SIFMA
Securities Industry and
Financial Markets Association

November 21, 2007

Submitted electronically

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Re: TREAS-DO-2007-0018

Dear Sirs:

The Securities Industry and Financial Markets Association[1] ("SIFMA") appreciates the opportunity to comment on the request by the Department of the Treasury ("Treasury Department") for comment regarding the regulatory structure for financial institutions.[2] SIFMA agrees with the Treasury Department that "it is important to continue to evaluate our regulatory structure and consider ways to improve efficiency, reduce overlap, strengthen consumer and investor protection, and ensure that financial institutions have the ability to adapt to evolving market dynamics."[3] The Treasury Department's inquiry is especially timely in light of the growing concern voiced by investors, market

1 SIFMA 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. It has offices in New York, Washington, D.C. and London and its parallel association, the Asia Securities Industry and Financial Markets Association, is based in Hong Kong. More information about SIFMA is available on its website at www.sifma.org.

2 72 Fed. Reg. 58,939 (Oct. 17, 2007).

3 Id.

participants, regulators, academics and others regarding the ability of U.S. firms to compete in the global economy.[4]

SIFMA has been a regular and active participant in the regulatory reform debates regarding financial regulation, presenting views and positions on issues ranging from state regulatory reform, to litigation reform, to cross-border reform and beyond. Therefore, we are pleased to provide our preliminary views on the need for regulatory reform in this letter. Indeed, we look forward to participating in the reform dialogue, including drafting a white paper addressing a wider range of issues related to regulatory reform.

A. Executive Summary

SIFMA believes that the U.S. regulatory regime for financial institutions is in need of both substantive and structural reform. Both are contributors to unnecessary regulatory burdens that adversely affect the competitive status of the regulated entities, which, in turn, disadvantages investors and consumers.

1. Substantive Reform

- Consider Competitive Effects. SIFMA believes that significant benefits would be achieved through a regulatory approach that specifically seeks to protect investors, strengthen competition, and promote safety and soundness.

- Embrace Principles-Based Regulation. SIFMA believes that a shift from a rules-based approach to regulation to a more principles-based approach should provide firms with the flexibility to respond appropriately to new market developments and innovations, without compromising investor protection. SIFMA emphasizes, however, that such a change in approach must be accompanied by the adoption of outcome-based supporting rules (where rules are needed), an open, constructive dialogue between the regulator and regulated, and an enforcement program focused on serious misconduct and fraud. In order to ensure that a principles-based approach does not become another layer of regulation, the principles should themselves not lead to new private litigation risk and communications with regulators during examinations should be protected as privileged.

- Enhance Efforts to Implement Prudential Regulation. SIFMA recommends that the regulators build upon current efforts to implement a more prudential approach to regulation. By "prudential regulation" we mean a consultative relationship between

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4 See, e.g., The Financial Services Roundtable, The Blueprint for U.S. Financial Competitiveness (2007), http://www.fsround.org/cec/pdfs/FINALCompetitivenessReport.pdf ("FSR Blueprint"); Commission on the Regulation of U.S. Capital Markets in the 21st Century, U.S. Chamber of Commerce, Report and Recommendations (March 2007), http://www.capitalmarketscommission.com/portal/capmarkets/default.htm ("Chamber of Commerce Report"); Interim Report of the Committee on Capital Markets Regulation (2006), http://www.capmktsreg.org/pdfs/11.30Committee_Interim_ReportREV2.pdf; Sustaining New York's and the US' Global Financial Services Leadership (2007), http://www.senate.gov/~schumer/SchumerWebsite/pressroom/special_reports/2007/NY_REPORT%20_FINAL.pdf ("Bloomberg-Schumer Report").

the regulators and regulated, where the regulators proactively assist the regulated in developing a robust control and compliance environment and in resolving potential issues without resorting to enforcement actions as a first step.

