



Commodity Futures Trading Commission

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Remarks

Remarks of Jill Sommers

Commissioner of the Commodity Futures Trading Commission Before the Futures Industry Association Law and Compliance Division and the New York City Bar Association, New York November 13, 2007

Thank you Dennis. I am delighted to be in New York today with my fellow Commissioner, Bart Chilton. We had the pleasure of speaking at an FIA luncheon in Chicago last month and, as in Chicago, I see many familiar faces around the room, having worked closely with the FIA over the years during my tenures with the Chicago Mercantile Exchange and ISDA. This is a great opportunity to meet those of you I haven't gotten a chance to know yet, and I look forward to working with all of you from my new perspective as a Commissioner of the CFTC.

As I said in Chicago, in the short span of time I've been at the CFTC I've been overwhelmed by the innovations and evolution of this industry. I am grateful for this opportunity for public service and am especially appreciative of my fellow Commissioners and all of the supportive staff at the CFTC. Someone once said "If you love your job you will never have to work another day in your life." I've got to tell you, it's a pretty good feeling.

As some of you may know, I grew up in Fort Scott, Kansas, a small town about 60 miles south of Kansas City. My family has owned and operated an Ace Hardware store for 38 years. As a young girl, I worked in the store and learned the value of a dollar and the importance of good business decisions.

After graduating from the University of Kansas with a degree in Political Science, my career plan consisted of interning for a few months with Senator Bob Dole in Washington, D.C. I did not dream of staying in Washington, but life had a different path for me. I ended up working for Senator Dole, both in Washington and in Kansas, for almost five years. I left the Capitol to work for an agricultural consulting firm and became involved with futures issues. In 1998, I began working for the Chicago Mercantile Exchange in its Washington, D.C. office, where I was responsible for regulatory and legislative affairs. This gave me the unique opportunity to work closely with congressional staff on the Commodity Futures Modernization Act, from the very beginning to the long awaited end. I left the CME in 2004, and most recently worked as Policy Director and Head of U.S. Government Affairs for ISDA.

While working for the CME on the CFMA, I met my husband Mike, who is a congressional staffer for Republican Leader John Boehner. We live in Alexandria, VA and have three children, ages five, four and three.

When Barbara asked me to speak to you today back in August, November seemed a long way off, but the time has flown by. I don't know whether that's a sign of getting older or because we've been so busy at the Commission, but I hope it's the latter. During the past couple of months since Bart and I were sworn in as Commissioners, the CFTC has been very busy.

In October, the Commission's Global Markets Advisory Committee hosted officials from the European Commission to discuss the European Union's implementation of the Markets in Financial Instruments Directive (MIFID) and the new European code of Conduct for Clearing and Settlement. I appreciate the difficulties inherent in harmonizing regulatory standards across jurisdictions and applaud the significant progress the EU has made through MIFID to facilitate cross-border business. The CFTC has a long history of facilitating global competition by recognizing comparable regulators around the world. It is exciting to be a member of an organization that has been a leader in opening financial markets and I look forward to a continuing dialogue with our foreign counterparts on cross-border issues.

Another issue that's been in the news is the CFTC's exclusive jurisdiction over futures markets. In July, the CFTC and the Federal Regulatory Energy Commission (FERC) each filed enforcement actions against Amaranth Advisors and its chief natural gas trader, Brian Hunter, alleging, respectively, violations of the Commodity Exchange Act and the Energy Policy Act of 2005 for manipulative activity on the New York Mercantile Exchange. Amaranth asked the court in the CFTC proceeding to stay FERC's administrative proceeding on the ground that FERC's jurisdiction does not extend to the futures markets. The FIA, joined by the Managed Funds Association, NYMEX, the CME Group and ISDA filed an amicus brief supporting the CFTC's exclusive jurisdiction. Not surprisingly, the court denied Amaranth's motion after finding that it was not the proper forum in which to raise the jurisdictional challenge. The situation has generated considerable interest from various members of Congress, but so far there has been no talk of a legislative response. Chairman Lukken has had discussions with Chairman Kelliher of the FERC and I am hopeful that the two agencies will be able to work cooperatively to resolve things going forward.

