Testimony Concerning "International Harmonization of Wall Street Reform: Orderly Liquidation, Derivatives, and the Volcker Rule"

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Chairman Johnson, Ranking Member Shelby, and members of the Committee, thank you for inviting me to testify on behalf of the Securities and Exchange Commission (SEC) about international cooperation in the realm of financial regulation.

Markets are global, and regulators have long been mindful that domestic changes can have an impact outside their own countries. The impact of regulation across borders has become ever more important as business has become increasingly global. As part of our rulemaking efforts to implement the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), the SEC has been actively engaged in discussions with our counterparts abroad to encourage international coordination of regulatory reforms.

Our international efforts include both informal and formal bilateral discussions and arrangements, and we also work through multilateral organizations, where we have leadership roles in several task forces and working groups.

My testimony will highlight some of the key areas in which the SEC is working internationally to identify risks to the global markets, what regulatory responses might be desirable, and how to best coordinate such cross-border regulatory responses.

International Coordination Efforts

Since the financial crisis began, the G20 has identified major financial issues it believes should be addressed by the individual member jurisdictions to mitigate risks in the global financial system. As an independent agency, the SEC does not participate directly in G20 Leaders' or Finance Ministers' meetings, but we coordinate with our domestic and international counterparts who participate in these meetings to identify concerns in the global capital markets that are relevant to the work we do.

The G20 often asks other multilateral organizations to conduct in-depth studies of the concerns that impact the global financial markets, which have taken the form of surveying various approaches in different jurisdictions and developing broad policies or principles to guide regulatory authorities as they develop their own rules and regulations consistent with their unique national mandates.

In recent years, the Financial Stability Board (FSB) has played an increasingly active role in coordinating international efforts to implement G20 objectives. The FSB includes officials from banking supervisors and capital markets regulators around the globe, along with representatives from finance ministries and central banks and the international financial institutions, and aims to identify and discuss broad trends affecting the financial system.

Currently, I represent the SEC in the FSB. My colleagues from the Federal Reserve Board and the Department of the Treasury, Governor Tarullo and Under Secretary Brainard, respectively, also represent the United States in the FSB. The SEC staff regularly communicates with staffs of these agencies as well as the staffs of the Office of the Comptroller of the Currency, the Commodity Futures Trading Commission (CFTC), and the Federal Reserve Bank of New York in order to present unified positions in FSB policy discussions and working groups.

The G20 and, in turn, the FSB also seek input from other international bodies, including the International Organization of Securities Commissions (IOSCO) and other standard setters. I also serve as the SEC's Head of Delegation to IOSCO.

Due to the extensive international coordination efforts undertaken by the SEC and other U.S. financial regulatory agencies within the context of these international bodies, the recommendations and international standards being developed by these groups are broadly consistent with the Dodd-Frank Act and the G20 objectives.

The SEC also participates in multilateral discussions with regional authorities, and the SEC facilitates targeted, multilateral discussions with key jurisdictions on its highest priority topics. For example, the SEC is active in the Council of Securities Regulators of the Americas (COSRA) on issues of regional importance in the Americas.

We also recognize the need and value of holding discussions outside of the FSB and IOSCO with regulators from other jurisdictions. While bodies such as the G20, FSB and IOSCO play an important role in the international policy dialogue, national regulatory bodies such as the SEC continue to exercise the authority granted to them in a manner that is necessary and appropriate to carry out their statutory missions and legislative mandates. International bodies, such as the G20, FSB, and IOSCO, neither legislate nor write governing rules; rather, mandates for regulation come from national authorities. In addressing the risks identified by the G20, all jurisdictions do not necessarily follow the same approach. Additionally, not all jurisdictions are members of the G20 and FSB. Within IOSCO, market regulators from around the world participate, but not all entities with the authority to shape relevant rules and regulations are members.

Because of the detailed nature of the discussions required or the country-specific nature of the issues involved, certain regulatory initiatives have proven to be managed more effectively in smaller forums or on a bilateral basis. To this end, the SEC has several ongoing bilateral dialogues with regulators in key international regulatory jurisdictions, including the United Kingdom, India, China, Korea, Turkey, and Japan. These dialogues are intended to facilitate identification and discussion of common issues of regulatory concern, enhance enforcement cooperation, and, in some cases, expand on existing training and technical assistance efforts.

The dialogues have taken on increasing importance as regulators around the globe engage in financial regulatory reform efforts in their respective jurisdictions.