- Address Differences in Wholesale and Retail Markets Comprehensively. SIFMA urges the regulators to undertake a comprehensive effort to create one regulatory regime appropriate for wholesale markets and one appropriate for retail markets, thereby bifurcating the rules and regulations applicable to wholesale versus retail markets.

- Streamline Introduction of New Financial Products. SIFMA advocates eliminating the prior review process for new financial products that are subject to competitive market forces, and replacing it with a more flexible and streamlined approach that both protects investors and recognizes the competitive issues related to new products.[5]

2. Structural Reform

- Implement a More Effective and Efficient Regulatory Structure. SIFMA also believes that more effective and efficient regulation of financial institutions is likely to be achieved through a reduction in the number of financial regulators, the regulation of similar firms in a similar manner, and the creation of a framework in which each financial institution is supervised by only one primary regulator.

- Consolidate CFTC and SEC. SIFMA recommends the consolidation of the Securities and Exchange Commission ("SEC") and the Commodity Futures Trading Commission ("CFTC"), bringing the oversight of many financial products (whether or not characterized as securities or futures) under one agency in a principles-based and prudential regime.

- Evaluate Need for Additional Financial Regulation Reforms. SIFMA believes that more extensive financial regulation reforms involving not only the SEC and CFTC, but also the banking, state and insurance regulators may be warranted. SIFMA continues to analyze the costs and benefits of more comprehensive financial regulation reform beyond the proposed SEC/CFTC merger.

- Update Cross-Border Regulations. SIFMA advocates a phased and tiered approach to cross-border regulatory reform, which addresses pressing issues facing investors and markets under current law in the short term, and works toward broader reforms in the longer term.

[5] SIFMA's comments here concerning streamlining the product approval process where robust competitive forces are at work in the financial markets are not intended to encompass products such as market data, for which SIFMA does not believe there exists the same sort of meaningful competition. SIFMA separately has provided recommendations concerning regulatory reform for market data requirements in other comment processes. See, e.g., SIFMA submissions concerning In the Matter of NetCoalition, File No. SR-NYSEArca-2006-21.

B. Need for Substantive Regulatory Reform

The regulatory policies in place for financial institutions must effectively protect the safety and stability of the financial system and maintain high standards of both consumer and investor protection. To date, these two goals have been the primary focus of financial regulation. Given the role that innovation, entrepreneurialism and competition have played in our national economic success (including the many benefits that flow to investors, such as lower costs and greater choice), SIFMA believes that efficient and competitive capital markets must be viewed as key objectives, which together with safety and soundness and investor protection, should form the foundation of our U.S. financial markets.[6]

The current regulatory regime, however, may be affecting the U.S. markets' ability to compete globally, thereby impeding capital raising, consumer choice and other critical functions performed for investors. One issue with the existing rules-based mode of regulation is the continued presence of outdated, overly broad, and/or unduly burdensome rules. For example, "one size fits all" regulation (i.e., rules that fail to recognize the many important distinctions between different types of investors and different types of products) and rules that fail to take into consideration changes in financial services may limit innovation and competition without providing a concomitant benefit. Second, this disconnect within the rule set is exacerbated by the often adversarial nature of the oversight relationship. For example, addressing minor, technical or operational failures that do not cause investor harm through enforcement actions may serve to preclude an open, constructive dialogue regarding the issues at hand and misallocates resources toward responding to the enforcement action and away from new compliance efforts. As a result, SIFMA believes that the adoption of a more principles-based and prudential regulatory approach may address many of the concerns regarding the current regulatory system, thus enhancing both regulatory compliance and the competitiveness of U.S. financial institutions to the benefit of investors.

1. Principles-Based Regulation

Under a principles-based approach, the regulators should develop a core set of high-level principles or objectives to guide proper behavior.[7] The implementation of these fundamental principles should be crafted so as to be flexible enough to adapt to new products and evolving market conditions, while providing enough direction for firms to comply with the principles. As Federal Reserve Board Chairman Bernanke recently suggested, "a consistent, principles-based, and risk-focused approach that

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[6] Congress recognized the importance of the SEC's promotion of efficiency, competition and capital formation, in addition to investor protection, when it required the SEC to take into consideration these factors when rulemaking. See National Securities Markets Improvement Act of 1996, Pub. L. No. 104-290, § 106, 110 Stat. 3416, 3424-25 (1996).

