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**SUMMARY OF
WRITTEN TESTIMONY OF CHARLES A. VICE
PRESIDENT AND CHIEF OPERATING OFFICER
INTERCONTINENTAL EXCHANGE, INC.**

1. **ICE Operates a Transparent Platform.** ICE provides a reliable, transparent over-the-counter market for trading physical energy commodities and financially-settled OTC derivatives. ICE has promoted competition and innovation on the derivatives market, which has lowered transaction costs for energy users.
2. **One Size Regulation Does not Fit All Markets or Contracts.** Many of the products on ICE are niche OTC products that trade in illiquid markets. Applying Designated Contract Market (DCM) core principles to these markets does not make sense. ICE supports creating appropriate oversight of energy markets that serve a significant price discovery market or impact a significant price discovery market on a DCM. However, the two-tier regulatory structure currently in place should be kept for DCMs and Exempt Commercial Markets.
3. **The Federal Energy Regulatory Commission and the Commodity Futures Trading Commission have Complementary Jurisdiction.** ICE believes that FERC and the CFTC have complementary jurisdiction in energy markets. However, dual regulation would cause harm to the markets. There is a clear role for each regulator to oversee the energy markets and FERC and the CFTC should be able to coordinate their oversight and enforcement responsibilities.
4. **Funding of the CFTC.** The CFTC is currently under-funded and ICE supports increasing their budget. However, ICE urges caution in levying a “transaction tax” or “user fee.”



WRITTEN TESTIMONY OF CHARLES A. VICE
PRESIDENT AND CHIEF OPERATING OFFICER
INTERCONTINENTAL EXCHANGE, INC.
BEFORE THE HOUSE
SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS
COMMITTEE ON ENERGY AND COMMERCE
UNITED STATES HOUSE OF REPRESENTATIVES

December 12, 2007

Chairman Stupak, Ranking Member Whitfield, I am Chuck Vice, President and Chief Operating Officer of the IntercontinentalExchange, Inc., or "ICE." We very much appreciate the opportunity to appear before you today to give our views on energy markets.

As background, ICE was established in 2000 as an over-the-counter (OTC) market. Since that time, ICE has grown significantly, both through its own market growth fostered by ICE's product, technology and trading innovations, as well as by acquisition of other markets to broaden its product offerings.

Today, ICE operates a leading global marketplace in futures and OTC derivatives across a variety of product classes, including agricultural and energy commodities, foreign exchange and equity indexes. Commercial hedgers use our products to manage risk and investors provide necessary liquidity to the markets. Headquartered in Atlanta, ICE has offices in New York, Chicago, Houston, London, Singapore, Winnipeg and Calgary.

ICE hosts four separate markets on our electronic trading platform – ICE's OTC energy market, which operates under the Commodity Exchange Act (CEA) as an "exempt commercial market," or ECM, and three subsidiaries: ICE Futures Europe, formerly known as the "International Petroleum Exchange," which is regulated by the UK Financial Services Authority; ICE Futures US, formerly known as "The Board of Trade of the City of New York (NYBOT)," which is a CFTC-regulated Designated Contract Market (DCM), and the Winnipeg Commodity Exchange, which is regulated by the Manitoba Securities Commission.

ICE has always been and continues to be a strong proponent of open and competitive markets in energy commodities and related derivatives, and of regulatory oversight of those markets. As an operator of global futures and OTC markets and as a publicly-held company, we strive to ensure the utmost confidence in the integrity of our markets and in the soundness of our business model. To that end, we have continuously worked with FERC, the CFTC and other regulatory agencies in the U.S. and abroad in



order to ensure that they have access to all relevant information available to ICE regarding trading activity on our markets and we will continue to work with all relevant agencies in the future. ICE strongly supports legislative and regulatory changes that will enhance the quality of oversight and available information with respect to the energy markets.

Over the past several months, ICE has been working with members of Congress to create appropriate oversight of certain energy markets that either impact a designated contract market, and its price discovery function, or which separately serve a significant price discovery function. By appropriate, ICE believes that any legislative or regulatory changes that are made need to reflect the different nature of ICE's varied markets and the significant differences between contracts on ICE that serve a significant price discovery function and those that do not. We also believe that any consideration of possible changes to the current regulatory structure must be based upon an understanding of the operations of "exempt commercial markets," such as ICE, and of the balance struck by Congress and the CFTC between overseeing these markets while still allowing them to function in the context of OTC trading by commercial and institutional participants. We welcome the opportunity to work with the Subcommittee and its staff on these important issues.