The Congress and the Commission have also been focusing their attention the regulatory structure of the energy markets. On September 18th the Commission held a hearing to examine the interrelationship between energy trading on designated contract markets (DCMs) and exempt commercial markets (ECMs). Based upon the record developed at the hearing and staff interviews of industry participants, the Commission issued a report containing findings and legislative recommendations on how the regulatory structure governing these markets could be improved. It has been my opinion that the structure created in 2000 was properly vetted and entirely appropriate, and the Commission confirmed in its report that the CFMA's tiered approach to regulation has worked well. Since that time, however, markets have evolved and grown at a dramatic pace, especially in the energy sector, where we now have contracts listed on an ECM that directly compete with contracts listed on a DCM. It was only prudent therefore, from a regulatory perspective, for us to examine the current framework in light of these developments to determine whether adjustments needed to be made to level the regulatory playing field and ensure adequate oversight.

The Commission found in its report that the lower level of regulation for ECMs has allowed them to serve as valuable incubators for new concepts, which has spurred DCMs to respond with innovations of their own. The Commission also found, however, that when a look-alike ECM contact matures and begins to serve a significant price discovery function, increased regulation is warranted. The Commission recommended amendments to the ECM provisions of the Commodity Exchange Act in four specific areas for these price discovery contracts. Notably, the Commission found that the over-the-counter (OTC) bilateral and voice broker markets do not exhibit significant price discovery attributes and therefore have limited impact on how energy markets function. The report also pointed out that the non-standardized form and dispersed nature of the OTC and voice broker markets would make it extremely expensive and difficult to extrapolate beneficial market surveillance information from them. Thus, the Commission did not recommend that Congress change the current regulatory structure governing these markets. Finally, the Commission announced its intention to form an Energy Markets Advisory Committee and to work closely with FERC to develop best practices for the end users of energy products on how to effectively use the futures and other derivatives markets in managing price risk and volatility.

On October 24th, the Commission delivered the report to our Congressional oversight committees in both the House and the Senate. On the same day, Chairman Lukken testified before our House subcommittee about the issues discussed in the report and other issues related to reauthorization, which, after having stalled in 2005 has gained traction once again. On October 30th Senator Crapo, who serves on both the Senate Agriculture and Banking committees, asked the President's Working Group on Financial Markets (PWG) whether it still supports statutory language it approved in 2005 addressing the retail foreign currency fraud issues arising out of the 7th Circuit's decision in *Zelener*, the implementation of risk-based portfolio margining for security futures products and security options, and the resolution of definitional issues relating to narrow-based security indexes. Senator Crapo asked the PWG for its opinion on the legislative changes recommended by the CFTC in its ECM report as well, and whether the PWG supports any additional changes to the CFMA. As of this morning, the PWG had not yet responded to Senator Crapo's request, but I expect it will do so some time this week.

Another issue that is of particular interest to me is portfolio margining of securities and futures positions. The securities industry has advocated what is known as a "one pot" approach that would require all positions to be held in a securities account. I fully support the concept of portfolio margining whenever it can be achieved. It fosters the efficient use of capital, is good for customers, and is good for the economy. But the "one pot" approach raises legal, regulatory, operational, and supervisory issues that would, at the very least, require legislation to amend the Securities Investor Protection Act of 1970 to extend SIPC coverage to futures. A better approach, I believe, would be the "two pot" approach under which offsets are recognized through a cross-margining agreement at the clearinghouse level between securities held in a securities account and futures held in a futures account. This would eliminate the need for legislation and many, if not all, of the regulatory, operational, and supervisory issues. It would also allow greater capital efficiency by retaining the traditional risk-based calculations for the futures positions that are not yet available for securities positions.

I am aware that there was interest from the industry last year in forming a working group comprised of industry, exchange and clearing experts to develop a structure for cross-margining futures and securities at the firm and clearing house levels. I have talked to Chairman Lukken

about my interest in spearheading such an effort and am hopeful that we can get this started in the very near future.

The CFTC does an outstanding job of encouraging market growth and innovation while ensuring the integrity of the marketplace and protecting market users. As a Commissioner, I hope to play an important role in promoting strong oversight, fair and flexible regulation, and competition in the marketplace. Thank you again for inviting me here today. I look forward to your input as we move forward with reauthorization and the many important issues facing the industry today and in the coming years.