

# Uncertain times

## President Donald Trump may have his sights set on deregulation but a full repeal of title VII looks unlikely

One might think that the stated intention of US president-elect Donald Trump and Republicans in the US Congress to roll back the Dodd-Frank Act means that the Trump administration is likely to substantially reduce the regulation of derivatives under title VII of Dodd-Frank. It is early in the day, and the policies of the president-elect may be unpredictable. However, there are reasons to believe that his administration's approach to modifying derivatives regulation may rely more on the scalpel than on the sledgehammer. Among those reasons are the international basis for many of the primary derivatives markets reforms, the paucity of changes to title VII contained in the draft bill that Republicans are touting to amend Dodd-Frank, and the apparent views of Commodity Futures Trading Commission (CFTC) Commissioner J. Christopher Giancarlo, who has been identified as the frontrunner to chair the CFTC under the Trump administration.

Title VII of Dodd-Frank brought about unprecedented regulation of the derivatives markets. The aims of the Title VII reforms included reducing systemic risk (by requiring margin and mandatory clearing for many transactions), increasing market transparency (by requiring transaction reporting and requiring swap dealers to register with the CFTC), and levelling the playing field for market participants (by requiring dealers to adhere to business conduct standards and to execute many transactions on facilities capable of providing pre-transaction price transparency).

Significantly, many of the most important reforms contained in title VII were agreed by the G-20, and many G-20 countries have implemented – and are still implementing – those reforms. The G-20 leaders agreed in concept to clearing, transaction execution and reporting requirements at their September 2009 summit in Pittsburgh. They further agreed, at their 2011 meeting in Cannes, to instruct the Basel Committee on Banking Supervision and the International Organization for Securities Commission to develop international standards for the margining of uncleared derivatives. While this broad international consensus would

not prevent the Trump administration from undoing title VII's fundamental reforms, that consensus, and the apparent lack of a clear political case to act unilaterally in this area, appear to make a broad repeal of title VII relatively less likely.

Indeed, fundamental derivatives market reforms do not appear to be top of mind even for the Republicans interested in dismantling other aspects of Dodd-Frank. The Republican proposal to amend Dodd-Frank, known as the Financial Choice Act of 2016, which passed the House of Representatives Financial Services Committee in September of last year, doesn't exactly trim meekly around Dodd-Frank's edges. Among other significant reforms, it would provide a so-called off-ramp for certain banking institutions deemed to be well capitalised and well managed, exempting them from many Dodd-Frank capital and liquidity requirements. In addition, the bill would abolish the Volcker Rule, which restricts banks' proprietary activities, and would eliminate the orderly liquidation authority for financial companies contained in title II of Dodd-Frank.

But even with the bill's important proposed changes, and even though the proposed legislation would require certain reforms of the CFTC itself, the bill would require few modifications of derivatives regulations. In fact, far from undertaking wholesale changes to title VII's substantive requirements, the bill would require US regulatory agencies to clarify the application of, and harmonise, their existing substantive rules. One provision contained in the bill would require the CFTC to clarify which of its substantive requirements apply to which cross-border transactions and the criteria guiding any CFTC determination that a market participant may comply with comparable non-US rules. That provision would also limit the time for the CFTC to make such comparability determinations. The bill's other provision pertaining directly to the substance of title VII would require the CFTC and the SEC to issue new rules to resolve inconsistencies between the CFTC's rules for swaps and the SEC's rules for security-based swaps. In sum, the Financial Choice Act of 2016, if enacted, would leave untouched the vast bulk of title VII's substantive requirements.

Nor do the views of commissioner Giancarlo, reportedly the new administration's top choice to serve as the next CFTC chairman, appear to support a fundamental undoing of title VII or the CFTC's rules thereunder (with the exception of the CFTC's trade execution rules). Instead, his publicly-stated views appear to favour the type of changes that appear the Republican bill, aimed at fostering greater clarity in the application of existing substantive regulations rather than dismantling those regulations. In dissenting last May from the CFTC's approval of rules pertaining to the cross-border application of the commission's margin rules, commissioner Giancarlo characterised the CFTC's approach as 'overly complex, unduly narrow and operationally impractical'. However, he wrote, it was his support of the G-20 reforms that accounted for his concerns. Instead of instituting such complex and impractical rules, he wrote, the CFTC should have built upon the strong foundation for mutual recognition of foreign regulatory regimes created by G-20 commitments, including the Pittsburgh accord's commitment to 'raise standards together so that our national authorities implement global standards consistently in a way that ensures a level playing field and avoids fragmentation of markets, protectionism, and regulatory arbitrage'.

As CFTC chairman, Commissioner Giancarlo would likely be inclined to significantly change the CFTC's execution rules, which are intended to effectuate the G-20 understanding that derivatives, where appropriate, should be traded on exchanges or electronic trading platforms. In a 2015 white paper, commissioner Giancarlo roundly criticised those rules, which he described as 'highly over-engineered' and a threat to market liquidity. However, the white paper described itself as 'pro-reform, and as a defense of the letter and spirit of Dodd-Frank, and on its face it gives little reason to think that its author would seek generally to dismantle the fundamental title VII reforms. Commissioner Giancarlo has also opposed the CFTC's controversial position limit rules, which have not yet been finalised. He has sponsored the CFTC's Energy and Environmental Markets Advisory Committee, which early last year released a report recommending that the commission's proposed position limit rules not be finalised in their then-current form. After criticism from senator Elizabeth Warren and others, commissioner Giancarlo withdrew that report.

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