[7] 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).

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.[8]

A principles-based approach, however, must be carefully implemented to avoid exacerbating the issues raised by the current rules-based approach. In particular, SIFMA believes that the move to principles-based regulation must be accompanied by outcome-oriented rules (where rules are necessary), an open dialogue between the regulator and regulated, and enforcement efforts focused on serious misconduct and fraud. Without these related changes, SIFMA is concerned that a principles-based approach could merely add another layer of regulation to the existing rules, a layer that is broadly stated, ineffectively explained by the regulators, and interpreted through enforcement actions.

Moreover, it is important that the principles themselves not lead to new private litigation risk and that communications with regulators during examinations are protected as privileged.[9] SIFMA does not believe that a principles-based system would be beneficial to any of the parties involved if it served to increase the litigation risk experienced by financial firms. Indeed, SIFMA has been a proponent of litigation reform for some time, especially with regard to securities litigation and class action suits.[10] SIFMA believes that such litigation reform is critical to ensuring the competitiveness of the U.S. markets.

SIFMA expects that a few broad principles will not be sufficient to guide the regulated entities as to appropriate and expected behavior; it appreciates the need to adopt specific rules, where warranted. To avoid the pitfalls of the current rules-based approach (<u>e.g.</u>, one size fits all regulation, or unnecessarily burdensome rules), SIFMA believes that any rules, insofar as possible, should be drafted more in terms of outcomes, performance or results rather than prescribed processes and inputs. For example, in prohibiting the "churning" of a client's investment account, a rule and its enforcement should look to whether or not brokers actually churned accounts, instead of mandating, for example, extensive supervisory and broker-training procedures aimed at preventing churning.[11]

2. Prudential Regulation

SIFMA believes that a move toward a principles-based approach to regulation should be paired with the implementation of more prudential regulation of the financial industry. Prudential regulation begins with 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 with the regulators specific issues and questions, and that the regulators will be willing to provide useful and timely advice as to how to comply with relevant regulations.

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[8] *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.

[9] <u>See</u> Chamber of Commerce Report, supra note 4, at 80.

[10] <u>See, e.g.</u>, Letter from J. Steve Judge, Senior Vice President, Government Affairs, SIA, to Hon. Thomas Daschle (July 9, 2002), http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/30598370.pdf.

[11] Interim Report of the Committee on Capital Markets Regulation (Nov. 30, 2006), http://www.capmktsreg.org/pdfs/11.30Committee_Interim_ReportREV2.pdf.

In keeping with this consultative relationship, the regulators will rely on a range of corrective measures to cure regulatory issues, rather than moving directly to an enforcement action for any violation, large or small. The regulators will evaluate the degree of any particular regulatory issue that arises, and turn to the most appropriate corrective measure to cure the problem. Minor or technical violations that do not cause true harm to investors, markets or others may be addressed through more informal remedial measures. In cases of material harm, however, the regulators will use a formal enforcement action. Indeed, it is imperative that the regulators continue their strong enforcement efforts to address material harm to investors or market integrity; such efforts are, and will continue to be, critically important to the effectiveness of the U.S. regulatory system.

The SEC successfully practices prudential regulation through its Consolidated Supervised Entity ("CSE") program.[12] The CSE program currently monitors the holding companies of five well-capitalized broker-dealers so that the SEC is better able to respond to financial or operational weaknesses in the whole entity, rather than focusing only on broker-dealer operations.[13] The CSE program provides benefits to both the regulators and supervised entities because while the regulators will learn more about the firms' procedures, the firms also can be more open with regulators about risks and deficiencies. Firms that participate in the CSE model often note the many benefits associated with the CSE program for investors, the firms and the regulators alike. SIFMA urges the SEC and other regulators to export the approach taken in the CSE context to all of its oversight activities.