For example, the SEC participates alongside the Department of the Treasury and the Federal Reserve Board in the Financial Markets Regulatory Dialogue (FMRD) with the European Union. The FMRD was created in 2002 as a forum to discuss regulatory initiatives in their early stages with a focus on avoiding unnecessary conflicts of law between the United States and the European Union. It has evolved into a vehicle for in-depth discussion of regulatory issues of mutual concern, enhancement of understanding of each other's regulatory systems, and exploration of areas of regulatory cooperation and convergence in the development of high-quality regulation.

OTC Derivatives

One area where international coordination is particularly important is reform of the global OTC derivatives markets. After the 2008 financial crisis, Congress recognized the need to bring transparency to these markets, and the G20 Leaders shared this concern. At the Pittsburgh Summit in September 2009, the G20 Leaders called for global improvements in the functioning, transparency and regulatory oversight of OTC derivatives markets. Specifically, the G20 stated that:

> [a]ll standardized OTC derivative contracts should be traded on exchanges or electronic trading platforms, where appropriate, and cleared through central counterparties by end-2012 at the latest. OTC derivative contracts should be reported to trade repositories. Non-centrally cleared contracts should be subject to higher capital requirements. We ask the FSB and its relevant members to assess regularly implementation and whether it is sufficient to improve transparency in the derivatives markets, mitigate systemic risk, and protect against market abuse.[1]

In subsequent summits, the G20 Leaders have reiterated their commitment to OTC derivatives regulatory reform and have asked the FSB to monitor OTC derivatives reform progress.

Congress also recognized the need for coordination in this area and directed the SEC to consult with its foreign counterparts, as appropriate, in several key areas under Title VII of the Dodd-Frank Act. Specifically, the Dodd-Frank Act states that

> in order to promote effective and consistent global regulation of swaps and security-based swaps, the CFTC, the SEC and the prudential regulators . . ., as appropriate, shall consult and coordinate with foreign regulatory authorities on the establishment of consistent international standards with respect to the regulation (including fees) of swaps, securities-based swap, swap entities, and security-based swaps entities and may agree to such information-sharing agreements as may be

[1] G20 Meeting, Pittsburgh, 25 September 2009. Available at http://www.treasury.gov/resource-center/international/g7-g20/Documents/pittsburgh_summit_leaders_statement_250909.pdf.

deemed to be necessary or appropriate in the public interest or for the protection of investors, swap counterparties, and securities-based swap counterparties.[2]

The SEC and the CFTC have conducted staff studies to assess developments in OTC derivatives regulation abroad. For example, as directed by Congress in Section 719(c) of the Dodd-Frank Act,[3] on January 31, 2012, the SEC and CFTC jointly submitted to Congress a "Report on International Swap Regulation" (Swap Report).[4] The Swap Report discusses swap and security-based swap regulation and clearinghouse regulation in the Americas, Asia, and European Union and identifies areas of regulation that are similar and other areas of regulation that could be harmonized. The Swap Report also identifies major clearinghouses, clearing members, and regulators in each geographic area and describes the major contracts (including clearing volumes and notional values), methods for clearing swaps, and the systems used for setting margin in each geographic area.[5] In addition, on April 8, 2011, SEC and CFTC staff submitted a joint study to Congress on the feasibility of requiring the derivatives industry to adopt standardized computer-readable algorithmic descriptions which may be used to describe complex and standardized financial derivatives.[6] In preparing this report, staff coordinated extensively with international financial institutions and foreign regulators.

SEC and CFTC staff have also been working on a bilateral basis with counterparts from Canada, the European Union, Hong Kong, Japan, and Singapore to coordinate technical issues that are in the interest of leveling the playing field for the regulation of derivatives transactions. In December, leaders and senior representatives of the authorities responsible for the regulation of the OTC derivatives markets in these jurisdictions met in Paris to discuss significant cross-border issues related to the implementation of new legislation and rules governing the OTC derivatives markets, including concerns about possible regulatory gaps, conflicts, arbitrage, and duplication. In addition to agreeing to continue staff-level bilateral technical dialogues, the leaders are planning to meet again as a group this spring.

