Commodity Futures Trading Commission
Office of External Affairs
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581
202.418.5080

Statement

Statement Commissioner Jill Sommers Regarding Global Markets Advisory Committee

July 15, 2008

Good afternoon and welcome to this meeting of the Global Markets Advisory Committee. This is my first time to chair a meeting of the committee and I am very much looking forward to this dialogue regarding issues of importance to global futures markets. We have a number of members here today who are continuing as members of GMAC and several new members as well. We really appreciate your taking time out of your busy schedules to participate because we rely on your input. Let me take a moment to recognize Acting Chairman Walt Lukken for his outstanding service to GMAC. Walt served as chairman of this committee from October 2003 to early February of this year, a period of nearly four and a half years. Under his leadership, the committee worked on an array of issues including MiFID, cross-border clearing, bankruptcy questions related to segregated and secured funds, as well as international regulatory coordination. I value your guidance on these international market issues.

The GMAC was established by the Commission in 1998 to seek industry input on matters that impact the global derivatives marketplace, and today's discussion certainly falls within that category. After an update on current international initiatives, we will discuss the implications of various legislative proposals that have recently been introduced in Congress concerning foreign boards of trade that provide access to U.S. customers without registering as a U.S. exchange. The issue of U.S. access to foreign exchanges has been debated by this committee before. In fact, the agenda for the very first meeting of the GMAC, held on May 14, 1998, included, and I quote, the "[p]lacement of U.S. exchange terminals abroad and foreign exchange terminals in the U.S." At that time, U.S. exchanges were concerned that foreign exchanges with trading terminals in the U.S. might gain a competitive advantage over U.S. exchanges due to less burdensome home regulatory structures, and the Commission was grappling with what it meant to be "located outside the United States" as that phrase is used in Section 4(a) of the Commodity Exchange Act. The global landscape has changed tremendously since that time. U.S. exchanges now operate around the world, and the Commission has issued no-action letters to 18 foreign exchanges permitting them to access U.S. customers. Advances in technology and innovative business plans have opened

markets and spurred competition in a way that has benefited economies world-wide, providing risk-management tools where they didn't exist before.

While the global landscape has changed, questions surrounding the Commission's no-action process and whether it provides both the regulatory tools necessary for proper oversight of cross-border business and a level regulatory playing field have persisted. In 2006, the Commission reaffirmed the no-action process as providing the most flexible method of ensuring that appropriate conditions are put in place to address the specific factual circumstances of a given market, as demonstrated most recently by the enhanced conditions added to the no-action relief for ICE Futures Europe and the Dubai Mercantile Exchange. But, as mentioned, questions persist. Jackie Mesa, our Director of International Affairs, will summarize the different categories of pending legislation, which will lead us into what I hope will be a productive discussion of the implications of the various proposals.

Futures exchanges and the means to access them are evolving in an era that is increasingly dominated by electronic trading. Sophisticated customers often want more control over trade execution, more direct access to the markets, and less intervention by their brokers. There are different terms for this trend, but the most widely used is direct market access or DMA, our second topic for discussion.

There are two main types of DMA. Traditional DMA provides centralized order routing where the customer inputs an order and relies on the futures commission merchant to route the order directly to the exchange of their choice. When this was introduced some years ago it was a huge advance compared to the pre-automated trading that preceded it. Pure DMA, which is newer than traditional DMA, allows customers to connect directly to the exchange instead of going through a futures commission merchant's traditional infrastructure. It is increasingly popular, particularly with high volume traders. Going directly to an exchange can reduce latency, or time delay, in routing orders.

DMA has improved trading efficiency and generally offers traders more safeguards via the clear audit trail it provides, but the emphasis on speed is challenging traditional approaches to risk management. Clearing firms traditionally assessed risk and pre-trade controls as trades passed through the firm's order routing infrastructure and before they reached an exchange. Some traders, whose trading strategies depend on high-speed access to exchanges, want to avoid delays caused by such pre-trade risk filters. Clearing firms are cautious about this kind of business, but competitive pressures make it hard to turn away such traders. This has meant that risk assessment for pure DMA clients is often done after the trade is executed, i.e., on a post-trade basis.

Today's meeting of the Committee gives us an excellent opportunity to discuss the risks and benefits of DMA, including the challenges to risk management, how exchanges and intermediaries have responded to these risks, and whether there is a need for industry-wide guidance.