SIFMA expects that expanding the prudential regulatory approach adopted in the CSE context, which includes an evolution in enforcement attitude and the development of a constructive working relationship between the regulated and regulator, should lead to heightened compliance within a competition-friendly framework. In particular, an open, cooperative problem-solving strategy for regulatory oversight is likely to ensure better compliance with regulatory requirements,[14] the regulators' better understanding of the regulated businesses, and a greater willingness by the regulated entities to engage in a constructive dialogue about potential problems with their regulators. Moreover, all constituents are more likely to have greater confidence in the resulting regulatory scheme.

3. Wholesale vs. Retail Markets

As part of the move to principles-based regulation and the effort to impose regulation only where necessary and in the most beneficial manner, a critical area for reform is the regulation of wholesale versus retail markets. The U.S. securities systems have operated for decades under legislation enacted when the U.S. markets and their regulation were dominated by concerns over the direct participation of retail investors in the markets. In the interim, the profile of market participation has fundamentally changed. Institutions are now far larger participants in the financial and capital

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[12] For additional information regarding the CSE program, see Consolidated Supervision of Broker-Dealers and Affiliates, http://www.sec.gov/divisions/marketreg/consupervision.htm.

[13] *See* Annette L. Nazareth, Commissioner, SEC, Remarks at the SIFMA Compliance and Legal Conference (Mar. 26, 2007).

[14] See, e.g., id.; Mary L. Schapiro, Chairman & CEO, FINRA, Remarks at the SIFMA Compliance & Legal Division's 38th Annual Seminar (Mar. 26, 2007); Richard G. Ketchum, CEO, NYSE Regulation, Inc., *You Say You Want a Revolution,* Remarks at the SIFMA Compliance & Legal Division's 38th Annual Seminar (Mar. 27, 2007).

markets.[15] The regulators have recognized this shift, and have adopted certain rules that acknowledge the sophisticated nature of institutional market participants. For example, the Financial Industry Regulatory Authority ("FINRA") has provided some regulatory relief to broker-dealers regarding their obligations to institutional customers in both the suitability and mark-up contexts.[16] SIFMA urges the regulators to expand upon these efforts and to undertake a comprehensive effort to create one regulatory regime appropriate for the wholesale market and one appropriate for the retail market, thereby bifurcating the rules and regulations applicable to wholesale versus retail markets as necessary.

As a preliminary part of such an effort, regulators must develop and employ a consistent standard for identifying what constitutes an "institutional customer."[17] SIFMA suggests the development of a universal definition that applies a bright line "investable assets" test, with the ability for investors that do not meet those eligibility criteria to be "approved" as wholesale investors based on such things as experience and sophistication, among other factors.

Once a definition is crafted, regulators should review and revise their rules to take into account the knowledge, background, sophistication and wherewithal of the customer as well as the different characteristics of markets (e.g., whether the market is essentially institutional, such as structured finance, over-the-counter derivatives and many parts of the fixed income market). On average, SIFMA expects regulators to provide greater flexibility in dealings with wholesale market participants due to the recognition that institutional clients generally are sophisticated enough to understand and assume risks that might not be appropriate for retail investors. One approach for dealing with the fact that wholesale investors do not need the same level of customer protection as retail investors is to provide wholesale investors with the ability to opt-out of certain protections, or to be presumed to have opted out unless the investor affirmatively "opts in" for the greater protection.[18]

4. New Financial Products

Similarly, the treatment of new products in the context of markets that are already competitive should be reexamined under a new principles-based approach.[19] Recently, product innovation has been one of the primary competitive forces driving the markets. Yet, U.S. regulators have been obliged to address these products within the confines of legislation that did not contemplate such innovations. As a result, the ability of financial institutions to compete has been hampered by restrictive or outdated rules regarding the introduction of new financial products. Not only does this adversely affect the

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15 See, e.g., Brian G. Cartwright, General Counsel, SEC, Remarks at The University of Pennsylvania Law School Institute for Law and Economics (Oct. 24, 2007), http://www.sec.gov/news/speech/2007/ spch102407bgc.htm.

