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October 26, 2015

Commissioners
c/o
Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street NE.
Washington, DC 20549–1090.

File Number S7–14–15.

Re: Applications by Security-Based Swap Dealers or Major Security-Based Swap Participants for Statutorily Disqualified Associated Persons to Effect or Be Involved in Effecting Security-Based Swaps

Dear Commissioners,

On behalf of the more than 400,000 members and supporters of Public Citizen, we provide the following comments on a proposed rubric to deal with "Applications by Security-Based Swap Dealers or Major Security-Based Swap Participants for Statutorily Disqualified Associated Persons to Effect or Be Involved in Effecting Security-Based Swaps."

As matter of principle, we believe that the Commission should simply adhere to the Congressional mandate to ban bad actors altogether as opposed to providing a rubric for allowing them to petition for a waiver or decreased penalties. We further object to the permission for other organizations, including the industry organization FINRA, to grant the waiver in lieu of the Commission. Finally, we believe that any petitioner for an exemption from disqualification should have to prove that the implicit deterrence impact of disqualification is not diluted by receiving a waiver from penalties do to criminal misbehavior.

Section 764 and deterrence

Section 764 of the Dodd-Frank Act adds to the Exchange Act Section 15F(b)(6). This renders it unlawful for a security-based swap dealer (SBS) to permit an associated person who is subject to a statutory disqualification "to effect or be involved in effecting" security-based swaps on behalf of the SBS Entity if the SBS Entity knew, or in the exercise of reasonable care should have known, of the statutory disqualification.

The Commission would serve the public by issuing a rule that simply restates this provision of the law. The rule would be clear and easily understood by the industry. Such a rule would provide for deterrence and firms would understand that failure to police bad actors jeopardizes business.

In practice, such a restatement would mean the automatic exclusion of as few as two individuals out of 21,465 natural persons who are associated with securities based swaps activities, based on the Commission's economic analysis.[1] [2]

We appreciate this rule alone will not likely change the course of Commission enforcement of Wall Street mischief. Still, it offers a venue to explore how the Commission should apply its rules generally for "bad actors" to reduce their number. Congress correctly declared that they should be disqualified from swap activity. That's because those who steal, axiomatically, should not be trusted to operate the cash register. But there is a further reason, axiomatically, for such disqualifications, and that is deterrence—deterrence who others who have not (yet) committed an offense.

Enforcement of all rules and regulations provide for the armory of deterrence. This is no more easily understood than in consideration of the opposite. That is, the absence of penalty invites misconduct. If libraries charged no overdue fines, they would soon be void of books. If traffic officers issued no fines for speeding, drivers would more frequently exceed the speed limit. (Notice the speeding drivers on a highway who slow precipitously when they pass a hidden patrol car.) All penalties for the violation of any rule provide not only a sanction for the violator, but deterrence for everyone. "For those interested in the effects of law on human behavior, deterrence is of course the central question," observed Cass Sunstein, then a University of Chicago law professor. [3] Concurs SEC Chair White, penalties involve

[1] See p. 51711 of Federal Register, August 25, 2015, Vol 80, No. 154.

[2] The preamble notes: In 2014 FINRA received 24 applications for individuals and 10 applications for member firms, out of approximately 272,000 registered representatives and 4,000 currently registered broker-dealers. We estimate that 55 entities will register with the Commission as SBS Entities, with an estimated 21,465 associated natural persons and 868 associated person entities. Assuming the number of applications for association with statutorily disqualified persons at SBS Entities is the same as at broker-dealers results in an estimate of approximately two applications for natural persons and one application for entities per year.

[3] "Do People Want Optimal Deterrence," by Cass Sunstein et al, University of Chicago Law School, (1999), available at: http://chicagounbound.uchicago.edu/cgi/viewcontent.cgi?article=1173&context=law_and_economics

messaging: “The SEC is a law enforcement agency. . . You have to try to send as strong a message as you can, across as broad a swath of the market as you regulate, and that’s pretty broad.”[45]

As law enforcers responded to the massive frauds underpinning the financial crisis without any penalties for senior Wall Street bankers, observers far and wide have lamented the long-term impact on Wall Street integrity. [6] There is no argument that Wall Street crime has been abundant and unacceptable, and little argument that the very culture may be corrupt.

That corruption seems to be particularly focused at the largest institutions, a phenomenon that has even earned the epithet “too big to jail.” Public Citizen has explored this problem at length.[7]

We are concerned that the Commission’s recent waivers exacerbated this “too big to jail” policy. In fact, the Commission grants waivers predominately to large financial institutions. This trend was recently quantified in an authoritative study by Urska Velikonja.[8] In a study of “bad actor” waivers granted between July 2003 and December 2014, Velikonja found that large financial firms received 81.6 percent of them. Observers from Rep. Maxine Waters (D-Calif), the ranking Democrat on the House financial services committee to the Commission’s own members Kara Stein and Luis Aguilar affirm that this trend compounds the problem that some banks are too big to jail. [9] As Wall Street’s primary police agent, the Commission should avail itself of every tool to address this corruption; and at a bare minimum it should advantage the deterrence tools imbedded in Dodd Frank Section 764.