We also have worked through multilateral organizations to facilitate further international cooperation. SEC staff represents IOSCO as a co-chair of the FSB's OTC Derivatives Working Group (ODWG). The FSB published a report on implementing OTC derivatives market reforms in October 2010.[7] This report, which was endorsed by the G20 Leaders,[8] includes 21 recommendations addressing practical issues that authorities may encounter in implementing the G20 commitments concerning standardization, central clearing, exchange or electronic platform trading, and reporting OTC derivatives transactions to trade repositories. The ODWG conducts

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[2] Dodd-Frank Wall Street Reform and Consumer Protection Act § 752 (Pub. L. 111-203, H.R. 4173) (2010).
[3] Dodd-Frank Wall Street Reform and Consumer Protection Act § 719(c) (Pub. L. 111-203, H.R. 4173) (2010).
[4] Available at http://www.sec.gov/news/studies/2012/sec-cftc-intlswapreg.pdf.
[5] The Swap Report points out that major dealers could not be identified as of the date of the report because rules requiring swap dealers to register as such had not been adopted yet. Neither could any major swap exchanges be identified in the report as no exchange was offering swaps or security-based swaps for trading as of the date of the report.
[6] Available at http://www.sec.gov/news/studies/2011/719b-study.pdf.
[7] Available at http://www.financialstabilityboard.org/publications/r_101025.pdf.
[8] G20 Leaders' Meeting, Seoul, Korea, 12 November 2010. Available at http://www.treasury.gov/resource-center/international/Documents/1%20%20FINAL%20SEOUL%20COMMUNIQUE.pdf.

semi-annual reviews of jurisdictions' efforts to implement the G20 objectives for OTC derivatives reforms and submits reports on its findings to the G20.

In October 2010, IOSCO formed a Task Force on OTC Derivatives Regulation to take a leading role in coordinating market regulators' efforts to work together in the development of supervisory and oversight structures related to the derivatives markets. Representatives from the SEC, CFTC, United Kingdom Financial Services Authority (UK FSA), and the Securities and Exchange Board of India (SEBI) serve as co-chairs of this Task Force. The Task Force was formed primarily to assist regulators in coordinating their derivatives legislative and regulatory reform efforts and in developing consistent regulatory standards, with a focus on derivatives clearing, trading, trade data collection and reporting, and the oversight of certain derivatives market participants.

In February 2011, the Task Force published a "Report on Trading of OTC Derivatives" (Report on Trading).[9] The Report on Trading sets out a framework for international regulators to consider when implementing the G20 Leaders' commitment to trade all standardized OTC derivatives on exchanges or electronic trading platforms, where appropriate, by the end of 2012. The Report on Trading analyzes the benefits, costs, and challenges associated with increasing exchange and electronic trading of OTC derivative products and contains recommendations aimed at assisting the transition of the trading of standardized derivatives products from OTC venues onto exchanges and electronic trading platforms (organized platforms) while preserving the efficacy of those transactions for counterparties. Following on that effort, earlier this year, the Task Force completed the "Follow-On Analysis to the Report on Trading," which describes the different types of organized platforms currently available for the execution of OTC derivatives transactions in IOSCO member jurisdictions and seeks to highlight the different approaches global regulators are taking or envisage taking to mandate the use of organized platforms for trading OTC derivatives.[10]

The Task Force also collaborated with the Basel-based Committee on Payment and Settlement Services (CPSS) to publish the "Report on OTC Derivatives Data Reporting and Aggregation Requirements" earlier this year (Data Report).[11] The Data Report specifies minimum requirements for the reporting of data to trade repositories and for trade repositories reporting to regulators, as well as types of acceptable data formats, and discusses issues relating to authorities' and reporting entities' access to data and the dissemination of OTC derivatives data to the public. The Data Report also describes data aggregation mechanisms and tools needed to enable authorities to aggregate data in a manner that fulfills their regulatory mandates, including methods, rationales and possible tools to implement data aggregation, such as legal entity identifiers. The Task Force plans to complete its work later this year when it finalizes reports setting forth international standards for mandatory clearing and the oversight of derivative market intermediaries.

Additionally, the SEC is working through IOSCO to review and improve international standards for financial market infrastructures. This project is a joint effort of IOSCO and the CPSS. In

[9] Available at http://www.iosco.org/library/pubdocs/pdf/IOSCOPD345.pdf.
[10] Available at http://www.iosco.org/library/pubdocs/pdf/IOSCOPD368.pdf.
[11] Available at http://www.iosco.org/library/pubdocs/pdf/IOSCOPD366.pdf.

March 2011, CPSS-IOSCO issued a "Consultation Report on Principles for Financial Market Infrastructures" (FMI Report).[12] The FMI Report proposes new and more demanding international standards for systemically important payment systems, central securities depositories, securities and settlement systems, central counterparties and trade repositories (collectively, financial market infrastructures, or FMIs).

