

Obama's Regulation of Credit Default Swaps

By [Washington's Blog](#)

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I have repeatedly stated that the exceptions to Obama's proposed regulation of credit default swaps will swallow up any real oversight.

For example, I [wrote](#) in July:

Obama's regulation of credit default swaps leave loopholes large enough to drive the biggest trucks through. Specifically, it forces over-the-counter credit default swap transactions to be traded through an exchange unless it is a non-standard cds. So all that the "financial innovators" who melted down the economy have to do is get a little creative in drafting their cds' - or just to tell regulators "oh no, that wasn't a standard contract", and they are excepted from the regulation.

Today, Gary Gensler, chairman of the Commodities Futures Trading Commission (an agency with responsibility for overseeing derivatives trades) - and one of the main people who blocked regulation of CDS in the past - [warned Congress](#) about this issue:

Gensler identified several loopholes in Obama's plan, noting that it would exclude foreign exchange swaps from regulation, possibly encouraging swap dealers to tailor products to fit this foreign exclusion.

"These exceptions could swallow up the regulation," Gensler said in his package to Congress.

As Gensler [told](#) Congress:

If a foreign entity or a foreign subsidiary of a U.S. entity is trading with an American counterparty, we should know about it. I am concerned that the Discussion Draft [of Congress' proposed regulation of credit default swaps] could allow foreign financial institutions to be exempted from our requirements. We must ensure that we do not inadvertently create gaps in our regulatory system through exemptions for foreign regulations...

I worry that the specific provisions might inadvertently permit market participants to shop for lax foreign regulators.

While Gensler gave one example of a "creative" scheme which would get around CDS regulation - running the contract through a foreign partner or foreign subsidiary - I guaranty that there are thousands of other creative schemes which could be used to evade regulation. Every time the IRS cracks down on a new tax shelter, "creative" tax lawyers come up with new ones. CDS will be exactly the same, unless the government actually deals with the underlying issues - including [looting](#).

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