

TESTIMONY OF GARY GENSLER
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BEFORE THE
U.S. HOUSE COMMITTEE ON AGRICULTURE
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Good morning Chairman Lucas, Ranking Member Peterson and members of the Committee. I thank you for inviting me to today's hearing on implementing the Wall Street Reform and Consumer Protection Act. I am pleased to testify on behalf of the Commodity Futures Trading Commission (CFTC). I also thank my fellow Commissioners for their hard work and commitment on implementing the legislation.

Before I move into the testimony, I want to congratulate Chairman Lucas on becoming Chairman of this Committee that is so critical to both the economy and American agriculture. I also want to thank Chairman Lucas, Ranking Member Peterson and this Committee for leading the effort to bring regulatory reform to the over-the-counter derivatives – or “swaps” – markets. This Committee passed the first bill during the last Congress – the bipartisan H.R. 977 – that included comprehensive reform of derivatives. The joint framework for derivatives legislation that was released later by this Committee's leadership also helped frame the debate on how to best protect the American public through regulatory reform of swaps. H.R. 977 and the joint framework formed the basis of the derivatives title of the Wall Street Reform and Consumer Protection Act.

The Wall Street Reform and Consumer Protection Act

On July 21, 2010, President Obama signed the Wall Street Reform and Consumer Protection Act (the Act). Title VII of the Act, entitled “The Wall Street Transparency and Accountability Act,” amended the Commodity Exchange Act (CEA) to establish a comprehensive new regulatory framework for swaps and security-based swaps. The legislation was enacted to reduce risk, increase transparency and promote market integrity within the financial system by, among other things:

1. Providing for the registration and comprehensive regulation of swap dealers and major swap participants;
2. Imposing clearing and trade execution requirements on standardized derivatives products;
3. Creating robust recordkeeping and real-time reporting regimes; and
4. Enhancing the Commission’s rulemaking and enforcement authorities with respect to, among others, all registered entities and intermediaries subject to the Commission’s oversight.

The reforms mandated by Congress will reduce systemic risk to our financial system and bring sunshine and competition to the swaps markets. Markets work best when they are transparent, open and competitive. The American public has benefited from these attributes in the futures and securities markets since the great regulatory reforms of the 1930s. The reforms

of Title VII will bring similar features to the swaps markets. Lowering risk and improving transparency will make the swaps markets safer and improve pricing for end-users.

Implementing the Wall Street Reform and Consumer Protection Act

The Wall Street Reform and Consumer Protection Act is very detailed, addressing all of the key policy issues regarding regulation of the swaps marketplace. To implement these regulations, the Act requires the CFTC and Securities and Exchange Commission (SEC), working with our fellow regulators, to write rules generally within 360 days. At the CFTC, we initially organized our effort around 30 teams who have been actively at work. We have recently added another team. We had our first meeting with the 30 team leads the day before the President signed the law.

The CFTC is working deliberatively and efficiently to promulgate rules required by Congress. The talented and dedicated staff of the CFTC has stepped up to the challenge and has recommended thoughtful rules – with a great deal of input from each of the five Commissioners – that would implement the Act. Thus far, the CFTC has approved 39 notices of proposed rulemaking, two interim final rules, four advanced notices of proposed rulemaking and one final rule.

The CFTC's process to implement the rulemakings required by the Act includes enhancements over the agency's prior practices in five important areas. Our goal was to provide

the public with additional opportunities to inform the Commission on rulemakings, even before official public comment periods. I will expand on each of these five points in my testimony.

1. We began soliciting views from the public immediately after the Act was signed and prior to approving proposed rulemakings. This allowed the agency to receive input before the pens hit the paper.
2. We hosted a series of public, staff-led roundtables to hear ideas from the public prior to considering proposed rulemakings.
3. We engaged in significant outreach with other regulators – both foreign and domestic – to seek input on each rulemaking.
4. Information on both staff's and Commissioners' meetings with members of the public to hear their views on rulemakings has been made publicly available at cftc.gov.
5. The Commission held public meetings to consider proposed rulemakings. The meetings were webcast so that the Commission's deliberations were available to the public. Archive webcasts are available on our website as well.

Two principles are guiding us throughout the rule-writing process. First is the statute itself. We intend to comply fully with the statute's provisions and Congressional intent to lower risk and bring transparency to these markets.

Second, we are consulting heavily with both other regulators and the broader public. We are working very closely with the SEC, the Federal Reserve, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency and other prudential regulators,

which includes sharing many of our memos, term sheets and draft work product. CFTC staff has had 376 meetings with other regulators on implementation of the Act.

Specifically, our rule-writing teams are working with the Federal Reserve in several critical areas: swap dealer regulation, clearinghouse regulation and swap data repositories, though we are consulting with them on a number of other areas as well. With the SEC, we are working on the entire range of rule-writing, including those previously mentioned as well as trading requirements, real time reporting and key definitions. So far, we have proposed two joint rules with the SEC as required by Congress.

In addition to working with our American counterparts, we have reached out to and are actively consulting with international regulators to harmonize our approach to swaps oversight. As we are with domestic regulators, we are sharing many of our memos, term sheets and draft work product with international regulators as well. Our discussions have focused on clearing and trading requirements, clearinghouses more generally and swaps data reporting issues, among many other topics.

We also are soliciting broad public input into the rules. On July 21st, we listed the 30 rule-writing teams and set up mailboxes for the public to comment directly. We determined it would be best to engage the public as broadly as possible even before publishing proposed rules. We have received 2,851 submissions from the public through the email inboxes as well as 1,111 official comments in response to notices of proposed rulemaking.