The new standards (referred to as principles) presented in the FMI Report are designed to ensure that the essential payment and settlements infrastructure supporting global financial markets is more robust and better placed to withstand financial shocks. The FMI Report contains a comprehensive set of twenty-four principles designed to apply to all systemically important FMIs and five responsibilities for central banks, market regulators, and other relevant authorities. CPSS-IOSCO plans to publish the final report this spring.

Finally, given the global nature of the derivatives market, the SEC intends to address the international implications of its rules arising under Subtitle B of Title VII in a single proposal in order to give interested parties, including investors, market participants, and foreign regulators, an opportunity to consider as an integrated whole our approach to the registration and regulation of foreign entities engaged in cross-border security-based swap transactions involving U.S. parties. We understand that our approach to the cross-border application of Title VII must both achieve effective domestic regulatory oversight and reflect the realities of the global derivatives market. As we do so, the SEC is continuing to actively coordinate with our counterparts in other jurisdictions to help achieve consistency and compatibility among approaches to derivatives regulation.

Identification and Mitigation of Systemic Risk

A second area that requires robust international cooperation is the identification and mitigation of risks that could have cross-border impact on markets. The SEC has worked to enhance our capability to spot emerging issues and to address proactively these issues before they have the potential to cause serious harm to the US financial markets and the global financial system. For example, we have open lines of communication with our international counterparts to discuss emerging risks and to promptly react to new developments. In addition, our bilateral efforts and work in multilateral organizations also give us insight into concerns faced by other jurisdictions.

The ability to collect and share compatible data is also essential to regulators' efforts to identify and mitigate systemic risk. An example of this information sharing is the Commission's work with other regulators, including the UK FSA and the Hong Kong Securities and Futures Commission, to develop an internationally-agreed upon template that would form the basis for future data collection efforts to better understand the hedge fund industry.

We worked through IOSCO first, to survey the role of hedge funds in other markets and to develop high-level, international general principles for regulation of the hedge fund sector. The template was published in February 2010 and contains a list of broad proposed categories of information (with examples of potential data points) that regulators could collect for general supervisory purposes and to help in the assessment of systemic risk (including, for example,

[12] Available at http://www.iosco.org/library/pubdocs/pdf/IOSCOPD350.pdf.

product exposure and asset class concentration, geographic exposure, liquidity information, extent of borrowing, and credit counterparty exposure).

After the Dodd-Frank Act was passed, we continued to work closely with the UK FSA, the EC and the European Securities and Markets Authority (ESMA) to discuss cross-border issues that have emerged as we implemented Title IV, including the development of Form PF. At the same time we were developing Form PF, which was finalized on October 31, 2011, [13] ESMA was developing its data collection form, which was published on November 11, 2011 as part of ESMA's formal advice to the EC on implementation of its Alternative Investment Fund Managers Directive. Given that each regulator must develop its reporting requirements based on its unique mandates, policies, and objectives, the forms are understandably not exactly the same. Nevertheless, due to our extensive coordination efforts, the two forms generally are compatible and will facilitate international efforts to compare, aggregate, and learn from the data.

In addition to our bilateral coordination efforts, we have worked in multilateral organizations to ensure that future efforts to identify and mitigate risk will benefit from international coordination. For example, early last year, IOSCO published a discussion paper entitled "Mitigating Systemic Risk – A Role for Securities Regulators" (Systemic Risk Paper), which focused on the role securities regulators play in addressing systemic risk.[14] The Systemic Risk Paper was intended to promote discussion among securities regulators on the ways in which systemic risk intersects with their mandates and to provide insight on how IOSCO and its members can better identify, monitor, mitigate and manage systemic risk. We are also playing a lead role in IOSCO's new Standing Committee on Risk Research, created to bring together economists from major market regulators to discuss these issues on a regular basis. We continue to work internationally to facilitate dialogue about systemic risk among securities regulators as well as with the broader international regulatory community.

Volcker Rule

Section 619 of the Dodd-Frank Act, commonly referred to as the Volcker Rule, may also have international implications. The Volcker Rule generally prohibits a banking entity from engaging in proprietary trading and having certain interests in, or relationships with, a hedge fund or private equity fund ("covered funds"), subject to certain exemptions. The defined term "banking entity" determines the scope of entities subject to the Volcker Rule and includes any: (i) insured depository institution, (ii) company that controls an insured depository institution, (iii) foreign bank with a branch, agency or subsidiary in the United States, and (iv) affiliates and subsidiaries of the foregoing entities. The Commission proposed a rule jointly with the Federal banking agencies to implement the Volcker Rule in October 2011 ("Proposed Rule"), and the CFTC issued its proposal in January 2012.

