

UNITED STATES OF AMERICA  
COMMODITY FUTURES TRADING COMMISSION

GLOBAL MARKETS ADVISORY COMMITTEE MEETING

Washington, D.C.

Tuesday, October 5, 2010

1 PARTICIPANTS:

2 CHAIRMAN GARY GENSLER, CFTC

3 COMMISSIONER MICHAEL DUNN, CFTC

4 COMMISSIONER BART CHILTON, CFTC

5 COMMISSIONER JILL SOMMERS, CFTC

6 COMMISSIONER SCOTT D. O'MALIA

7 PATRICK PEARSON, European Commission

8 PETER KERSTENS, European Commission

9 COMMISSIONER KATHLEEN L. CASEY, SEC

10 YUKIHIRO MORI, Japanese FSA

11 CHIKAHISA SUMI, Japanese FSA

12 MICHAEL DAWLEY

13 BOB WASSERMAN

14 DAN BEKOVITZ

15 JACKIE MESA

16 DUANE ANDRESEN

17 DAVID VAN WAGNER

18 ANTHONY BELCHAMBERS

19 THOMAS CALLAHAN

20 GEORGE CRAPPLE

21 LAURIE FERBER

22 DONALD WILSON

1 PARTICIPANTS (CONT'D)

2 ROGER LIDDELL

3 BONNIE LITT

4 JIRO OKOCHI

5 DAN ROTH

6 JEFF SPRECHER

7 CONRAD VOLDSTAD

8 RICHARD BERLIAND

9 JOHN NIXON

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## 1 P R O C E E D I N G S

2 (1:10 p.m.)

3 COMMISSIONER SOMMERS: I want to thank  
4 the Global Markets Advisory Committee members for  
5 being here today. I know you all have a lot on  
6 your plates right now, so I want to say how much  
7 we appreciate you taking time out of your busy  
8 schedules to join us today to discuss a number of  
9 the important issues that we have before us at the  
10 CFTC. I also want to thank CFTC staff that have  
11 worked hard to put together the presentations that  
12 we have on our agenda today.

13 I'd like to welcome Patrick Pearson and  
14 Peter Kerstens from the European Commission. They  
15 were kind enough to join us last December at our  
16 GMAC meeting and they're here again today to  
17 continue the discussion on coordinating our  
18 financial reform globally, and so I want to thank  
19 them also for being here.

20 I also want to welcome two guests from  
21 the Japanese FSA, Mr. Sumi and Mr. Mori, who are  
22 here to update us on legislation that passed in

1 Japan earlier this year regarding OTC derivatives.  
2 I want to welcome also SEC Commissioner Kathy  
3 Casey, who is with us today and, as you all know,  
4 is very active in global coordination on financial  
5 regulatory issues.

6 I'd like to start by asking if the GMAC  
7 committee members could go around the table and  
8 introduce themselves and their affiliation and  
9 then I will turn my colleagues on the dais. If we  
10 could start with Don.

11 MR. WILSON: I'm Don Wilson. I'm the  
12 founder and CEO of DRW Trading which is a  
13 principal trading group. I am also one of the  
14 founding members of the Eris Exchange which is a  
15 futures exchange that has listed swap futures and  
16 clears them at the CME.

17 MR. SPRECHER: I'm Jeff Sprecher. I'm  
18 the CEO of Intercontinental Exchange.

19 MR. OKOCHI: I'm Jiro Okochi, CEO of  
20 Reval. We provide derivatives solutions to about  
21 400 end users.

22 MS. LITT: I'm Bonnie Litt. I'm an

1 attorney at Goldman Sachs.

2 MS. FERBER: I'm Laurie Ferber, General  
3 Counsel at MF Global.

4 MR. CALLAHAN: I'm Tom Callahan. I'm  
5 the CEO of NYSE Liffe U.S. which is the U.S.  
6 derivatives business of NYSE Euronext.

7 MR. BELCHAMBERS: I'm Anthony  
8 Belchambers, CEO of the European Futures and  
9 Options Association.

10 MR. CRAPPLE: I'm George Crapple. I'm  
11 co-CEO of Milburn Ridgefield CTA/CPO.

12 MR. LIDDELL: I'm Roger Liddell, CEO of  
13 LCH Clearnet.

14 MR. NIXON: I'm John Nixon, Executive  
15 Director of ICAP.

16 MR. ROTH: I'm Dan Roth, CEO of National  
17 Futures Association.

18 MR. VOLSTAD: I'm Conrad Volstad and I'm  
19 the CEO of ISDA.

20 MR. BERLIAND: I'm Richard Berliand,  
21 head of market structure and prime services at JP  
22 Morgan.

1           MR. MORI: I'm Yukihiro Mori, from  
2 Japanese FSA.

3           MR. SUMI: I'm Chikahisa Sumi from  
4 Japanese FSA. Thank you for your invitation.

5           COMMISSIONER SOMMERS: Thank you so much  
6 for being here. I think we may have Mike Dawley  
7 who is the Chairman of the Futures Industry  
8 Association on the phone. Mike, are you on the  
9 phone?

10          MR. DAWLEY: Yes, I'm on.

11          COMMISSIONER SOMMERS: Thank you for  
12 participating with us today. I'm going to go over  
13 a couple of housekeeping items and then I'm going  
14 to turn to my colleagues for any opening  
15 statements. I'd like to let you know that as for  
16 the microphones you push to talk, and if you could  
17 push after you're finished with your remarks.  
18 There can only be so many microphones on at the  
19 same time so I ask you to turn those off after  
20 you've finished speaking. If you would like to  
21 make a remark or have a question or comment, if  
22 you can put your name tent up to be recognized.

