March 7, 2008

The Honorable Mike Crapo
239 Dirksen Senate Building
Washington, DC 20510

Dear Senator Crapo,

The Securities Industry and Financial Markets Association ("SIFMA")[1] thanks you for your letter of February 5 and is pleased to offer the Senate Republican Capital Markets Task Force our recommendations to enhance the competitiveness of the U.S. capital markets. Although America's capital markets have long been the fundamental engine for economic growth domestically and internationally, since the federal securities laws were enacted nearly 75 years ago we believe that various legal and regulatory changes are necessary to maintain our nation's preeminent status.

Specifically, SIFMA encourages Congress and regulators to adopt proposals in the following areas: 1) financial regulation; 2) securities litigation; 3) tax policy; 4) visa and immigration procedures; and 5) international trade. This letter details specific recommendations in each of the enumerated areas that are designed to increase the efficiency of capital markets, promote investor protection, and create a robust, reasonable system of oversight.

I. Financial Regulation

The United States has long had the world's deepest, fairest and most vibrant capital markets. This success is due in large part to efforts to maintain a strong regulatory structure that fosters innovation and competition while protecting investors. The public's trust that all market participants adhere to regulatory principles, vigorously and fairly applied, has contributed considerably to the integrity, strength, and stability of our markets.

However, while the capital markets and those participating in them have moved boldly into the new century, the United States has not made substantial changes to its regulatory structure to address the increasingly global nature of financial markets. Over the last several decades, technological advances, shifting demographic trends, new forms of competition, and rapid globalization have transformed the financial services landscape and made it truly global, integrated and interconnected. Many recent reports have found that regulatory burdens and legal risk have driven significant capital markets activity

[1] The Securities Industry and Financial Markets Association brings together the shared interests of more than 650 securities firms, banks and asset managers. SIFMA's mission is to promote policies and practices that work to expand and perfect markets, foster the development of new products and services and create efficiencies for member firms, while preserving and enhancing the public's trust and confidence in the markets and the industry. SIFMA works to represent its members' interests locally and globally. SIFMA has offices in New York, Washington D.C., and London and its associated firm, the Asia Securities Industry and Financial Markets Association, is based in Hong Kong.

away from U.S. markets to non-U.S. exchanges.[2] In light of these findings, SIFMA strongly believes that the U.S. regulatory regime for financial institutions needs both substantive and structural reforms that would shift regulation toward a regulatory approach based on principles and prudential regulation, simplify the regulatory oversight structure, and modernize regulation of cross-border activities of global firms and exchanges.

A. Principles-Based and Prudential Regulation

The current rules-based regulatory approach for financial services in the United States relies on outdated, overly broad, and/or unduly burdensome rules, thereby impeding our ability to compete globally, raise capital, provide consumers the widest range of choice possible, and perform other critical services for investors. As a result, SIFMA believes a shift from a rules-based regulatory approach to a more principles-based approach accompanied by prudential regulation will improve regulatory compliance, increase firms' ability to compete and respond quickly to new market developments, and enhance investor protection.

Under a principles-based approach, the regulators should develop a core set of high-level principles or objectives to guide proper behavior.[3] These fundamental principles should be crafted so they are flexible enough to adapt to new products and evolving market conditions while also providing enough direction for firms to comply with the principles. We agree with Federal Reserve Board Chairman Bernanke's recent comment that, "a consistent, principles-based, and risk-focused approach that takes account of the benefits as well as the risks that accompany financial innovation" is an effective way to protect investors while maintaining the integrity of the marketplace.[4]

The move toward a principles-based approach to regulation should be paired with the implementation of more prudential regulation of the financial industry. The essence of prudential regulation is an ongoing, open, and constructive dialogue between the regulator and the regulated firm. Under this approach, regulated firms may be confident that they can discuss specific issues and questions with their regulators and that the regulators will be willing to provide useful and timely advice as to how to comply with relevant laws and regulations.

B. Structural Reform

In the United States, many different regulators with different mandates and approaches to regulation govern the financial industry. This patchwork of regulatory oversight imposes an unnecessary drag on the competitiveness of U.S. firms, both within our borders where similar, competing institutions are subject to differing regulatory requirements regardless of the similarities in

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[2] *See Interim Report of the Committee on Capital Markets Regulation,* Committee on Capital Markets Regulation, (November 2006); *Sustaining New York's and the US' Global Financial Services Leadership* (January 2007); *Report and Recommendations,* Commission on the Regulation of U.S. Capital Markets in the 21st Century (March 2007).

[3] For current examples of principles-based regulation, *see* Section 5(d) of the Commodity Exchange Act, 7_U.S.C. § 7(d) and Part 38 of the CFTC's regulations (setting forth 18 core principles) and High Level Standards, FSA Handbook, http://fsahandbook.info/FSA/html/handbook/ (Financial Services Authority's high level principles adopted when it implemented a principles-based approach).