In the Proposed Rule, the five regulatory agencies requested and received comment on several international issues. For example, the Proposed Rule, which closely follows statutory construction, includes an exemption for proprietary trading in certain U.S. and municipal

[13] Summary and final rule are available at http://www.sec.gov/news/press/2011/2011-226.htm and http://www.sec.gov/rules/final/2011/ia-3308.pdf.
[14] Available at http://www.iosco.org/library/pubdocs/pdf/IOSCOPD347.pdf.

government obligations, but does not establish an additional exemption for proprietary trading in foreign government obligations. Many commenters, including some foreign governments, have requested that such an exemption be adopted and have expressed concerns about the proposed rule's potential impact on liquidity in foreign sovereign debt markets. Moreover, consistent with the statute's exemptive authority, some of these commenters have suggested ways that such an exemption would promote and protect the safety and soundness of banking entities and the financial stability of the United States. However, some commenters have indicated that such an exemption would not be necessary or would not meet such standards.

In addition, the proposal also includes the statutory exemptions for foreign banking entities' activities conducted "solely outside of the United States." The Proposed Rule sets forth certain requirements for these exemptions that are intended to give effect to the statutory language. Some commenters have stated that the exemption's requirements may result in unintended extraterritorial application of the Volcker Rule's restrictions on a foreign banking entity's offshore activity. The proposed definition of "covered funds" also includes certain non-U.S. funds, and this may have international implications. In an effort to prevent circumvention of the Volcker Rule's general prohibition on covered fund activities by simply relocating covered fund-related activities offshore, the proposal defined "covered fund" to include certain types of non-U.S. funds. Some commenters have stated that this definition may be too broad and could include foreign retail mutual funds or other types of regulated pooled investment vehicles.

Commission staff is reviewing and considering the comment letters that we have received on this proposal, including comments on the international implications of the Proposed Rule. I anticipate that staffs of the five regulatory agencies will have in-depth discussions about these topics as they work together through the next steps of the rulemaking process.

Market Efficiency and Integrity

A fourth area where we and our foreign counterparts have an interest is market efficiency and integrity. In early 2010, the SEC issued a Concept Release on Equity Market Structure to begin an in-depth review to ensure that the U.S. equity markets remain fair, transparent and efficient in light of new technology and trading strategies.[15] Not surprisingly, many other jurisdictions face similar challenges. The rapid developments in trading technologies and trading platforms have had a profound impact on the structure of markets around the world.

As we have considered these issues, the EC also has been reviewing its Markets in Financial Instruments Directive (MiFID) in light of new technology, and in October 2011, the EC issued proposals to amend MiFID, focusing on developing safeguards for algorithmic and high frequency trading activities. Throughout this process, we have had ongoing discussions with our international counterparts.

On October 14, 2011, Chairman Schapiro and her regulatory counterparts in Europe, the Americas, Asia, and Australia spent a full day discussing the impact of advances in technology, new trading strategies, and the increasing integration and globalization of markets as part of an international roundtable of regulators that the SEC co-hosted with the UK FSA in London. The

[15] Available at http://www.sec.gov/rules/concept/2010/34-61358fr.pdf.

discussion focused on sharing views about automated trading strategies, high frequency trading, market fragmentation, and dark pools.

Last year, the SEC also adopted a large trader reporting system, providing us with access to better data to help us assess the impact of high frequency traders and other major market participants on the quality of our markets, as well as to assist in our surveillance and enforcement efforts.[16] In addition, we are continuing to work toward the adoption of a consolidated audit trail system to further help regulators keep pace with new technology and trading patterns in the markets.[17] As we utilize and develop new tools, we are also coordinating with our international counterparts to share knowledge and develop complementary strategies that will ultimately facilitate the sharing of information for supervisory and enforcement purposes.

To that end, SEC staff also is engaged actively with IOSCO to address the continuing challenges that technological changes pose for regulators in their market surveillance, including: the fragmentation of markets and the resulting dispersal of trading information; the increased speed of trading; and regulators' ability to gather and process the increased volume of trading data.

In addition, in the fall of 2010, the G20 Leaders asked IOSCO to develop "recommendations to promote markets' integrity and efficiency to mitigate the risks posed to the financial system by the latest technological developments." In response, IOSCO undertook a review of global perspectives on the impact of technological developments, including work on trading halts, direct electronic access, dark liquidity, and high frequency trading. In April 2011, IOSCO published principles to assist regulators in minimizing the potential adverse effects of the increased use of dark liquidity, focusing on transparency and price discovery, market fragmentation, knowledge of trading intentions, fair access, and the ability to assess actual trading volume in dark pools.