1 Finally, for the reporter doing the transcript  
2 today, if everyone could identify themselves  
3 before they speak that's very helpful.

4 I'd like to it over to Chairman Gary  
5 Gensler for any opening statements.

6 CHAIRMAN GENSLER: Thank you,  
7 Commissioner Sommers for chairing today's meeting.  
8 I just turned to Commissioner Sommers as you were  
9 introducing yourselves and said this is really an  
10 extraordinary group of people to be in one room at  
11 the same time. Many of you came in and chatted  
12 with us before the Dodd-Frank bill and now that  
13 it's passed. I thank you each for your service  
14 because I know I benefit and I think staff  
15 benefits and I'm sure our Commissioners benefit  
16 from your expertise.

17 We're hard at work at this and I want to  
18 also thank my fellow Commissioners for everything  
19 that they're doing, and Kathy you're here too, so  
20 thanks to everything the SEC is doing because we  
21 have so many joint rules with the SEC. We're  
22 moving forward to harmonize our rules with the SEC



1 so it's terrific to have Kathy with us. Sometimes  
2 we need an odd number to sort through things. I  
3 also want to thank the members of the Japanese  
4 Financial Services Authority and the European  
5 Commission. I've worked a little bit more closely  
6 with the European Commission recently but I lived  
7 in Japan for 3 years so maybe that will up for the  
8 fact that I haven't been to visit yet in my stead  
9 here. Japan passed their derivatives reform bill  
10 first in I think it was May, the European  
11 Commission just released their proposals and I  
12 look forward to coordinating in consultation with  
13 each jurisdiction as we implement the reform. We  
14 benefit from a very strong working relationship  
15 across the oceans. Last week I traveled to  
16 Brussels to meet with members of the European  
17 Commission and spoke at a conference at their  
18 request. As we had in Dodd-Frank, the European  
19 proposal covers the entire derivatives marketplace  
20 both bilaterals and cleared swaps. It's the whole  
21 product suite. The Japanese proposal as well  
22 includes the requirement that certain derivatives

1 be centrally cleared and that's where the European  
2 proposal is. I'm sure we'll hear more from  
3 Patrick and Peter on that. And it's where we are.  
4 So though we have different political systems and  
5 different cultures, we have a remarkable consensus  
6 here between the largest markets. Clearinghouses  
7 have worked since the late 19th century. They're  
8 not perfect but they really do lower risk through  
9 clear skies and through difficult times like the  
10 2008 crisis. The U.S., European and Japanese  
11 proposals all recognize though the need for very  
12 robust risk-management standards. We were  
13 chatting a little bit about this socially at  
14 lunch. I think that we certainly recognize this  
15 here and I know those do around the globe.

16 Also the Dodd-Frank Act and the various  
17 proposals in Europe and in Japan recognize that  
18 the dealers themselves have to have the necessary  
19 capital to stand behind these trades, whether it  
20 be through collateral requirements or margin  
21 requirements, that markets will have lower risk  
22 with that. All three proposals also have

1 requirements that transactions be reported to swap  
2 data repositories. As we write the rules  
3 regarding the clearing requirement, our staffs are  
4 going to look closely to the European and Japanese  
5 proposals to ensure consistency. We are also  
6 looking to the CPSS-IOSCO standards and certainly  
7 the work Kathy is doing not just there but on the  
8 FSB which we'll hear about because the consistency  
9 in bringing these rules together is so critical.  
10 At today's meeting I at least looking forward to  
11 hearing the views on the global financial  
12 regulatory system. Specifically I'm looking  
13 forward to hearing not only how we move forward in  
14 the U.S. but how we move forward in the U.S. to be  
15 consistent with what people are doing overseas,  
16 and in terms of the swap data repositories what  
17 data do we need to require. We're going to go  
18 before the Europeans so that in the next 8 to 10  
19 weeks we'll be putting rules along with the SEC on  
20 swap data repositories and I think it's incumbent  
21 upon us where we can to include data that the  
22 European and the Japanese markets also need, and

1 as to clearinghouses as well to meet rigorous  
2 risk-management standards though we hope to be  
3 able to comply with all the IOSCO principles and  
4 are there specific principles from Europe or from  
5 Asia that you see that we need to do because at  
6 some moment in the future, maybe it's 2 or 3 years  
7 from now, we're going to want to make sure that  
8 the clearinghouses that we regulate meet the  
9 equivalency standard in Europe. Also we're going  
10 to look to ultimately negotiate international  
11 arrangements. The statute does give this  
12 Commission and the SEC authority to negotiate  
13 international arrangements for information sharing  
14 and we want to make sure that that can be done in  
15 a way that regardless where a data repository is  
16 that information can be shared amongst regulators.

17 I know that Commissioner Sommers also  
18 put on this agenda to talk about foreign boards of  
19 trade and that's a very important matter. I think  
20 that we have I can't recall 15 or 20 foreign  
21 boards of trade that currently have no action  
22 regimes and as we move forward with rule writing

1 in that area it would be very helpful to hear  
2 people's thoughts on that. Again I thank you and  
3 I thank everybody for being here.