ICE Operates a Transparent Platform

Broadly, because OTC markets tend to be global in nature, most OTC markets are now conducted electronically across most asset classes, including OTC markets for U.S interest rate instruments, foreign exchange and debt securities. ICE responded to the transparency and speed enjoyed in other OTC markets by establishing its many-to-many electronic marketplace for trading physical energy commodities and financially-settled over-the-counter derivatives, primarily swaps, on energy commodities. ICE in effect performs the same function as a "voice broker" in the OTC market, but does so through an electronic platform. Voice brokers offer limited transparency and only then to the largest trading firms. ICE, however, provides the same high quality information to all traders, big and small, and at the same instant. The ICE electronic market also offers faster and more efficient execution while providing regulators with a comprehensive audit trail with respect to orders entered, and transactions executed – none of which is available from voice brokers. The introduction and development of ICE's platform have promoted competition and innovation in the energy derivatives market, to the benefit of all market participants and consumers generally. The reliability of ICE's markets has also resulted in an increasing preference for electronic trading in these markets. NYMEX, in its recent testimony before the Senate Permanent Subcommittee on Investigations (the "Senate PSI"), noted that 80-85% of its volume is now traded electronically, a development driven largely by competition from ICE. The CFTC also pointed out, in its Senate PSI testimony, that "the ability to manipulate prices on either



[NYMEX or ICE] has likely been reduced, given that ICE has broadened participation in contracts for natural gas.” Importantly, greater participation means heightened liquidity, which results in lower transaction costs and tighter bid/ask spreads. This makes the cost of hedging energy price risk lower, which results in cheaper operating costs for businesses.

Participants on ICE enter bids and offers electronically and are matched in accordance with an algorithm that executes transactions on the basis of time and price priority. Participants executing a transaction on our platform may settle the transaction in one of two ways – on a bilateral basis, settling the transaction directly between the two parties, or on a cleared basis through LCH.Clearnet using the services of a futures commission merchant that is a member of LCH.Clearnet. In addition to providing the clearing house with daily settlement prices, ICE is also responsible for maintaining data connectivity to the clearing house.

It is important to note that there are substantial differences between ICE's OTC market, other portions of the OTC market, and the NYMEX futures market. These differences necessarily inform and guide the appropriate level of oversight and regulation of our markets. First, ICE is only one of many global venues on which market participants can execute OTC trades. A significant portion of OTC trading in natural gas is executed through voice brokers or direct bilateral negotiation between market counterparties. Of the available forums, only ICE (and any other similarly-situated ECMs) is subject to CFTC jurisdiction and the CFTC's regulations, or to limitations on the nature of its participants.

Second, participants in the futures markets must either become members of the relevant exchange or trade through a futures commission merchant that is a member. In contrast, ICE's OTC market, by law, is a "principals only" market in which participants must have trades executed in their own names on the system.

Third, the OTC market offers a substantially wider range of products than the futures markets, including, for example, hundreds of niche derivative contracts on natural gas and power pricing at over 100 different delivery points in North America. The availability of these niche markets on ICE has improved transparency and lowered transaction costs via tighter bid-ask spreads, but volume nonetheless remains very low at most points. The market reality, for most of these illiquid points, is that participation is limited to the very small number of marketers, utilities, and others that have some intrinsic supply or demand interest.

Fourth, the most liquid products traded in the OTC market broadly and on the ICE OTC market specifically are cash-settled swaps that require one party to pay to the other an amount determined by the final settlement price in the corresponding futures contracts



but do not, and cannot, result in the physical delivery or transfer of energy commodities. These ‘lookalike’ swaps have been widely used by OTC energy market participants long before the creation of ICE. In fact, these swaps are useful and common in any market for which there are benchmark futures prices. Our Henry Hub natural gas swap, for example, constitutes an important commercial hedging vehicle and has served as an important complement to and a hedge for the NYMEX Henry Hub natural gas futures contract. An understanding of the ICE markets is critical to any determination of the appropriate regulation of these markets.

ICE and its market participants, including energy producers, distributors and users, benefited significantly from the regulatory flexibility embodied in the CFMA through the ECM structure established under section 2(h)(3) of the Act. The tangible benefits to the marketplace included more efficient hedging of energy price risk (tighter markets), greater price transparency in all parts of the marketplace, and vastly improved liquidity through the introduction of more participants (and thus greater price competition) in the markets. These benefits have not been limited to those brought about directly by ICE’s business and its product offerings, but include those resulting from changes to the business models and product offerings of other market participants that responded to the competitive challenge presented by ICE’s business.

As these markets have grown and developed since passage of the CFMA, new regulatory challenges have emerged. ICE advocates a targeted approach to any reform of the CEA. Such an approach recognizes the unique characteristics of the many customized markets that have evolved and the importance of continuing to encourage market innovation.

One Size of Regulation Does Not Fit All Markets or Contracts

The problem with “one size fits all” regulation can best be illustrated by contrasting the historic nature of futures markets (limited number of actively traded benchmark contracts, all transactions executed through a broker who can trade for its own account or that of a retail customer) with the ECM OTC swaps markets (large number of niche products, many illiquid and thinly traded, principals only trading). Recognizing the importance of futures pricing benchmarks to the general public (a DCM is obligated to publish its prices to be used by the broader market), and in recognition of the potential for conflicts of interest due to members trading for their own accounts alongside business transacted on behalf of customers, some of whom were retail customers, DCM core principles were developed to facilitate regulation of the markets by the DCM, which acted as a self regulatory organization. The typical high level of liquidity in benchmark contracts make application of core principles such as market monitoring and position accountability and limits feasible and appropriate.