[4] *See* Ben S. Bernanke, Federal Reserve Board Chairman, Remarks at the Federal Reserve Bank of Atlanta's 2007 Financial Markets Conference, Sea Island, Georgia (May 15, 2007), at http://www.federalreserve.gov/boarddocs/Speeches/2007/20070515/default.htm.

their product offerings and services and globally where non-U.S. competitors do not face the same patchwork of competing regulators. Moreover, the complicated structure may lead to very different regulatory protections for investors receiving similar services.

SIFMA advocates simplifying and reforming the structure to maximize oversight efficiency and effectiveness. As a general matter, we recommend reducing the number of financial regulators, ensuring that comparable entities are subject to comparable standards, and creating a framework in which each financial institution is supervised by just one primary regulator. A first step toward achieving these goals is the consolidation of the Commodities Futures Trading Commission ("CFTC") and the Securities and Exchange Commission ("SEC") in order to begin simplifying the patchwork of regulatory oversight.

C. Cross-Border Regulatory Modernization

SIFMA strongly supports the SEC's ongoing efforts to modernize regulation of cross-border activities of broker-dealers and exchanges operating globally. Overall, these efforts include new approaches to cross-border regulation, including enhanced cooperation with non-U.S. regulators, potential recognition of foreign regulatory regimes and much-needed reforms to existing exemptive rules. As an immediate step, SIFMA advocates significantly redrafting Rule 15a-6 under the Securities Exchange Act of 1934[5] to permit sophisticated investors below the $100 million threshold to obtain direct access to non-U.S. broker-dealers. Another important focus would be the elimination of regulatory distinctions that limit trading of portfolios containing both U.S. and non-U.S. securities.

A more long-term cross-border regulatory modernization effort involves developing a "mutual recognition" framework that would recognize comparable regulatory regimes in other countries. Regulators in a number of countries have adopted or are moving toward such a regulatory model under which firms would be allowed to operate in foreign countries under their home country's regulation as long as the foreign country had recognized such regulation as adequate. Mutual recognition would elevate global supervisory practices, promote collaboration among like-minded regulators, improve the efficiency of cross-border regulation, and enhance investor protection. Importantly, mutual recognition could also increase international investment opportunities and enhance risk diversification in the United States at a time when our economy could benefit significantly from new investment and liquidity.

II. Securities Litigation

America's securities fraud litigation system needs reform. Several studies have concluded that the threat of shareholder lawsuits against directors of U.S. listed companies has deterred international companies from listing in the United States.[6] Moreover, foreign company executives frequently cite America's unpredictable and expensive legal lottery as a major impediment to listing securities in the United States.

Congress and the SEC should take steps to improve the securities class action system, while preserving investors' rights of action against issuers that engage in fraud. SIFMA believes the following

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5 In this regard, SIFMA is encouraged by recent dialogue with the SEC concerning reform of Securities Exchange Act Rule 15a-6 to better reflect the realities of conducting cross-border securities business.

6 *See* Studies cited in footnote 2 above.

recommendations would help to dispel some of the negative perceptions of the U.S. litigation system:

A. Hold SEC Shareholder Litigation Roundtable. The SEC should honor its commitment to hold a roundtable in early 2008 on the topic of shareholder litigation with a view toward recommending realistic alternatives and improvements to the current system. As part of the roundtable discussions, the SEC should evaluate the effectiveness of the *Private Securities Litigation Reform Act of 1995* (PSLRA), as well as consider whether any additional legislative reform is necessary to better achieve the goals of investor protection and capital formation.

B. Update Gatekeeper Liability Standards. The SEC should amend Rule 176 of the Securities Act of 1933 to address the current mismatch between underwriters' traditional liability standards and the realities of today's capital markets.

C. Give Defendants Right to Appeal Denial of a Motion to Dismiss. Congress should create parity between plaintiffs' and defendants' appellate rights by giving defendants in securities class actions the express right to appeal a trial court's denial of a motion to dismiss. In a securities class action, the motion to dismiss is the most critical stage of the process, because if the motion to dismiss is denied then the claim is almost always settled thereafter. Currently, plaintiffs have an automatic right of appeal if the motion to dismiss is granted, but defendants have no right of appeal if the motion is denied.

D. Cap Liability for Non-U.S. Issuers. Congress should cap liability for non-U.S. private issuers in proportion to their degree of exposure to the American markets so their potential liability would be in direct proportion to their U.S. capital raising and other U.S. business activities. Such a cap would discourage class action suits against foreign issuers that seek damages unrelated to U.S. markets or U.S. investors.