16 See NASD IM-2310-3 (Suitability Obligations to Institutional Customers); NASD IM-2440-2 (Additional Mark-Up Policy for Transactions in Debt Securities, Except Municipal Securities).

17 For examples of the varied definitions of a wholesale investor currently in place, see, e.g., Rule 144A(a) under the Securities Act of 1933 (definition of qualified institutional buyers); and Rule 501(a) of the Securities Act of 1933 (definition of "accredited investor").

18 This approach would be consistent with the approach to client classification under the Markets in Financial Instruments Directive of the European Economic Union (known as "MiFID") which requires securities firms to categorize clients as either "retail" or "professional" and to take those categorizations into account in their compliance in certain areas including risk disclosures, best execution, and marketing and related communications. *See* Commission Directive 2006/73/EC of 10 August 2006.

19 See supra note 5.

financial institutions developing the products, but it also hurts investors by limiting the range of available investment options.

The current review process, which sometimes requires prior review and affirmative approval of the new product by a number of different groups within the same regulator or multiple regulators, delays the introduction of the products, without providing a significant regulatory benefit. Therefore, regulation that provides a flexible framework for providing necessary market and investor protections without prohibiting or restricting products by category is a preferable approach. For example, requiring notice, rather than approval, of new products may serve to enhance U.S. regulation and the competitiveness of U.S. markets, and to ensure consumer choice is not limited unnecessarily.

5. Implementation of Change

The move to a principles-based approach to regulation must be comprehensive, affecting the SEC as well as the self-regulatory organizations ("SRO"). The recent consolidation of the member regulation operations of NASD and NYSE into the new combined SRO, FINRA, and the resulting review of their respective rulebooks provides an excellent opportunity to shift away from prescriptive rules where appropriate, and implement a more principles-based approach to regulation. A single rulebook drafted using a principles-based approach should eliminate the duplicative, and sometimes conflicting, rules applicable to the many firms that are dual members of FINRA's predecessor organizations, NASD and NYSE Regulation, and should provide a more workable approach to SRO oversight. Moreover, as discussed below, the proposed combination of the SEC and CFTC and the ensuing harmonization of their operating statutes similarly would provide an opportunity to shift the focus to principles-based regulation.

C. Need for Structural Reform: More Effective Oversight through Fewer Regulators

1. Issues Raised by Current Regulatory Structure

The U.S. regulatory structure for financial institutions developed into its current form as a result of particular reasons from bygone eras. The structure has not kept pace with the many changes that have occurred in the financial industry, including changes related to technology, global competition, new products, and the increasing bifurcation of the retail and wholesale markets. As a result, the industry is plagued by too many regulators, with overlapping jurisdiction for the same conduct. It is time for a comprehensive reevaluation of the existing structure.

In the U.S., there is no single regulatory authority responsible for the oversight of all financial services. Instead, there are many different regulators, with different mandates, and different approaches to regulation. For example, on the banking side, the Federal Reserve Board regulates bank holding companies and insured state member banks; the Office of the Comptroller of the Currency regulates national banks (whether or not they are subsidiaries of a bank holding company); the Federal Deposit Insurance Corporation regulates state non-member banks that are insured by the Corporation (also whether or not they are subsidiaries of a bank holding company); and the Office of Thrift Supervision regulates federal and state chartered savings associations and their holding companies. Moreover, state banking regulators oversee non-insured state member banks, state thrifts and state credit unions. Correspondingly, the SEC regulates broker-dealers, and oversees certain holding companies. The SEC's oversight of broker-dealers is supplemented by the state securities regulators and the SROs (FINRA and the exchanges). Also, the Municipal Securities Rulemaking Board sets rules for municipal securities brokers and dealers. In addition, futures firms are regulated by the CFTC and National Futures Association. And, the insurance industry is regulated by 50 state insurance regulators.