In October, IOSCO published the "Report on Regulatory Issues Raised by the Impact of Technological Changes on Market Integrity and Efficiency" (Technological Changes Report).[18] The Technological Changes Report analyzes significant technological developments and related micro-structural issues that have arisen in financial markets in recent years, notably high frequency trading, and their impact on market structure, participants' behavior, price discovery and formation, and the availability and accessibility of liquidity. In addition, the Technological Changes Report recognizes the benefits of technology, including facilitating the establishment of globally competitive markets, enabling market participants to reduce transaction time, generation of electronic audit trails, enhancement of order and trade transparency, enabling markets and market participants to develop and apply (and regulators to monitor) automated risk controls.

Supervisory Cooperation

Another key priority for the G20 is increasing the effectiveness of global supervision of financial institutions and other market participants. In a world with interconnected markets and actors with cross-border operations, more effective supervision will require increased international supervisory cooperation.

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[16] *See* Securities Exchange Act Release No. 64976 (July 27, 2011), 76 FR 46960 (August 3, 2011).
[17] *See* Securities Exchange Act Release No. 62174 (May 26, 2010), 75 FR 32556 (June 8, 2010).
[18] See http://www.iosco.org/library/pubdocs/pdf/IOSCOPD361.pdf.

The SEC has long recognized the importance of international cooperation to its own supervisory mission, especially in our examination program. The SEC staff has been developing arrangements and, where possible, entering into formal Memoranda of Understanding (MOUs), to facilitate supervisory cooperation with foreign regulators. These agreements generally establish clear mechanisms for consultation, cooperation and the exchange of supervisory information. Such mechanisms minimize the need to address supervisory information sharing on an *ad hoc* basis and seek to address new information sharing needs created by globally active firms and cross-border affiliated markets.

The SEC's supervisory cooperation agreements can vary in scope and purpose. To date, the SEC has entered into bilateral MOUs that cover information sharing and cooperation related to, among other things, firms registered with both the SEC and a foreign authority; the oversight of markets in the U.S. and a foreign jurisdiction affiliated through common ownership structure; and the sharing of non-public issuer specific information relating to the application of International Financial Reporting Standards.

This month, the SEC entered in a supervisory MOU with the Cayman Islands Monetary Authority (CIMA) Concerning Consultation, Cooperation and the Exchange of Information Related to the Supervision of Cross-Border Regulated Entities (CIMA MOU). The CIMA MOU covers those entities that are regulated by the SEC and the CIMA and operate or provide services across our respective borders. It also sets forth the terms and conditions for the sharing of information regarding regulated entities, such as broker-dealers and investment advisers. The scope of the CIMA MOU is broad, allowing our cooperation to evolve and adapt to a changing regulatory landscape and covers not only regulated entities that currently operate on a cross-border basis, but also those that may come under our respective jurisdictions in the future.

In September 2011, the SEC entered into an expanded supervisory MOU with its Canadian counterparts. The Canadian MOU is a comprehensive arrangement that will help to facilitate the supervision of regulated entities that operate across the U.S.-Canadian border. The SEC and Canadian provincial securities authorities have a long history of cooperation, particularly in securities enforcement matters. The Canadian MOU extends this cooperation beyond enforcement by establishing a framework for consultation, cooperation and information-sharing related to the day-to-day supervision and oversight of regulated entities. The supervision of regulated entities is critical to encouraging compliance with the securities laws, which in turn helps to protect investors and the securities markets generally.

The SEC is also actively engaging its regulatory counterparts abroad to develop new supervisory cooperation tools. For example, the SEC and the European Securities Markets Authority recently concluded an MOU that would allow us to share information regarding the oversight of credit rating agencies that are registered in both our markets. The MOU lays out the processes by which we could conduct examinations of the offices of credit rating agencies located in each other's jurisdictions. In addition, the MOU provides a clear mechanism by which the SEC and ESMA staffs can share observations about the compliance cultures of registered credit rating agencies to better inform both agencies.

The SEC also has comprehensive supervisory MOUs with the securities regulators in the United Kingdom, Germany and Australia, as well as several tailored arrangements and protocols for

information sharing with other regulators.[19] Under these agreements, SEC staff is increasingly able to obtain and exchange documents and information about cross-border regulated entities and globally-active market participants. SEC staff has also conducted many on-site examinations of SEC registrants located overseas in cooperation with foreign authorities. These types of arrangements improve our ability to share information at the operational level and to have frank, open discussions with our counterparts abroad about the entities we regulate, such as broker-dealers and investment advisers.