E. Defeat Anti-Arbitration Legislation. Congress should defeat the *Arbitration Fairness Act* (H.R. 3010/S. 1782). This bill would retroactively declare unenforceable potentially millions of existing arbitration provisions – and prohibit the use of pre-dispute arbitration agreements – in consumer, employment, brokerage, and franchise contracts. If passed, this legislation would effectively raise the cost of dispute resolution for both consumers and businesses; eliminate the ability of consumers and employees to obtain redress for many types of wrongdoing; and increase the caseload of our already overburdened courts.

SIFMA believes that these litigation reforms would reduce litigation costs while preserving investor rights and protections. As a result, they would change the cost-benefit calculations of companies deciding whether or not to list on a U.S. exchange by making listing on the U.S. markets more attractive.

III. Tax Policy

A. Make Capital Gains and Dividends Tax Rate Reductions Permanent

SIFMA strongly supports making the dividend and capital gains tax rate reductions enacted in the *Jobs and Growth Tax Relief Reconciliation Act of 2003* permanent. Making these tax cuts permanent will provide economic certainty to taxpayers and the financial markets, and will help all Americans continue saving for retirement, education and homeownership. The lower rates have contributed directly to a period of sustained economic growth and job creation. Immediately after the enactment of the rate reductions in 2003, quarterly GDP growth increased to 7.5 percent – the highest quarterly growth rate in nearly 20 years. In addition, the U.S. economy has created 8.7 million jobs since enactment of the tax cuts. Allowing the rates to expire in 2010 will be a direct tax increase on American families at a time when taxpayers are already facing turmoil in the housing markets and reduction in available credit.

Taxpayers have also reaped the benefits of more and larger dividends as a result of the tax rate reductions. Beyond the direct benefit of lower taxes on dividends paid, the 15 percent tax rate also increased shareholder value whether the stocks were held directly or through mutual funds. Total equity market value increased $4.2 trillion between May 2003 and the end of November 2004.

The impending expiration of the lower rates is already contributing to market uncertainty and instability. As the expiration date gets closer, shareholders may sell their stocks to take advantage of the lower rates. A stock sell off could have a very damaging effect on the stock market. Given the important role of savings in long-term economic growth, the United States should not be increasing taxes on saving and investment or compounding the deleterious effects of double taxation.

B. International Taxation

Similar uncertainty exists in the international taxation arena since the Active Financing Exception (AFE) under Subpart F is scheduled to expire at the end of 2008. This exception should be made permanent. It allows U.S.-based manufacturers and financial services firms to defer tax on the active business income they earn in their overseas operations until that income is repatriated to the United States – a benefit every other industry already receives on a permanent basis under current law.

If the AFE is not extended, U.S.-based financial services firms will face a steep tax increase beginning next year. This looming tax increase is already affecting firms' business decisions. U.S.-based financial services firms need certainty in order to price their products overseas and to compete with foreign competitors. If U.S. firms cannot compete overseas because their income is taxed twice, the void will be filled by foreign competitors. Firms need certainty more than ever in today's highly competitive and unstable financial marketplace.

IV. Visa and Immigration Process

U.S. financial services firms must be able to attract the highest caliber of talent, both domestically and overseas, to stay competitive globally. Long a hallmark of the industry, the ability to move employees and clients freely around the globe has been an essential component of the success of our financial services sector. SIFMA agrees with New York City Mayor Michael Bloomberg and New York Senator Charles Schumer that the cumbersome visa application process and caps on H1-B visas have made it harder to recruit global talent and have negatively affected the competitiveness of the U.S. capital markets.[7]

While U.S. citizens will continue to be the most significant source of employees for the U.S. financial services industry, highly skilled foreign nationals are a vital source of unique ideas and expertise in new markets and regions. Competition from both developed and developing countries for bright, capable foreign personnel, particularly students, is becoming fierce. The European Union, Australia, Canada, and South Korea have been actively recruiting foreign talent and attempting to lure foreign students away from the United States. We can no longer assume that the United States will be able to, by default, attract the most talented students. To retain our position of leadership, we must cast our net ever wider and welcome gifted individuals in *all fields* of study.[8]

In order to reclaim our position of leadership, SIFMA recommends the adoption of several initiatives: 1) reduce administrative hurdles in the visa process to facilitate short-term visits by foreign nationals for road shows, conferences, training and other similar events; 2) increase the number of H1-B visas that enable skilled and experienced foreign nationals to work in the United States for specified periods of time; and 3) extend Optional Practical Training (OPT) visas beyond the STEM category (Science, Technology, Engineering, and Math) from one year to 29 months. In light of the current limitations on acquiring H1-B visas, extending OPT would allow firms to fill gaps in employment and continue building expertise of new employees. Taken together, these reforms would ensure that companies have the ability to attract, train, move, and retain the talented and specialized employees they need to compete globally.