The negative consequences of this patchwork of regulatory oversight are real and pervasive. Financial institutions are subject to duplicative, costly and unnecessary regulatory burdens, including multiple rulebooks, and multiple examinations and multiple enforcement actions for the same activity, that provide questionable benefits to consumers and the markets as a whole. In particular, this jumble of regulation imposes an unnecessary drag on the competitiveness of U.S. firms, both within the U.S. where similar, competing institutions are subject to differing regulatory requirements, regardless of the similarities in their product offerings and services, and globally where non-U.S. competitors do not face the same regulatory burdens. Moreover, the complicated structure may lead to very different regulatory protections for investors receiving similar services. For example, similar financial advisory services may be delivered to private retail clients via a broker-dealer, a trust, an investment adviser or an insurance agent, thereby subjecting similar advisory activities to widely disparate regulatory requirements. As a result, this structure imposes higher costs on investors, deprives them of investment opportunities and provides differing protection.

Simply enhancing regulatory cooperation between the many different regulators is not sufficient to address these issues. Although SIFMA advocates such cooperation where possible, as a practical matter, the cooperation happens more in theory than in practice and does not yield significant results. For example, such cooperation is often hindered by the individual agendas of the different regulators, sometimes self-imposed, sometimes imposed by political realities, and sometimes imposed by the agencies' governing statutes themselves.

In light of the issues raised by the current regulatory structure, SIFMA advocates simplifying and reforming the structure to maximize oversight efficiency and effectiveness. As a general matter, SIFMA recommends 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. Although SIFMA continues to evaluate how best to implement these three basic goals on a comprehensive basis across the financial industry, it believes that the first step toward these goals is the consolidation of the CFTC and SEC.

2. First Step: Consolidation of CFTC and SEC

The SEC regulates activities involving securities; the CFTC regulates activities involving commodity options, futures and futures options; and both agencies regulate securities-related commodity products. In the past, separate regulation of the securities and futures markets was useful because the two markets operated in dramatically different fashions and rarely interacted. Futures contracts primarily covered commodities and foodstuffs, not government securities, equities and currency. Today the "commodities" markets have evolved into markets primarily trading futures on financial instruments and options on those futures. The past distinctions between the commodities and securities markets have disappeared for the most part, leaving what many consider a single financial market.[20] Yet, the divided regulatory and statutory system remains intact. This bifurcated structure hampers the competitiveness of U.S. financial markets, impedes innovation and creates significant public policy concerns.

The bifurcated jurisdiction has created needless legal uncertainty as to the status of new financial products. U.S. financial participants regularly raise difficult issues regarding whether a particular instrument is a security or a futures contract. Any such novel derivative often must be vetted by the SEC and the CFTC as to its legal status, thereby resulting in significant delays in bringing the derivative to market as the two agencies try to decide which has jurisdiction over the product.[21] These debates reveal the artificiality of the distinction between securities, futures, and other financial instruments that can be engineered to meet virtually any objective, and the resulting need to amend the current structure to protect the innovation and competition inherent in new product development.

The jurisdictional issues also raise concerns about the unequal regulatory treatment of virtually identical products, and about attempts to exploit these differences through regulatory arbitrage. The SEC and CFTC may apply very different regulatory requirements to nearly identical products. For example, the SEC and CFTC handle key investor protection and market soundness provisions very differently, even for similar products. This clearly serves no regulatory purpose, and operates against our guiding principle of treating like entities and products alike.

In light of these issues, SIFMA believes that the first step towards comprehensive structural reform is the consolidation of the SEC and CFTC, whereby the securities and futures industries would be regulated under a single regulatory scheme and by a single agency. [22] SIFMA believes that the merger of the SEC and CFTC would provide tremendous efficiencies and cost-savings without compromising regulatory objectives.