Consequently, we are dismayed that the value of deterrence figures not at all in this proposed rule and request for comment. The Commission fails to mention the term, nor even ask the public for comment about deterrence. How can a rule about “bad actors” fail to address to overarching question about how to help keep “bad actors” generally from the stage?

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[4] “SEC’s Broken Window Policy,” by Suzanne McGee, The Guardian (October 2015), available at: http://www.theguardian.com/business/2015/oct/04/sec-broken-windows-wall-street-crackdown-flawed-effective; also Fed Gov. Daniel Tarullo, remarks, (Oct. 20, 2014), available at: http://www.federalreserve.gov/newsevents/speech/tarullo20141020a.htm

[5] “On the Brink,” by Henry Paulson

[6] Fed Gov. Daniel Tarullo, remarks, (Oct. 20, 2014), available at: http://www.federalreserve.gov/newsevents/speech/tarullo20141020a.htm

[7] See “Justice Deferred,” by Amit Narang, Public Citizen (2014), available at: http://www.citizen.org/justice-deferred-too-big-to-jail-report; or “Continued Concerns with HSBC,” by Andrew Perez, Public Citizen (2015), available at: http://www.citizen.org/Page.aspx?pid=6477&frcrld=1

[8] “Waiving Disqualifcations,” by Urska Velikonja, California Law Review (2015), available at: http://poseidon01.ssrn.com/delivery.php?ID=297024085004103026023068088084084099024027003059021038093121012009025120091029108022021026029022118061047125123108120104074092044038034079014007027085068084101116018055055100121127025003000125094100082080110122007090004010001122022106066069070021082&EXT=pdf#page=3&zoom=auto,-265,85

[9] Letter from Representative Maxine Waters, U.S. House of Representatives Committee on Financial Services, to Mary Jo White, Chair, U.S. Securities and Exchange Commission, at 2 (May 14, 2015) *available at* http://democrats.financialservices.house.gov/uploadedfiles/letter_to_chair_white_5.14.15.pdf.

This void regarding deterrence mirrors a speech by Chair White at Georgetown University.[10] The chair declared that it would "not be an appropriate exercise of our authority to deny a waiver "in an effort to "deter it or others from possible future misconduct."[11] Yet the specific rule that White referenced in this speech actually does address deterrence. In fact, it speaks of deterrence five times, including this: "The deterrent effect of a potential threat of disqualification . . . could have the indirect impact of reducing the number of bad actors in the securities markets and the conduct resulting in sanctions that trigger disqualification."[12]

We ask that the final rule make appropriate response to the role of deterrence in the Commission's treatment of waivers.

The Commission's proposal

The Commission has chosen to focus on the modification that Congress provided at the end of Dodd-Frank Section 674 in their proposed rule, which was intended to catch exceptions that expert regulators might better understand than lawmakers. The modification provides that bad actors might be allowed to participate "to the extent otherwise specifically provided by rule, regulation, or order of the Commission.''

Consequently, the Commission devotes the lion's share of its proposal on a mechanism to permit the one or two individuals each year who are bad actors to remain near the swaps business, nor do we protest the idea that financial regulators may have more expert information than Congress on specific financial crimes.

We also have no quarrel with the methods the Commission currently proposes to review waiver requests. We do, however, believe they are incomplete, and that waivers should be an exception, not the rule... In addition to the current hurdles a bad actor must surmount, we ask that such actor establish that the public interest would be served if their penalty was waived. Such public interest must include a consideration of whether the deterrent effect of disqualification would be diluted. An applicant should be required to show that an exemption would actually enhance the deterrent effect. We assume this will be a high bar, as it should be.

Finally, we strongly oppose the SEC's proposal to allow other agencies to make determinations that the Commission itself should make. The Commission proposes to allow the CFTC and even FINRA to

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[10] See "White Noise," by Bartlett Naylor, Huffington Post, (March 2015), available at: http://www.huffingtonpost.com/bartlett-naylor/white-noise-i-trust-wall_b_6880238.html

[11] "Understanding Disqualifications," speech by Mary Jo White, (March 2012), available at: http://www.sec.gov/news/speech/031215-spch-cmjw.html#.VQGn4xBmP6E

[12] "Disqualification of Bad Actors," (July 2013), available at: http://www.gpo.gov/fdsys/pkg/FR-2013-07-24/pdf/2013-16983.pdf

effectively grant waivers. The Financial Industry Regulatory Authority is a private corporation, and its members are the firms overseen by the SEC. Any bad actor it disqualifies means one less dues-payer. Subcontracting this responsibility also renders the SEC unaccountable to Congress.

For further questions, please contact Bartlett Naylor at [redacted], or [redacted].

Sincerely,

Public Citizen