4 COMMISSIONER SOMMERS: Commissioner  
5 Dunn?

6 COMMISSIONER DUNN: Thank you. The  
7 world we live in today is smaller and more  
8 interconnected than at any time in our history.  
9 Financial events taking place in the United States  
10 are like skipping stones across oceans sending  
11 ripples through markets in Europe and Asia. The  
12 United States cannot stand alone in an effort to  
13 bring transparency to the over-the-counter markets  
14 and in crafting best practices for risk management  
15 in the financial industry. If we are to make  
16 financial reform meaningful and effective, we must  
17 tackle these issues hand in hand with our sister  
18 regulators in the world. Only together can we  
19 accomplish the ultimate goal of creating a secure,  
20 stable and productive financial system. I would  
21 like to thank Chairwoman Sommers and her staff for  
22 all the work in this area. The panelists she has

1 assembled here from throughout the financial world  
2 to discuss the new OTC and clearing paradigms is  
3 impressive and I look forward to hearing the  
4 thoughts of our distinguished speakers.

5 As the world reacts to the recent  
6 financial crises that threatened everyone's  
7 economic stability, it has become apparent that  
8 prudential regulators from all countries need to  
9 better communicate and harmonize their efforts.  
10 Additionally I would like to welcome Kathleen  
11 Casey to this meeting as the past Chairman of the  
12 IOSCO Technical Committee in work on the FSB. Her  
13 insights into today's topics will undoubtedly be  
14 very, very valuable.

15 I'd like to recognize the tremendous  
16 work done by our Office of International Affairs  
17 under the leadership of Director Jacqueline Mesa.  
18 Although understaffed, this office has done an  
19 excellent job in representing the CFTC around the  
20 world. Lastly, I would like to thank Chairman  
21 Gensler for all of his efforts in advocating for  
22 greater international regulatory oversight and

1 harmonization and I urge him to get to Japan soon.

2           As we begin to implement the Dodd-Frank  
3 legislation I would again stress the importance of  
4 U.S. Regulatory agencies working in concert with  
5 regulators around the world as opposed to acting  
6 unilaterally. The world's bodies such as the  
7 G-20, the FSB and IOSCO are already working on  
8 financial reform and it is imperative that we  
9 understand the directions they are heading. I am  
10 hopeful at today's meeting that GMAC members will  
11 be able to shed some light on actions taken  
12 internationally and share their concerns and  
13 recommendations with this Commission. My hope is  
14 that regulatory cooperation between countries with  
15 substantial assistance from market users will lead  
16 us to developing a set of compatible financial  
17 regulations used throughout the world. Only by  
18 working together can financial regulators create  
19 an adequate structure for the over-the-counter  
20 markets that promote stability and transparency  
21 while at the same time discourage any type of  
22 regulatory arbitrage. Thank you all for your

1 participation today.

2 COMMISSIONER SOMMERS: Thank you,  
3 Commissioner Dunn. Commissioner Chilton?

4 COMMISSIONER CHILTON: Thanks. Thank  
5 you all for being here this afternoon. I could  
6 echo what both Chairman Gensler and all of my  
7 colleagues have said so far, but I'll put it in a  
8 little bit different way and then I have something  
9 that's different.

10 This watch that I have is one of my  
11 favorite watches. It's an Omega that is similar  
12 to that that Neil Armstrong wore on the moon and  
13 there's a picture from the moon. Neil Armstrong  
14 is the one who had the camera on the front of his  
15 space suit so you can see Buzz Aldren with this  
16 watch. Dave Stawick who is our secretariat here  
17 is our expert on space and he has one of them too.  
18 Those pictures that Armstrong took of the Earth  
19 from up in space made it look so small, you could  
20 see Europe and North America and you could see  
21 Africa and Asia, and even though we have folks  
22 here who have come from London, Anthony and maybe



1 Jeff, and from Asia, our friends from Japan, in  
2 the trading world it is really microseconds away.  
3 It's a small world as they say and that's why what  
4 we're doing here is so important. It's nice that  
5 we've moved forward on our law and others have  
6 moved forward, but as the flash crash report  
7 taught us last week, these markets are really  
8 interrelated. They're interrelated domestically  
9 in the U.S., but had that crash happened earlier  
10 in the day when the European markets were open it  
11 could have rocked the global financial world so  
12 that we're inextricably linked. I agree with all  
13 my colleagues that we need to work better to go  
14 forward on parallel not necessarily identically,  
15 but parallel policy objectives at least. What we  
16 don't want to have happen is have regulatory  
17 arbitrage. That is a race to the regulatory  
18 bottom where traders go to the least-transparent  
19 and the last-regulated places. I don't think that  
20 would be good for anyone.

21 The other thing that I wanted to mention  
22 is that we've reached a milestone in the U.S. this

1 week that was the end to the Troubled Assets  
2 Relief Program as we know it where nobody could  
3 come in and get bank bailout funds anymore. It's  
4 still not paid off yet, but we can't make them  
5 anymore. It comes to us and our brethren at the  
6 SEC to ensure that whatever we do under the new  
7 law doesn't have a new systemic risk and doesn't  
8 have the possibility for a new bailout. I'm  
9 specifically concerned about what we do with  
10 clearinghouses, that we need to ensure that  
11 they're safe, sound and secure and that they  
12 aren't a place where taxpayers could ultimately  
13 have to bail out these things. Quite frankly,  
14 even though we have the wherewithal to provide the  
15 regulatory constructs to set up safe, sound and  
16 secure clearinghouses, we may not have the money.  
17 A lot of us talked about this in the last several  
18 days about how imperative it is for us to have the  
19 money not just to ensure that we're meeting the  
20 intent of Congress with regard to the Wall Street  
21 Reform Act, but that we're protecting taxpayers  
22 with regard to ensuring we don't set up new

1 systemic risk in the form of clearinghouses.

