

# drums along the potomac

## The Cost of Dodd-Frank

American Action Forum, a center-right think tank of sorts, has an unbelievable, online, interactive presentation focused on your favorite policy punching bag: Dodd-Frank. They call it Regulation Rodeo.

Director of Regulatory Policy Sam Batkins and research analyst Dan Goldbeck detailed the costs to the economy of the Dodd-Frank Act. In an article entitled, “Six Years After Dodd-Frank: Higher Costs, Uncertain Benefits,” Batkins and Goldbeck revealed that Dodd-Frank has imposed more than \$36 billion in final rule costs and 73 million paperwork hours, up from \$24 billion in final rule costs and 61 million paperwork burden hours from last year’s report. To put those figures in perspective, the costs are approximately \$112 per person or \$310 per household; for paperwork, it would take 36,950 employees working full-time (2,000 hours annually) to complete a single year of the law’s paperwork, and those are based on agency calculations.

**Definitely hit the site, it’s a real treat. You should plan on drinking early. See it at <http://regrodeo.com/>.**

Batkins and Goldbeck argued that the sixth year of Dodd-Frank has been the most expensive in the law’s history. “Much of the law has already been implemented,” the authors observed, “but there are still at least 61 rulemakings remaining ... that are directly related to Dodd-Frank.” They cautioned that one “can only expect ... costs to continue to rise.”

We would have no way in heck to verify these numbers, any of these numbers. We doubt the agencies who write and implement these laws could actually verify or dispute these numbers. All that time and treasure spent on this imposing body of law, and at least one presidential nominee wants to 86 the whole thing. The very idea gives us pause. Would rescinding

Dodd-Frank, at this point be a good idea? Well, maybe if you’re new to the market. But if you’ve been here a while, and plan to stay, would you want to ditch all those man-hours spend on getting your operation compliant? Trash that massive investment at this late stage? It’s debatable. Or, should be. We are open to any comments on this thought; send them directly to the editor at [johns@scudderpublishing.com](mailto:johns@scudderpublishing.com).

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**Cadwalader ran a brief piece in their Cabinet this week citing a Delta Strategies analysis on all the various comments that came in following the CFTC’s latest request for comments RE: Reg. AT.** The summary categorizes the comment letters by registration, source code, definitions, risk controls, self-trade prevention, annual reports, software development, deployment and testing, and SEFs.

Highlights from the comments made by various industry groups and associations include:

- The rulemaking is too prescriptive and instead should be more principles-based;
- The rulemaking should focus on implementing appropriate risk controls (pre-trade risk and other controls) and address other important areas in a separate rulemaking;
- Requirements specific to AT personnel or those engaged in algorithmic trading should be considered in separate rulemakings differentiated from the requirements applicable to all market participants;
- Registration for AT personnel is unnecessary, would have unintended consequences and is an inappropriate criterion for triggering risk controls;
- The proposed definition of “Direct Electronic Access” (“DEA”) is problematic in that the DEA is not an appropriate filter for determining an

AT person;

- The definition of “algorithmic trading” should focus only on algorithmic trading activity that may pose a risk to the derivatives markets.
  - The CFTC should not be permitted to obtain source code via a subpoena.
- For a full copy, go to <https://www.findknowdo.com/sites/default/files/news/attachments/2016/07/dsg-summary-second-round-reg-comment-letters-copy.pdf>.

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**Two weeks ago, the House Agriculture Committee held a hearing examining Reg. AT.** Committee members heard testimony that focused primarily on the regulation’s source code provision, something the industry seems ready to go to the mat to prevent regulators from getting unless a subpoena is in hand. Agriculture Committee Chairman Michael Conaway opened the hearing, calling for a “more modest” CFTC proposal that would leverage industry incentives by requiring the “universal adoption of a flexible framework for best practices.” He said, “The most confusing parts of Reg. AT – the source code rules, the registration regime, the reporting requirements and the inflexible risk controls – are unnecessary to achieve the (CFTC’s) stated goals. Market participants already have incentives to police bad algorithms, prevent disruptions and plan for recovery. In many cases, there are already ongoing processes across the industry to impose and refine risk controls ...” We wonder which AT/HFT firm is writing the chairman’s stuff these days. The Delta Strategy Group summary of the hearing noted that all four witnesses agreed that the source code provision was unprecedented and posed significant due process and confidentiality concerns. The four witnesses also asserted

*(Continued)*

that the CFTC should continue to issue subpoenas and safeguards before requiring access to source code.

Other highlights of the hearing include:

- RGM Advisor CEO Richard Gorelick and Trading Technologies International, Inc. Executive VP and General Counsel Michael Ryan argued that source code is of little value in itself, since it is difficult to interpret and future trading events depend on many factors working in conjunction with source code in the marketplace.
- Futures Industry Association Market Access Committee Chairman Greg Wood and Mr. Gorelick recommended that the CFTC focus on activities instead of arbitrarily designat-

ing who should apply risk controls by creating unnecessarily specific definitions, i.e., “AT Persons.”

- Chicago Mercantile Exchange Executive Director of Global Investigations Andrew Vrabel and Mr. Wood emphasized that a market participant’s size and complexity have no bearing on the risk that it poses to the marketplace; all market participants pose the same risks, and every market participant should be subject to risk controls (for which Mr. Vrabel specified a two-tier, pre-trade risk control structure).
- Mr. Gorelick and Mr. Wood stressed that the focus of CFTC’s cost-benefit analysis of Reg. AT is too narrow. They concluded that the

regulation fails to address wider implications for the markets, and warned that it could have an adverse effect on competition and liquidity in US futures markets.

We’re not sure how this will eventually play out, but we think that once the term “smoking gun” begins to be heard in the same sentence as “source code” and “spoofing” or “flash crash,” we think the whole subpoena argument will wither and die. We heard a very good argument once for regulator access to algo source code to aid in investigations. Code doesn’t think or change its mind, we were told, and it only does what it is told. In that context, context doesn’t matter all that much.

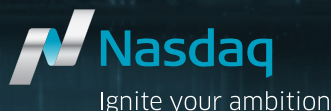
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