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Clearinghouse Standards Get Regulators' Selective Backing

By **Rachel Graf**

Law360 (September 6, 2019, 7:30 PM EDT) -- The nation's top securities and derivatives regulators recently underscored their commitment to certain clearing agency standards put in place after the 2008 crisis, despite concurrent efforts to dismantle other financial protections mandated by the Dodd-Frank Act.

The U.S. Securities and Exchange Commission and the U.S. Commodity Futures Trading Commission on Wednesday fined the derivatives clearinghouse Options Clearing Corp. **a collective \$20 million** for alleged lapses in its risk management policies and margin requirements that the agencies said violated clearing agency standards required by the Dodd-Frank Act. OCC didn't admit or deny the claims, which were laid out in the agencies' first enforcement actions alleging violations of **the regulations**.

The settlement announcements came just weeks after the Federal Deposit Insurance Corp.'s board of directors and the Office of the Comptroller of the Currency approved changes that would **ease various banking restrictions** enacted after the financial crisis.

"A lot of the regulatory changes post-financial crisis were designed to learn from the lessons of the past, and the current administration is dismantling those protections," said Benjamin Galdston of Berger Montague, who **until recently** represented investors at Bernstein Litowitz Berger & Grossmann LLP.

It's crucial not to understate how important clearing agency standards are in preventing another "catastrophic collapse," he added.

The SEC and CFTC seemed to recognize that importance in their orders this week, fining OCC for alleged procedural problems despite no allegations of financial harm.

The regulators accused OCC of failing to maintain risk management procedures, monitor its liquidity risks and review margin requirements, among other compliance shortcomings.

"They didn't wait for harm to occur — no blood on the walls yet," said David Chase, who worked in the SEC's enforcement division before opening his own law firm defending against securities claims. "But [it's] kind of a smart, preventative measure."

In its order, the SEC said OCC had been out of compliance with some of the rules for years. The agency said OCC failed to come into compliance despite SEC staff's "advance warnings and ample time to comply."

After the OCC's repeated failures to fix the problems on its own, the SEC could have lost patience, said Wiley Rein LLP partner Kevin Muhlendorf, a former senior counsel in the SEC's enforcement division.

The SEC's apparent hesitation to bring a public enforcement action might have stemmed from concerns about roiling the markets, said Galdston.

OCC has been designated a systemically important financial market utility, meaning "the failure of or a disruption to the functioning of such [financial market utility] could create or increase the risk of significant liquidity or credit problems spreading among financial institutions or markets and thereby threaten the stability," according to the SEC.

"These were serious allegations and serious charges, and the consequences of disrupting or potentially putting the OCC out of business would be monumentally significant for the marketplace," Galdston said.

The actions also highlighted interagency cooperation, with CFTC enforcement director James McDonald saying in a statement the agency will "continue to work closely with our regulatory and enforcement partners."

Chase said he's noticed more SEC and CFTC collaboration recently.

In the past year, they have teamed up to accuse a trader of **inflating the value of investments** to boost his personal bonus, a CEO of **trading unregistered bitcoin**, and a slew of marketers of **producing and distributing videos** that misled investors into believing they could make easy money by opening accounts to trade binary options.

"I am seeing what I think, to some extent, is an unprecedented level of cooperation as reflected by joint investigations and joint enforcement actions between the SEC and CFTC, which over the last 20 years I have not seen," Chase said.

The cases are In the Matter of The Options Clearing Corp., administrative proceeding number 3-19416 before the U.S. Securities and Exchange Commission and docket number 19-19 before the U.S. Commodity Futures Trading Commission.

--Editing by Brian Baresch and Kelly Duncan.

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