2 Thank you again for being here. I know  
3 it may not seem like a small world when you have  
4 to travel 20 hours, but we appreciate the fact  
5 that you're with us. Thank you.

6 COMMISSIONER SOMMERS: Thank you,  
7 Commissioner Chilton. Commissioner O'Malia?

8 COMMISSIONER O'MALIA: Thank you to all  
9 our participants, guests from Europe and Japan.  
10 Mister Chairman, if it's any consolation I did go  
11 to Japan but I made you pay for it so that you  
12 were well represented.

13 CHAIRMAN GENSLER: Thank you,  
14 Commissioner O'Malia.

15 COMMISSIONER O'MALIA: My colleagues  
16 have obviously stated the importance of working  
17 internationally and cooperatively to implement the  
18 detailed reforms passed by Japan and proposed by  
19 Europe as well as the reforms that have been  
20 implemented here and I look forward to continued  
21 dialogue to make sure that our regulations are  
22 harmonized to ensure that we're able to mitigate

1 systemic risk, increase transparency through trade  
2 reporting and continue to provide cost-effective  
3 solutions for the management of risk.

4 I'm going to end here and I want to  
5 reiterate my strong support that I'm glad you're  
6 having this hearing and compliment our CFTC staff  
7 for their participation, Jackie, your staff for  
8 keeping us well informed on international matters  
9 and I look forward to the presentations today.

10 COMMISSIONER SOMMERS: Thank you. GMAC  
11 was created over 12 years ago to provide a forum  
12 for the Commission so that we could hear from  
13 market participants regarding the globalization of  
14 futures markets and to discuss regulatory and  
15 competitive issues. At that time screen-based  
16 trading was just in its infancy and although so  
17 much has changed over the past decade, it's always  
18 been important for this Commission to participate  
19 in international organizations and to coordinate  
20 with our colleagues around the globe regarding  
21 futures regulation.

22 I think all of those efforts have been

1 very successful and now it's time for us to build  
2 upon those relationships and to participate in  
3 global consultations on regulations for the OTC  
4 derivatives markets. We'd like to create a  
5 transparent and sound regulatory environment  
6 around the world. The products are different and  
7 they may not fit into the regulatory models that  
8 we're all very familiar with and that we're  
9 operating under now, but many of the issues that  
10 have been identified such as clearing,  
11 standardization, trade repositories, data  
12 collection, all require close coordination between  
13 regulatory agencies to determine the appropriate  
14 policy response. That's why I believe it's so  
15 important that we have both the European  
16 Commission and the Japanese FSA as well as the SEC  
17 here today with us to discuss these important  
18 issues.

19 I'd now like to turn to Patrick Pearson  
20 who is the head of Financial Markets  
21 Infrastructure Unit at the European Commission for  
22 him to give a presentation on the legislative

1 proposal that was introduced I think September 15  
2 formally. Patrick?

3 MR. PEARSON: Thank you, and thank you  
4 to the Chair of the GMAC, Commissioner Sommers and  
5 the other Commissioners of the CFTC for this  
6 invitation. I don't have an expensive watch like  
7 Commissioner Chilton.

8 COMMISSIONER CHILTON: I didn't say that  
9 it was expensive, that it was unique.

10 MR. PEARSON: Believe me, sir, it's  
11 expensive in its uniqueness.

12 COMMISSIONER CHILTON: I went to Japan  
13 also.

14 MR. PEARSON: I'm encouraged by your  
15 words and your inspiration and Commissioner Dunn  
16 as well. And without an expensive watch and  
17 coming from the Old World, all I have to carry  
18 with me is words and so I'll inject some of my  
19 comments with the words that I bring with me and  
20 I'll try and give you some inspiration from  
21 Shakespeare as we go along so that you know what I  
22 was doing for 8 hours in the airplane yesterday,

1 it was not reading Dodd-Frank, it was brushing up  
2 my Shakespeare.

3 Let me start off with a quote from  
4 "Julius Caesar" when he said, "Friends, Romans,  
5 countrymen, lend me your ears." I think that is  
6 quite appropriate today because what we're  
7 discussing today is not a small matter that is  
8 restricted to one or two of our jurisdictions,  
9 it's something that actually I believe is of  
10 importance to everybody around the table,  
11 everybody in this room and many other people  
12 beyond this room; the regulation, regulatory  
13 responses to some of the mishaps and misfortunes  
14 we encountered in mid-2007.

15 The word regulation is quite appropriate  
16 because in July as you said the U.S. Congress  
17 passed Dodd-Frank, 2 weeks ago the European  
18 Commission released its regulatory proposal on OTC  
19 derivatives on swaps, and these regulations. You  
20 call yours an act, we call ours a regulation, but  
21 these are legislative statutes because nothing can  
22 come of nothing and that was "Lear" by the way.

1 We need a regulatory response because these are  
2 issues that require public authority and public  
3 leadership and self- regulation in this area we  
4 believe in Europe, we believe and also the G-20 is  
5 quite clear about, will not deliver what we're  
6 looking for.