To complement our bilateral supervisory cooperation efforts, the SEC worked within IOSCO to establish a Task Force on Supervisory Cooperation. This SEC-led task force developed principles for supervisory cooperation and a model MOU that was endorsed by IOSCO's Technical Committee and published in 2010.[20] The model MOU was designed to assist securities regulators in building and maintaining cross-border cooperative relationships with one another and has proven helpful in our ongoing efforts to expand the number of bilateral agreements focused on supervision.

With the SEC's authority under the Dodd-Frank Act to supervise additional market participants such as hedge fund advisers, security-based swaps dealers and major security-based swaps participants, SEC staff will seek to expand its cooperative networks with foreign counterparts on supervisory matters. We also anticipate that the FSB and IOSCO will continue to consider ways to improve international supervisory cooperation, and we will continue to work in these multilateral forums to support our bilateral efforts and fulfill our supervisory mission.

In addition to enhancing our ability to oversee registrants that operate cross-border, SEC staff has assisted other US regulators in carrying out their mandates. As you know, the SEC also has oversight responsibilities for the Public Company Accounting Oversight Board (PCAOB), which oversees both foreign and domestic public accounting firms that audit US public companies. The Commission continues to work closely with the PCAOB on efforts to achieve meaningful inspection of PCAOB registered firms overseas.

Unfortunately, at the present time, the PCAOB is unable to conduct inspections in a number of European countries, as well as the People's Republic of China. While the PCAOB continues its efforts to enable inspections of registered firms to be conducted in these countries, the Board has taken a number of interim steps to help protect investors. These steps include regularly publishing information that provides transparency around the status of firms' ability to be inspected, such as the jurisdictions that are not allowing PCAOB inspections, the firms that are overdue for inspections and are in jurisdictions that will not allow those inspections to go forward, as well as a list of companies whose audit firms have not been inspected by the PCAOB. In addition, the PCAOB has reevaluated its approach to considering registration applications from firms in jurisdictions where the PCAOB is unable to conduct inspections. The inability to conduct inspections can and has resulted in the PCAOB determining to disapprove a registration application. The PCAOB continues to work, with SEC support and at the urging of

[19] *See Cooperative Arrangements with Foreign Regulators* at http://www.sec.gov/about/offices/oia/oia_cooparrangements.shtml.
[20] Available at http://www.iosco.org/library/pubdocs/pdf/IOSCOPD322.pdf.

the Commission, to achieve the goal of accomplishing meaningful oversight of registrant firms wherever they may be.

Enforcement Cooperation

Finally, the cornerstone of any effective regulatory regime is its enforcement. In global markets, bad actors can wreak havoc both at home and abroad, and the proceeds of their violations can and do move throughout our global marketplace. No matter how robust and coordinated global regulation and supervision may be, if those rules are not enforced, or if investors are not confident that the markets are fair, the global financial system will not function efficiently. The SEC has over 35 bilateral MOUs with its counterparts for information sharing for enforcement purposes. These agreements vary in scope, but generally allow for broad information sharing, including provisions for assistance with locating individuals of interest and conducting testimony abroad.

While international enforcement cooperation has long been important to our mission, and many of our enforcement cooperation agreements are now more than twenty years old, I want to highlight our international enforcement cooperation for two reasons. First, now more than ever, it is essential to the success of our enforcement program. Last year, nearly 30 percent of the SEC's enforcement cases had an international element that required the agency to reach out to foreign authorities. As just one example, in a major insider trading case where we charged a doctor in France with tipping a U.S. hedge fund manager about clinical drug trials, the French Autorité des marchés financiers (AMF) accomplished the important task of helping us obtain bank records, phone records, and compelled testimony – key evidence crucial to our success in the case. [21]

During fiscal year 2011, the SEC made 772 formal requests to foreign authorities for enforcement assistance, and frequently conducted informal discussions with our partners about investigations with cross-border elements. Importantly, our cooperation is not one-way; in the same year, the SEC responded to 492 requests from abroad. We are less than halfway through FY 2012 and are well on track to meet or exceed these record numbers yet again.

