rule. In its discussion of "Title VII Programmatic Costs and Benefits", the analysis simply asserts that protections such as the "listed jurisdiction" requirement (discussed below) will ensure prudential safeguards for swap dealers, despite the explicit statement in the Proposal that designation as a "listed jurisdiction" will not require comparable rules to U.S. standards. The analysis also asserts that the changes in the Proposal will reduce market fragmentation and increase competition. This is in direct opposition to the analysis in the 2016 Final Rule which found that permitting non-U.S. firms to conduct large amounts of transactions that were ANE in the U.S. without being designated as U.S. dealers would exacerbate fragmentation and create competitive imbalances and distortions. Yet no clear reason for the reversal is given.

After considering the lack of justification for the complete change in direction between the 2016 Final Rule and the current Proposal, it is hard to avoid the conclusion that what has changed is not any new evidence or experience, but simply the change in presidential administration and a concomitant change in political pressures on Commission staff.

The Commission freely admits that the exemptions to the ANE requirement in this Proposal will lead a substantial number of participants in the highly concentrated and globalized interdealer SBS market to avoid registration as U.S. dealers by booking their swaps in non-U.S. subsidiaries. This includes, again by the Commission's own admission, current U.S. dealing entities that will change their booking practices to book ANE swaps in foreign subsidiaries and thus avoid registration as dealers. The Commission finds 12 such entities in its examination of current DTCC data and then (arbitrarily) assumes that as financial institutions optimize to the new rules this number would double to 24. Strikingly, the analysis does not include any estimate of the total fraction of the global SBS market, or of SBS transactions with any nexus to the U.S., would flow through entities that took advantage of the ANE exemption to conduct transactions in the U.S. without being designated as U.S. derivatives dealers. However, given the concentrated nature of the SBS market we suspect it would be large.

The absence of Title VII dealer regulation of entities operating in the U.S. market would of course reduce the extent to which Title VII protections under U.S. law applied to the SBS market. The Proposal advances various mechanisms to mitigate the increased risk from this reduction in oversight of the derivatives market. Most prominently, the Proposal would require that such swaps are booked in subsidiaries located in so-called "listed jurisdictions". However, the Proposal is explicit that the Commission would not be required to find that the regulatory regime in a listed jurisdiction is comparable to U.S. regulation. Instead, designation as a listed jurisdiction is completely at the discretion of the Commission, which "may conditionally or unconditionally determine" which jurisdictions qualify based on a vague public interest standard. While a few criteria are set forward, such as the existence (but not the stringency) of capital and margin standards in the jurisdiction, and the effectiveness of the supervisory compliance

program in the jurisdiction, Commission consideration of these factors is completely optional.[6] Thus, by no means would regulation in a listed jurisdiction guarantee regulatory protections comparable to U.S. oversight under Title VII of Dodd-Frank.

There are various other protections recommended in the options offered under the Proposal, including requirements that the SBS dealing operate through a U.S. registered broker-dealer and that the Commission have access to books and records of the entity making use of the exemption. However, these protections also would not guarantee protections in any way comparable to those mandated under Title VII of Dodd-Frank. Further, these alternatives were explicitly considered and rejected by the Commission in the 2016 Final Rule, as not providing adequate protection against the risks created by permitting dealing activity that is ANE in the United States to be exempted from the de minimis threshold.

The changes in this Proposal, specifically the new exemptions to the ANE test for the swap dealer de minimis threshold, would thus substantially reduce and in many areas negate the public benefits of SBS dealer designation under Title VII. We are continuing to review the complexities of this Proposal and may offer further comment in the future. However, we strongly oppose the sweeping exemptions to the ANE test and do not believe the Commission has met the burden of justifying these radical changes to the 2016 Final Rule.

Thank you for the opportunity to comment on the Proposal. If you have questions, please contact Marcus Stanley, AFR's Policy Director, at 202-466-3672 or marcus@ourfinancialsecurity.org

Sincerely,

Americans for Financial Reform Education Fund

[6] See the new paragraph d(v) added to 240.3a71-3 in the Proposal, regarding "subject to the regulation of a listed jurisdiction", on 84 FR 24292 of the Proposal