7 In our proposal 2 weeks ago we  
8 identified three important priorities, regulate  
9 the dealers, require standardized derivatives to  
10 be cleared by regulated clearinghouses and  
11 thirdly, require all trades to be reported to  
12 registered trade repositories. You will say there  
13 is something missing and that's true because our  
14 proposal is part of a triptych of measures, three  
15 measures, not one. There will be two other  
16 regulators measures in Europe. The first is to  
17 regulate trading and require standardized swaps to  
18 be traded on trading venues. We're working on  
19 that. There will be consultation, impact  
20 assessment in the next 3 months and the  
21 legislative proposal beginning next year and the  
22 legislative proposal will be called MIFID review.



1 We don't have sexy acronyms but people really  
2 should understand the importance of the MIFID  
3 review beginning next year. That is where we will  
4 regulate the trading, that is where we will  
5 regulate position limits and a host of other  
6 measures.

7           And there is a third measure and that is  
8 capital, that is, require the banks to meet high  
9 minimum capital requirements for noncleared  
10 trades. This is part of the revision of the Basel  
11 Agreement, Basel III, and that third proposal will  
12 be put on the table at the end of this year.  
13 Unlike Dodd-Frank, there will be three regulatory  
14 measures in Europe so that there is method to this  
15 madness, and the connoisseurs that was Polonius  
16 from "Hamlet." There is method to this madness  
17 and it is quite important because there is some  
18 misunderstanding. There are those who say Europe  
19 is not moving in tandem with the United States,  
20 there are things missing from our regulatory  
21 approach. That is wrong. We're doing things  
22 different for different reasons but the idea is to

1 end up in the same space.

2 Before I make some preliminary remarks  
3 comparing Europe to the USA on swap regulation,  
4 two initial comments. The first is past is  
5 present, the famous Shakespeare quote and quite  
6 important because we're all at the global level  
7 seeking solutions to the same problems because we  
8 suffered the same consequences as colleagues in  
9 the United States, Japan and other parts of the  
10 globe, the same regulatory failure, the same  
11 regulatory myopia and the same economic downturn  
12 so that we're in this together.

13 My second comment is Europe and the  
14 United States of America have different regulatory  
15 systems. We have different institutions. My  
16 point is keep your eye on the ball. There are a  
17 lot of people out there who are trying to make a  
18 living out of finding differences between our  
19 regulatory approaches and I agree with the  
20 Commissioners is the one thing we cannot afford is  
21 a different regulatory outcome. My advice to you  
22 is focus on the product, not on the process --

1 focus on the product, not on the process and look  
2 at what the words on paper say in the different  
3 jurisdictions. Then come to a judgment whether  
4 Europe and Japan and other parts of the globe and  
5 the U.S. are different are not. Keep your eye on  
6 the ball, look at the product and not the process.

7 My first point is what we're trying to  
8 do in Europe is increase safety in the system,  
9 regulate the dealers. How are we going to do  
10 that? Four points. First, the rules that we put  
11 out 2 weeks ago cover the entire product suite for  
12 clearing and reporting of swaps. The entire  
13 product suite. That means interest rate swaps,  
14 currency, commodity, equity and credit default  
15 swaps. The whole suite with no exception. The  
16 same as in Dodd-Frank. Secondly, we want robust  
17 margining requirements, real margining  
18 requirements fully collateralized at least in --  
19 collection similar to Dodd-Frank. Thirdly, the  
20 bilateral, the noncleared transactions. We're all  
21 aware of the fact that there is only so much you  
22 can standardize, there is only so much that can be

1 cleared. For the uncleared transactions, we will  
2 require margin or capital, mark to market daily,  
3 robust risk-management arrangements, again  
4 operational risk and credit risk, electronic  
5 confirmation, portfolio reconciliation obviously  
6 -- resolution, and this is where it's interesting  
7 to look what Dodd-Frank says because the only  
8 difference we've been able to identify is that  
9 where we say we want margin or collateral,  
10 Dodd-Frank says margin and collateral.

11 Interesting. But that's as far as the difference  
12 goes. Section 731 for the connoisseurs of  
13 Dodd-Frank.

14 Segregation. Both Europe and the U.S.  
15 require segregation. In Europe you must have  
16 segregation. In the U.S. you may have segregation  
17 but held as an independent custodian so that  
18 they're similar approaches. And my fourth point  
19 on regulating the dealers is address conflicts of  
20 interest. Absolutely critical if you look at the  
21 European regulation. You have six whole  
22 provisions in that text on conflicts of interest.

1 We focus on governance, we focus on ownership. We  
2 want shareholders and clearing members with a  
3 significant interest to have regulatory approval.  
4 Intrusive. That means any major shareholder that  
5 wishes to acquire more than 10 percent or 20 or 30  
6 percent in the CPP must have regulatory approval  
7 subject to very clear conditions. Are there  
8 conflicts of interest? Is the ownership conducive  
9 and propitious to the safety of the system? And  
10 the regulators will have the power to not approve  
11 ownership if it impinges on sound and prudent  
12 management. We also want all of our  
13 clearinghouses to have very clear and public and  
14 transparent written arrangements to identify  
15 potential conflicts of interest. Again here,  
16 very, very similar to Dodd-Frank. There's one  
17 issue that is not similar and that is the  
18 proposition that the regulatory authorities in the  
19 U.S. may ownership caps and limits. We don't have  
20 that, but if that's the only difference I ask you  
21 how big a difference is that?