The details of how such a consolidation would occur are critical to its success. To make sure that the consolidation not only occurs, but also that it occurs in an appropriate timeframe that is not disruptive to the regulated business, and occurs in the most beneficial fashion for all involved, SIFMA recommends a two stage approach, covering both the short and long term. In the short term, SIFMA proposes the creation of one new, consolidated commission ("NewCo") to administer the SEC's and CFTC's existing statutes and organizations, thereby bringing a unified oversight approach to the securities and futures markets. This NewCo would be charged with the responsibility for studying what the best statutory framework for securities and futures should be, and then revising or

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[20] Indeed, the presidential study of the October 1987 stock market crash, the Brady Report, found that the markets for stocks, options, and futures were actually one market and should come under the overarching purview of a single regulatory agency. Report of the Presidential Task Force on Market Mechanisms, vi (U.S. Government Printing Office (1988)).

[21] See, e.g., William J. Brodsky, A Real Regulatory Redundancy, Wall St. J., Oct. 19, 2007, at A19 (noting the significant delays to new product introduction caused by jurisdictional debates between the SEC and CFTC).

[22] See, e.g., Mary Schapiro, Chairman & CEO, FINRA, Remarks at Distinguished Speaker Series, Georgetown University, McDonough School of Business (Sept. 26, 2007), http://www.finra.org/PressRoom/SpeechesTestimony/MaryL.Schapiro/P037079 (questioning the sense of having two separate regulatory agencies for securities and futures); Brodsky, supra note 21, at A19 (stating that "[a]ny rational, unbiased assessment of the bifurcated regulatory system leads to the conclusion that there should be a single agency" for securities and futures); Arthur Levitt, Jr., SEC-CFTC, Wall St. J., Aug. 5, 2006, at A10 (advocating the merger of the SEC and CFTC).

harmonizing the statutes currently administered by the SEC and CFTC, as appropriate, within two years.

SIFMA recognizes, however, that this short term fix is designed for expediency and to minimize disruption while more extensive reforms are considered and implemented. In the longer term, after a careful study of the best way forward, SIFMA anticipates a more complete integration of the two agencies, their statutes and organizations. Although SIFMA's final views about the eventual reforms would be influenced by the results of both the recommended study and SIFMA's own internal evaluation of the issues at stake, SIFMA believes that the new organization should embrace the concepts outlined in this letter, including treating similar entities similarly, and adopting principles-based and prudential regulation.[23]

In addition to these structural modifications, SIFMA believes that the merger of the SEC and CFTC would provide an excellent opportunity to implement a more principles-based approach to regulation, as advocated above. In this regard, SIFMA envisions the adoption of an approach more akin to the CFTC's current model than the SEC's rules-based approach, as the CFTC has an established record of applying a principles-based oversight framework.[24]

3. Next Step: Comprehensive Financial Services Reform

The issues presented regarding the SEC and CFTC are only a small subset of the issues raised by U.S. financial services regulation generally. SIFMA is in the process of analyzing the extent to which comprehensive structural reform of financial services regulation is needed, and whether additional regulatory consolidation will prove beneficial to investors, firms and the U.S. economy as a whole. SIFMA has not yet settled on a particular approach, but is considering the costs and benefits of various reform efforts that may reach to the state regulators, banking regulators, and insurance regulators, as well as the SEC and CFTC, and will discuss these issues in its forthcoming white paper in more detail.

For example, SIFMA believes that state financial regulation needs to be addressed in the context of U.S. financial services regulation generally. SIFMA recognizes that the distinct regulatory requirements imposed on financial institutions by the many U.S. states and territories may increase costs for investors and create competitive disadvantages for U.S. market participants. Therefore, while recognizing the important investor protection role provided by state regulators, SIFMA is analyzing

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[23] SIFMA believes that the benefits of such a transition plan are manifold. First, because the substantive changes are minimal during the transition period, NewCo would not disrupt existing institutions or oversight mechanisms, while facilitating further reforms. Second, placing existing SEC and CFTC activities within NewCo subject to the oversight of one set of commissioners, even without changing the statutes or organizational structure in other ways, should strongly encourage cooperation and likeminded thinking about the full spectrum of financial issues. Third, the study of the best way forward should help ensure that the final reforms are carefully considered and thoughtfully implemented. Fourth, the imposition of a sunset provision for NewCo should prevent the proposed reforms from stagnating following the initial consolidation. Finally, the short term plan should assist in reaching the best long term resolution of the many issues raised by a CFTC-SEC merger.