Second, our international enforcement cooperation efforts also illustrate the efficacy of the multi-faceted international coordination strategies we employ. In May 2002, IOSCO developed a Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information (MMoU). The MMoU is a multilateral enforcement information-sharing and cooperation arrangement. It provides an international benchmark for the types of

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[21] *SEC v. Yves Benhamou*, Lit. Rel. No. 21721 (November 2, 2010), available at http://www.sec.gov/litigation/litreleases/2010/lr21721.htm; see also related action *SEC v. Joseph "Chip" Skowron*, Lit. Rel. No. 22158 (November 17, 2011), available at http://www.sec.gov/litigation/litreleases/2011/lr22158.htm.

information securities regulators should have authority to share as well as the terms under which information sharing should occur. The MMoU provides a baseline as to what is expected of a regulator in order to cooperate fully in global efforts to combat securities fraud. When a jurisdiction applies to become a signatory, IOSCO conducts a rigorous review to assess the jurisdiction's ability to fulfill its obligations under the MMoU.

This multilateral effort also has expanded significantly the number of securities regulators who have the ability to gather information and share information with the SEC for enforcement investigations and proceedings. The international pressure on non-signatory jurisdictions increased after the financial crisis, when IOSCO set a goal of January 1, 2013 for all of its members to acquire the powers and authorities necessary to become full signatories to the MMoU. As of the 2011 IOSCO Annual Meeting, over 80 securities regulatory authorities have become signatories to the MMoU, and another 30 have made the necessary commitment to seek national legislative changes to allow them to do so by the 2013 deadline.

Similarly, the FSB is actively encouraging global cooperation in information sharing. In 2010, the FSB launched an initiative to encourage the adherence of all countries and jurisdictions to international cooperation and information exchange standards. As part of this initiative, the FSB reviewed the policies and practices of 61 jurisdictions to evaluate and rate compliance with international cooperation and information exchange standards. This past November, the FSB published the results of its review, including the names and categories of the evaluated jurisdictions. The United States was referenced as a jurisdiction demonstrating sufficiently strong adherence.

In addition to participating in multilateral efforts to raise standards for cooperation, the SEC has a long-standing commitment to training foreign regulatory and law enforcement officials in enforcement strategies and techniques. Every fall, we hold an International Enforcement Institute (Enforcement Institute), a flagship event for securities enforcement professionals worldwide that provides an excellent opportunity to develop important relationships with our counterparts, while serving to strengthen their capacity to conduct effective enforcement in their respective jurisdictions. Similarly, we also host an annual International Institute on Securities Market Development, which is a key part of our efforts to strengthen global capital markets and lays a strong foundation for bilateral engagement around the world. In addition to these successful outreach efforts, we continue to work bilaterally and regionally to provide technical assistance to regulators around the world in many topic areas.

Finally, I want to highlight one of the SEC's major current efforts focused in the enforcement arena, the Cross-Border Working Group, an inter-divisional team that brings various experiences and expertise to address risks associated with U.S. issuers whose primary operations are located overseas. This team emerged out of an SEC proactive risk-based inquiry into US audit firms with a significant number of issuer clients with primarily foreign operations. That inquiry revealed serious accounting irregularities among certain U.S. issuers based abroad. The efforts of this group have resulted in a wide array of actions to protect U.S. investors, including suspending trading in at least 20 foreign-based entities because of deficiencies in information about the companies, instituting stop orders against foreign-based entities to prevent further stock sales under materially misleading and deficient offering documents, revoking the securities

registration of at least a dozen foreign-based issuers, and instituting administrative proceedings to determine whether to suspend or revoke the registrations of 27 more. The majority of issuers in the United States whose operations are primarily overseas are located in the PRC region; accordingly, most of these actions have involved companies based in China. The Cross-Border Working Group's endeavors also extend outside of the enforcement area and include reaching across borders to enhance cooperation with SEC counterparts.

Conclusion

Our ability to develop shared objectives and cooperative relationships with our counterparts abroad is a critical part of our mission, and increasingly more so every year. Since the 2008 financial crisis, through the SEC's work in the FSB and IOSCO, participation in bilateral dialogues, and discussions with SEC staff who work on these issues on a day-to-day basis, I have observed a reinvigorated global commitment to the core objectives shared by securities regulators: protecting investors; promoting fair, efficient and transparent markets; and facilitating capital formation to fuel global economic growth. However, shared objectives alone are not sufficient. We must also pursue a shared commitment to work together to identify compatible regulatory approaches in pursuit of those objectives. The SEC works tirelessly to pursue such commitment through cooperation with counterparts throughout the international regulatory landscape and will continue to pursue and promote international cooperation.

Thank you for the opportunity to testify today on this important set of issues. I am happy to answer any questions you may have.