22 Let's move on to a second point,

1 mandatory central clearing. What are we going to  
2 do in Europe? Require central clearing of all  
3 eligible contracts. Dodd- Frank does the same.  
4 It just calls it clearable contracts. Why didn't  
5 we use the word clearable? Because we were told  
6 by the Brits that it's not an English word, that  
7 it doesn't exist. I'll reserve my judgment, but  
8 we were told the word is eligible. If that's the  
9 biggest difference -- in Europe the regulation  
10 applies to all eligible contracts of specific  
11 counterparties. Very simple. And that is quite  
12 important though. If you look at the first  
13 provision in the European law, it's point of  
14 departure is to regulate the entities, the  
15 counterparties. It says that every single bank,  
16 savings bank, cooperative bank, mutual, investment  
17 bank, life insurance company, long life insurance  
18 company, pension fund, hedge fund, every regulated  
19 financial entity in Europe will be subject to the  
20 clearing requirement. Juxtapose this to  
21 Dodd-Frank. It doesn't use the regulatory  
22 approach at the beginning, it focuses on the swap

1 contract. Is that a big difference? No. It's a  
2 different regulatory point of departure, but where  
3 we end up is in exactly the same space. So why  
4 didn't we use the U.S. approach? Very simple.  
5 Because in our discussions with the U.S. Treasury  
6 and the Congress it became very clear to us that  
7 the U.S. regulators had to follow that approach  
8 based on the swap contract for the reason that  
9 they had a lot of difficulty in using the point of  
10 departure of the regulated entity because the  
11 legislation simply wasn't in place at that time.  
12 In Europe it's much easier to focus on the  
13 departure of the regulated entity because we have  
14 all of that legislation in place and it's very  
15 easy to build on that building block.

16 Dodd-Frank allows commercial end users  
17 to opt out of clearing. Fine. We only require  
18 clearing for commercial end users if positions  
19 exceed a threshold. A different point of  
20 departure but we end up in the same space. For a  
21 number of reasons first through the back door of  
22 the commercial entities can be required to clear

1 if they're considered to be major swap  
2 participants. In Europe, commercial entities can  
3 be required to clear if they meet a certain  
4 threshold. The whole idea is that the European  
5 threshold and the definition of major swap  
6 participant in the end converge so that you have a  
7 different way of achieving exactly the same  
8 objective. And Europe and the USA are analogous  
9 as well if you look at the European legislation  
10 and if you look at Dodd-Frank by excluding  
11 corporate exposures that are directly linked to  
12 their commercial activity. Exactly the same  
13 approach in two jurisdictions.

14 A final point. The process and the  
15 framework for determining which contracts must be  
16 cleared, clearable or eligible, are remarkably  
17 similar in both regulatory approaches. CCPs can  
18 submit for regulatory review the contracts they  
19 seek to clear, the approach in Europe and the same  
20 approach here in the U.S. And regulators are  
21 authorized to identify additional contracts to  
22 mandate for clearing even if they're not already



1 cleared by a CCP clearinghouse. The same in  
2 Europe, same in the U.S. Different words. The  
3 U.S. legislation is more lengthy and laborious and  
4 has several sub-sentences which reek of Teutonic  
5 drafting in Germany to us in Europe, but they all  
6 say the same thing in the end. And the criteria  
7 the regulators have to take into consideration in  
8 determining clearing eligible and clearable are  
9 remarkably similar. Look at the texts. The same  
10 criteria with one difference. Dodd-Frank adds an  
11 additional criteria or two. First, there has to  
12 be an effect on competition. We don't have that  
13 criteria in Europe. Why not? Because we don't  
14 need it because we have an autonomous competition  
15 power under the treaty for the Commission to  
16 intervene in cases of negative effects on  
17 competition. The second difference, the only  
18 difference we could find when plowing through  
19 Chapters 7 and 8 of Dodd-Frank was the existence  
20 of significant outstanding exposures. That's the  
21 only difference in comparing the clearable and the  
22 clearing eligible approaches between Europe and

1 the U.S. Remarkably similar.

2 I'll move on to my third point is that  
3 is regulation of CCPs because if mandatory  
4 clearing comes around, we will shift significant  
5 amounts of swap contracts onto CCPs. We will not  
6 be removing risk from the system, we will be  
7 moving risk in the system. We will be moving risk  
8 from the banks' books to the clearers'. That's  
9 good. That's fine. That's what we want. That  
10 brings safety to the system. We never again want  
11 to be in a position where liquidity dries up  
12 because financial institutions have no confidence  
13 in each other. We move the risk off the books of  
14 the banks into the CCPs. That raises one problem  
15 and that is from our perspective in Europe these  
16 clearinghouses must be able to withstand financial  
17 Armageddon. They must be absolutely, safe  
18 absolutely sound, the words of Commissioner  
19 Chilton a moment ago. That is why if you look at  
20 the CCP standards enumerated in the European  
21 regulation, they're pretty detailed. They're in  
22 fact one area of regulation where Europe is more

1 detailed than the U.S., far more detailed. We  
2 will require minimum capital. We will define what  
3 the capital is. We will define margin  
4 requirements. We will require horizons. We will  
5 require default -- we will require a mandatory  
6 default fund and so forth and so forth and so  
7 forth. In eurospeak we harmonize the regulatory  
8 licensing requirements for CCPs to the very, very  
9 highest standard possible.