[24] See, e.g., Jeremy Grant, US Regulators' Approach Under Pressure, Financial Times, Nov. 6, 2007, available at 2007 WLNR 21924414 (reporting on CME Group's CEO Craig Donohue's view that CFTC's record in applying a principles-based oversight framework means it should serve as a model for any reform of the country's markets regulation).

how best to eliminate redundancies and inefficiencies related to state regulation, thereby better serving investors and markets alike.

SIFMA is also evaluating the possible benefits of a comprehensive modernization of all federal oversight of financial entities, including the consolidation of all federal financial regulators – the banking regulators, SEC and CFTC, to address the evolving roles of the regulated entities. Another possible alternative under consideration is a more streamlined and coordinated approach to banking regulation that addresses the multiple levels of regulation present in the current system. Finally, SIFMA is also evaluating the possible benefits of changes to the regulatory structure for the insurance industry.

D. Regulatory Reform for the Global Markets

SIFMA strongly supports ongoing efforts to develop updated regulatory structures to address the increasingly global nature of financial markets. We believe such efforts can elevate global supervisory practices, promote collaboration among like-minded regulators, improve the efficiency of cross-border regulation and enhance investor protection. In light of the critical need for practical reforms to address existing regulatory obstacles to the effective delivery of cross-border services, SIFMA advocates a phased and tiered approach, which addresses pressing issues facing investors and markets under current law in the short term, and works toward broader reforms in the longer term.

In the short term, the phased and tiered approach emphasizes new rules that focus on the most significant markets, transactions and investors rather than using a "one-size-fits-all" model. For example, near-term reforms should focus on significantly redrafting Rule 15a-6 under the Exchange Act[25] and permitting 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.

SIFMA acknowledges that, as regulators address longer term reforms, the increased competitive activity in global markets raises difficult questions about the "best" approach to pursue. Recognizing that the longer term goal of a globally competitive marketplace is not simply trading for its own sake, but rather the ability to raise capital efficiently and provide investors with useful products, the techniques to achieve such objectives will vary with the circumstances. In some cases, exceptions by individual nations from their otherwise applicable regulatory regimes will be necessary; in others mutual recognition of comparable regulatory regimes will be appropriate and, in some instances, standardization on a multilateral scale will be essential. Therefore, just as we believe that "one size does not fit all" for domestic regulation, so too do we believe that U.S. regulators should pursue all three of these avenues and be flexible in considering the benefits of each one as they continue to develop cross-border regulatory structures. Doing so will help ensure robust and vibrant markets capable of efficiently raising capital and providing effective investor protection.

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

We appreciate the opportunity to provide SIFMA's input on the Treasury's timely request for comment regarding U.S. regulatory reform. Please do not hesitate to contact the undersigned with any questions.

Sincerely,

Marc E. Lackritz

Marc E. Lackritz
President and CEO

cc: Henry M. Paulson, Jr., Secretary, Department of the Treasury
Robert Steel, Under Secretary, Department of the Treasury
David Nason, Assistant Secretary, Department of the Treasury

Ben S. Bernanke, Chairman, Board of Governors of the Federal Reserve System
Christopher Cox, Chairman, Securities and Exchange Commission
Walter Lukken, Acting Chairman, Commodity Futures Trading Commission

Ira D. Hammerman, Senior Managing Director and General Counsel, SIFMA
Alan E. Sorcher, Managing Director and General Counsel, SIFMA
Brandon Becker, WilmerHale