Suggesting that these same DCM core principles, which were developed with the futures exchange model in mind, should apply to all OTC swap contracts traded on an ECM market is attempting to fit the proverbial square peg in a round hole. While some level of additional reporting and a system of position accountability limits may be appropriate for certain contracts – specifically, those that settle on a futures market contract price and that are the true economic equivalent of a contract actively traded on a regulated futures market – most of the energy swaps available on ICE are niche OTC products that trade in illiquid markets that are not amenable to the application of DCM core principles. For example, how would an ECM actively monitor an illiquid swaps market in an attempt to “prevent manipulation” where price changes can be abrupt due to the limited liquidity in the market? How would an ECM swaps market administer accountability limits in a market that has only a handful of market participants? Should the ECM question when a single market participant holds 50% of the liquidity in an illiquid market when the market participant is one of the only providers of liquidity in the market?

It is important to analyze these questions not in isolation, but in the context of market participants having alternatives such as OTC voice brokers through which they can conduct their business. Importantly, such OTC voice brokers can even offer their customers the benefits of clearing through use of block clearing facilities offered by NYMEX (and also by ICE). Faced with constant inquiries or regular reporting by the ECM related to legitimate market activity, and facing no such monitoring when it transacts through a voice broker, market participants might choose to conduct their business elsewhere. It is for these and other reasons that Congress and the Commission have developed the carefully calibrated two-tier regulatory structure applicable to DCMs and ECMs. We believe that the judgments made by Congress and the Commission thus far have been prudent and should generally be maintained.

FERC and the CFTC have Complementary Jurisdiction

In 2005, Congress passed the Energy Policy Act, which granted FERC broader authority to police manipulation in energy markets. Although many believe that FERC and CFTC’s jurisdictions conflict, ICE believes that they complement each other. As noted before, ICE operates a global company across the span of energy markets: physical, OTC, and futures. Accordingly, it works closely with FERC and the CFTC to help ensure fair, competitive trading. ICE believes that FERC and the CFTC are capable regulators in their respective areas in the physical, OTC, and futures markets.

It is important that this jurisdiction remain complimentary, however. Overlapping regulation of the same conduct would likely result in harm to markets. Applying dual regulation to energy markets would create uncertainty over compliance with two separate, varying and sometimes conflicting legal standards. The only certainty would be



the increased cost to U.S. businesses from having to comply with two regulators. The possible effect would be that these firms, operating on a global scale, would take their business overseas to other trading venues. There is a clear role for each regulator to oversee the energy markets, and we believe that FERC and the CFTC should be able to coordinate, rather than duplicate, their oversight and enforcement responsibilities.

Funding of the CFTC

ICE believes that the CFTC is currently under funded and we support Congress increasing the CFTC's budget. ICE strongly supports increasing the Commission's budget, but urges caution in considering whether to levy a "transaction tax" or "user fee" on futures transactions. As an operator of both domestic and foreign futures exchanges, ICE recognizes that the futures industry is highly competitive, on both a domestic and global basis. Trading firms often operate on thin margins. A transaction tax could double the trading costs for market makers, who provide important liquidity to the market. If these trading participants left all or some markets, that would take important market liquidity with them. A recent study of transaction taxes on futures markets found that a futures tax would negatively impact volume and bid/ask spreads.¹ Consumers would feel the brunt of this tax, as businesses would be pass on the increased cost of offsetting price risk in less liquid markets to them.

Further, it is questionable whether a transaction tax would raise the revenue needed for the Commission. Again, firms operate on thin margins and might choose to move their business offshore or to less transparent markets. This would increase the Commission's cost of surveillance, while decreasing taxable transactions.

Conclusion

ICE has always been and continues to be a strong proponent of open and competitive markets in energy commodities and other derivatives, and of appropriate regulatory oversight of those markets. As an operator of global futures and OTC markets, and as a publicly-held company, ICE understands the importance of ensuring the utmost confidence in its markets. To that end, we have continuously worked with the CFTC and other regulatory agencies in the U.S. and abroad in order to ensure that they have access to all relevant information available to ICE regarding trading activity on our markets. We have also worked closely with Congress to address the regulatory challenges presented by emerging markets and will continue to work cooperatively for solutions that promote the best marketplace possible.

¹ Robin K. Chou and George H.K. Wang, *Transaction Tax and the Quality of the Taiwan Stock Index Futures*, JOURNAL OF FUTURES MARKETS, 1195-1216 (2006).



Mr. Chairman, thank you for the opportunity to share our views with you. I would be happy to answer any questions you may have.