10 But it remains to be seen if that  
11 difference between the European legislation and  
12 Dodd-Frank continues as colleagues in the SEC and  
13 the CFTC work out this in rulemaking in the U.S.  
14 Why is that important? I'll tell you why.  
15 Although we have broadly similar rules for CCPs,  
16 we need to have more convergence in this area  
17 because of the slightly different approaches that  
18 Dodd-Frank and the European Union apply to  
19 regulating foreign-domiciled CCPs. There are two  
20 points, because Dodd-Frank's registration  
21 requirements apply to all CCPs regardless of the  
22 location and the CFTC and the SEC can exempt a CCP

1 from registration if it's subject to comparable,  
2 comprehensive supervision and regulation. So far  
3 so good. In Europe we require CCPs established  
4 outside of Europe to be recognized subject to  
5 certain conditions including the determination  
6 that the CCP is subject to equivalent standards.  
7 So again you see remarkable convergence in how we  
8 approach this. The United States uses the  
9 laborious terminology comparable, comprehensive  
10 supervision and regulation, and in Europe we have  
11 one word, equivalent which means exactly the same.  
12 So it's quite important that those details in  
13 Dodd-Frank to ensure the safety and soundness of  
14 CCPs are comparable and comprehensive and  
15 equivalent to what we have in Europe.

16 A last point on regulation of CCPs,  
17 segregation and portability. What we will  
18 introduce in Europe are a couple of very important  
19 things for CCPs, clearing members and obviously  
20 for the clients. CCPs will have to segregate  
21 their own assets from those of the clearing  
22 members. Pretty simple. Pretty obvious. We want

1 CCPs to segregate the assets and positions between  
2 the clearing members for pretty good reasons. We  
3 want the clearing member itself to segregate its  
4 assets and positions from those of its clients for  
5 pretty good reasons. We've seen some bad things  
6 happen over the past 2-1/2 years. And we want  
7 CCPs to give the option to clients for more  
8 granular segregation, the option, disclosing the  
9 risk, disclosing the costs, it's cheaper to have  
10 an omnibus account, we know that, but we want the  
11 clients to have the option for greater granularity  
12 in the segregation. And portability. We will  
13 want CCPs to be able to transfer assets and  
14 positions between the clearing members. Many have  
15 said this is pretty hairy because this touches on  
16 bankruptcy rules and regulations and it's  
17 difficult enough in the U.S. Where you have one  
18 bankruptcy code. Come to where I live where I  
19 have 27 bankruptcy codes. This is where you see  
20 the phenomenal power of European regulation.  
21 There is one sentence in Europe's regulation that  
22 says we don't care. We say you will allow a CCP

1 to transfer assets and positions between the  
2 clearing members regardless of whatever any  
3 national bankruptcy law says so that the European  
4 law overrides any contradictory requirement in  
5 national law. Segregation and portability,  
6 similar, not identical but very similar to the  
7 approach considered in the U.S.

8 That brings me to my final point,  
9 increased transparency. We've spoken about  
10 clearing, we've spoken about the need to regulate  
11 the dealers, the clearing mandate, the regulation  
12 of CCPs. I want to talk about transparency and  
13 trade repositories. Like Dodd-Frank, Europe will  
14 require the reporting of trades into a trade  
15 repository. No difference except the scope of the  
16 reporting requirement differs slightly at this  
17 point in time. Dodd-Frank requires all trades to  
18 be reported to a trade repository. Europe exempts  
19 those contracts, those trades between two  
20 corporates. A trade between two corporate  
21 entities is exempt from a reporting requirement.  
22 That's quite interesting because the comprehensive

1 approach in Dodd-Frank where even a  
2 corporate-corporate contact would need to be  
3 reported to a trade repository is not followed in  
4 Europe. Why is that? Two reasons. The first,  
5 when we did our impact assessment and we spoke to  
6 the corporates, it was very clear that most of the  
7 contracts are two financials or between a  
8 financial and a corporate. The financial  
9 corporates, I think we're looking at 17.3 percent  
10 of the contracts as of the end of last year, the  
11 corporate-to-corporate contracts we found were  
12 almost difficult to find if at all. They do exist  
13 but they're absolutely minimal in their volume and  
14 the impact assessment determined that the  
15 cost-benefit analysis of requiring these  
16 corporates to put a reporting framework in place  
17 would be disproportionate so that they're exempt  
18 at this point in time. Timeframe for reporting?  
19 Anything as long as it's not longer than 24 hours  
20 and that could be, I don't know, 5, 10, 15 minutes  
21 for block trades, up to 24 hours for more complex  
22 trades.

1           The further details of the report, the  
2   format, the content, these will be subject to what  
3   we call implementing rules in Europe and that's  
4   pretty important. These rules are very similar to  
5   what the SEC and the CFTC put in place because  
6   what use is it if European counterparties report  
7   trades to a trade repository in a slightly  
8   different format than those reported in the U.S.  
9   Or in Japan? So that reporting format, the  
10  reporting framework, must be absolutely similar  
11  when convergence doesn't cover the term there.  
12  They probably have to be as similar and identical  
13  as possible with one objective, to allow the  
14  regulators, to allow the market to have a  
15  comprehensive overview of the risks and the  
16  position in the system.