V. International Trade

Over the last decade, the U.S. economy and securities markets – while still the largest in absolute terms – have seen their share of the global pie shrink. More than two-thirds of the world's GDP, half of the world's equity and debt markets, and 95 percent of the world's consumers are located outside the United States. Clearly, the continued well-being of America's financial services sector is directly linked to its ability to sell its products in foreign markets. Indeed, in exporting a record $37.1 billion of services (excluding insurance) and generating a trade surplus of $28.6 billion in 2006, the U.S. financial services industry is already strongly committed to doing business with foreign markets. Foreign individuals, institutions and governments eagerly seek cutting-edge services and products – such as portfolio management, advisory work in corporate finance activities, and global custody services – that U.S. financial firm's offer.

To increase our competitiveness, economic growth, and status as a global economic leader, SIFMA urges Congress to work towards the reduction and elimination of the barriers in China's capital markets; ratify the Free Trade Agreements ("FTAs") with Korea, Colombia, and Panama; and advocate for the successful conclusion of the Doha Round of the World Trade Organization ("WTO") financial services negotiations.

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7 *See Sustaining New York's and the US' Global Financial Services Leadership* cited in footnote 2 above.

8 Canada, for example, has allowed eligible foreign students to work up to two years in their chosen field of study since 2006.

A. China

Many of the best future growth opportunities lie in "non-U.S." markets. For example, markets such as Brazil, India and China are projected to be among the largest in the world by 2050. Although U.S. investors and corporations have begun tapping these new markets, U.S. securities firms will need greater and fairer access to best serve their clients' international focus.

In particular, China has been identified as the largest single emerging market opportunity in the world, yet U.S. securities firms cannot fully access China's capital markets. U.S. securities firms can participate in the securities business in China, but are limited to minority-owned joint ventures with foreign ownership capped at just 33 percent. In addition, these foreign-owned joint ventures cannot engage in the full range of securities activities. China has not made any commitments in the securities sector for further increases in foreign ownership in the Doha Round of WTO negotiations. SIFMA recommends seeking such commitments from China since fair access to this rapidly growing market is important to U.S. securities firms seeking growth opportunities.

B. FTAs

FTAs are an important building block of opening foreign markets to U.S. business, consumers, and investors. Ratifying FTAs with Korea, Colombia, and Panama will create jobs, bolster economic growth, and signal our intention to remain the global leader in promoting open trade and investment worldwide.

The U.S.-Korea FTA is particularly important to the securities industry because Korea's capital market is the largest of any emerging market country when measured by market capitalization and the value of stocks traded. Indeed, for the securities industry, Korea represents a more significant market than any other recent FTA partner. The U.S.-Korea FTA will eliminate many market access and national treatment barriers as well as the more discreet administrative and regulatory transparency barriers that, if left in place, would severely limit the value of any of Korea's FTA financial services commitments. The robust and comprehensive financial services commitments in the U.S.-Korea FTA will expand commercial opportunities for U.S. firms, and add to the depth, vibrancy and liquidity of Korea's capital markets – an economic win-win situation for both countries. Accordingly, SIFMA strongly encourages ratification of the U.S.-Korea FTA as well as the FTAs with Colombia and Panama.

C. WTO

The Doha Round of the WTO provides U.S. negotiators with an opportunity on a multilateral basis to remove obstacles in foreign markets that impede the competitiveness of U.S. firms and hamper U.S. economic growth and job creation. Liberalization of trade in financial services in general – and in capital markets-related services in particular – benefits both developed and developing countries by enhancing and strengthening capital market efficiency, increasing financial sector stability, and bolstering economic growth. Broadly, SIFMA recommends seeking commitments during the Doha Round of the WTO that: 1) provide for the ability to establish a commercial presence in choice of corporate form and the same treatment to those firms as accorded to domestic firms; 2) expand the ability to engage in cross-border transactions with sophisticated investors; and 3) promote regulation that is developed, adopted, and enforced in a transparent, non-discriminatory manner.

Conclusion

SIFMA applauds and thanks you for the important work you are doing as chairman of the Senate Republican Capital Markets Task Force. We share your goal of enhancing the competitiveness of the U.S. financial services industry to ensure America's economic prosperity and to keep high-paying jobs at home. We look forward to working with you, your Senate colleagues, regulators, and the Administration to implement these much-needed reforms in the areas of financial regulation, securities litigation, tax policy, visa and immigration procedures, and international trade.

Sincerely,

Richard Hunt
Senior Managing Director
Government Affairs

Scott DeFife
Senior Managing Director
Government Affairs