We also have organized nine roundtables to hear specifically on particular subjects. We have coordinated the majority of our roundtables with the SEC. These meetings have allowed us to hear directly from investors, market participants, end-users, academics, exchanges and clearinghouses on key topics including governance and conflicts of interest, real time reporting, swap data recordkeeping and swap execution facilities, among others. The roundtables have been open to the public, and we have established call-in numbers for each of them so that anyone can listen in.

Additionally, many individuals have asked for meetings with either our staff or Commissioners to discuss swaps regulation. To date, we have had more than 500 such meetings. We are now posting on our website a list of all of the meetings CFTC staff, my fellow Commissioners and I have with outside organizations, as well as the participants, issues discussed and all materials given to us.

We began publishing proposed rulemakings at our first public meeting to implement the Act on October 1, 2010. We have sequenced our proposed rulemakings over 11 public meetings thus far. Our next meeting is scheduled for February 24.

Public meetings have allowed us to discuss proposed rules in the open. For the vast majority of proposed rulemakings, we have solicited public comments for a period of 60 days. On a few occasions, the public comment period lasted 30 days. As part of seeking public comment on each of the individual rules, we also have asked a question within many of the proposed rulemakings relating to the timing for the implementation of various requirements

under these rules. In looking across the entire set of rules and taking into consideration the costs of cumulative regulations, public comments will help inform the Commission as to what requirements can be met sooner and which ones will take a bit more time.

We have thus far proposed rulemakings in 26 of the 30 areas established last July. We still must propose rules on capital and margin requirements, product definitions (jointly with the SEC) and the Volcker Rule. We also are considering comments received in response to advanced notices of proposed rulemaking with regard to disruptive trading practices and segregation of funds for cleared swaps.

A number of months ago we also set up a 31st rulemaking team tasked with developing conforming rules to update the CFTC's existing regulations to take into account the provisions of the Act. This is consistent with one of the requirements included in the recent executive order issued by the President, entitled "Improving Regulation and Regulatory Review."

In reviewing the executive order more broadly, the CFTC's practices are consistent with the executive order's principles. The CFTC has a robust process to involve and ensure public participation in the rulemaking process. The CFTC also consults broadly with other regulators to coordinate, harmonize and simplify regulations. We work to identify and consider regulatory approaches that reduce burdens and maintain flexibility and freedom of choice for the public. Further, the CFTC routinely seeks public comment on technical information and data considered during the regulatory process. Lastly, the CFTC conducts cost-benefit analyses in its rulemakings as prescribed by Congress in Sec. 15(a) of the CEA rather than as prescribed in

Section 1 of the executive order. The statute includes particularized factors to inform cost-benefit analyses that are specific to the markets regulated by the CFTC. Thus, we will continue to fulfill the CEA's statutory requirements. Even though the statute dictates different cost-benefit analysis methodology, the CFTC's practices are consistent with the executive order's principles.

In addition to considering conforming amendments to update the CFTC's existing regulations, we also will examine the remainder of our rulebook consistent with the executive order's principles to review existing significant regulations. We intend to develop and make public a preliminary plan for the periodic review of significant regulations within the 120 day timeframe outlined in the executive order.

End-User Margin

One of the rules that the CFTC will consider pertains to capital and margin requirements. As it relates to margin, the Act states that, "to offset the greater risk to the swap dealer... and the financial system from the use of swaps that are not cleared," regulators shall "help ensure the safety and soundness of the swap dealer" and set margin requirements that are "appropriate for the risk associated with the non-cleared swaps."

Congress recognized the different levels of risk posed by transactions between financial entities and those that involve non-financial entities, as reflected in the non-financial end-user exception to clearing. Transactions involving non-financial entities do not present the same risk

to the financial system as those solely between financial entities. The risk of a crisis spreading throughout the financial system is greater the more interconnected financial companies are to each other. Interconnectedness among financial entities allows one entity's failure to cause uncertainty and possible runs on the funding of other financial entities, which can spread risk and economic harm throughout the economy. Consistent with this, proposed rules on margin requirements should focus only on transactions between financial entities rather than those transactions that involve non-financial end-users.

Conclusion

Before I close, I will briefly address the resource needs of the CFTC. The futures marketplace that the CFTC currently oversees is approximately \$40 trillion in notional amount. The swaps market that the Act tasks the CFTC with regulating has a notional amount roughly seven times the size of that of the futures market and is significantly more complex. Based upon figures compiled by the Office of the Comptroller of the Currency, the largest 25 bank holding companies currently have \$277 trillion notional amount of swaps.

The CFTC's current funding is far less than what is required to properly fulfill our significantly expanded mission. Though we have an excellent, hardworking and talented staff, we just this past year got back to the staff levels that we had in the 1990s. To take on the challenges of our expanded mission, we will need significantly more staff resources and – very importantly – significantly more resources for technology. Technology is critical so that we can be as efficient as an agency as possible in overseeing these vast markets.

The CFTC currently is operating under a continuing resolution that provides funding at an annualized level of \$169 million. The President requested \$261 million for the CFTC in his proposed fiscal year (FY) 2011 budget. This included \$216 million and 745 full-time employees for pre-reform authorities and \$45 million to provide half of the staff estimated at that time needed to implement the Act. The President is scheduled to release his FY 2012 budget request soon.

Given the resource needs of the CFTC, we are working very closely with self regulatory organizations, including the National Futures Association, to determine what duties and roles they can take on in the swaps markets. Nevertheless, the CFTC has the ultimate statutory authority and responsibility for overseeing these markets. Therefore, it is essential that the CFTC have additional resources to reduce risk and promote transparency in the swaps markets.

Thank you, and I'd be happy to take questions.