17           On trade repositories we've got some  
18  pretty granular and detailed rules to regulate  
19  them. We have rules on governance. We have rules  
20  on systems. We have rules on senior management.  
21  They've got to be fit and proper. We have rules  
22  on access. We have rules on price disclosure. We



1 have rules on fee disclosure including discounts  
2 including rebates. We have rules on safeguarding.  
3 We have rules on recordkeeping for trade  
4 repositories. We have rules on transparency. And  
5 we have rules on data availability. And both  
6 Dodd-Frank and Europe require trade repositories.  
7 No difference. The only difference is that Europe  
8 allows third-country trade repositories, and  
9 there's one that I can think of in the U.S. at  
10 this point in time, to be active in Europe  
11 provided it's recognized as being subject to again  
12 equivalent regulation in its home country. So  
13 we've got exemptive relief for trade repositories  
14 coming into Europe and digging through Dodd-Frank  
15 we found one other area where there is a slightly  
16 different approach. There is no exemptive relief  
17 for trade repositories in the U.S. so there's a  
18 possibility of double-registration requirements  
19 for at least four European trade repositories  
20 wishing to do their services in the United States  
21 of America.

22 One final comment and this is quite

1 important. European regulation proposes the  
2 existence of an international agreement between  
3 Europe and third countries for mutual access to  
4 information and exchange of information in a trade  
5 repository. Again there is method to that  
6 madness. This harkens back to March of this year  
7 where there was an unfortunate hiccup and some  
8 unfortunate events where a number of European  
9 regulators had some difficulty in accessing  
10 information in a trade repository outside of  
11 Europe. And the very, very, very clear comment  
12 from our Congress and our ministers was this is  
13 once but never ever again. So when you look at  
14 this, what were the options we were faced with in  
15 Europe? Require all trade repositories to locate  
16 in Europe? It's a pretty simplistic approach.  
17 But if you look at it, it doesn't really make a  
18 lot of sense. That's why the option that we've  
19 put in the proposition and the regulation is you  
20 don't have to have a location requirement as long  
21 as there is a guarantee, an international  
22 arrangement, with third countries that there is a

1 guarantee that the regulators can access that  
2 information in a trade repository even if it's  
3 located outside of Europe. And I'm encouraged by  
4 the comments from Chairman Gensler that he has the  
5 locus to actually engage in this type of  
6 arrangement which is very, very important. I'll  
7 conclude. I have four comments to leave with you.  
8 Europe and the U.S. are very, very similar in  
9 scope, application and requirements. Are there  
10 differences? Yes. Frankly, I wouldn't only be  
11 surprised, I'd be pretty annoyed if there were no  
12 differences because it means that we couldn't  
13 implement half of Dodd-Frank in Europe, A, because  
14 it's not proper English according to my native  
15 English speakers, B, because it uses words we have  
16 no idea what that mean but we will be enlightened  
17 by the SEC and the CFTC as to what some of these  
18 words mean like SEFs and MSPs and what-have-you.  
19 But I'll tell you one thing. I not only read  
20 Shakespeare yesterday on the flight coming over,  
21 you got a pretty idea that I was also plowing  
22 through Dodd-Frank and I actually had to detect

1 the differences with a Maglight. I flew business  
2 class and I have one of these strange lights that  
3 come out of the seat and you have to really focus  
4 it and it's a LED light on the text. I had a  
5 great deal of difficulty finding the differences  
6 between our piece of legislation in Europe and  
7 Dodd-Frank. You really have to go through this  
8 with a Maglight.

9           The differences I've just indicated to  
10 you are really not fundamental, they're in detail,  
11 and I'm quite sure that some of the differences  
12 probably came through regulatory mishap. Speaking  
13 to come of the staffers and the congressmen there  
14 was a lot of pace and speed in the final days of  
15 the regulation in Congress, and I'm sure I know  
16 I've been told some of the differences actually  
17 were because of the need to get this text out and  
18 agreed in the U.S. But a lot of these differences  
19 can be considered and there is room and scope to  
20 minimize these differences even further as our  
21 work on implementing the rules continues on both  
22 sides of the Atlantic.

1           My second point is we are converging, we  
2 are not competing, convergence, not competition in  
3 regulation, and we are looking closely at the SEC  
4 and the CFTC rules as they develop to ensure there  
5 is consistency, consistency between Europe and the  
6 U.S. and wider, the G-20, the Financial Stability  
7 Board, IOSCO, Commissioner Casey, important work  
8 to do in the IOSCO framework on ensuring that  
9 consistency not only occurs between Europe and the  
10 U.S. but also on a wider frame in the G-20. We're  
11 in this together. This is a global market and it  
12 needs a global response.

13           Timing issues have been overstated.  
14 I've seen these comments in the press and in the  
15 public arena. There is no timing issue. Will  
16 Europe be ahead of America, will America be  
17 lagging behind the European Union? This is not a  
18 race. This is a marathon and the marathons that I  
19 run with my lousy consideration we usually end up  
20 finishing the finishing line at the same time, we  
21 never have winners in my marathons. This is a  
22 European regulation and for the lawyers in the

1 room there is a difference between a regulation  
2 and a directive in Europe. If Europe had put  
3 forward a directive, we would have had to give the  
4 European member states 18 months to implement that  
5 in national legislation. This is a regulation and  
6 not a directive. If our Congress and our  
7 ministers agree with this text, it becomes the law  
8 of the land immediately. The regulation is the  
9 law directly evocable by any stakeholder before  
10 any national court in 27 countries in Europe or  
11 before the Court of Justice of the European Union  
12 in Luxembourg. Speed is not of the essence with a  
13 regulation. Getting it right is.

14 My third point is cooperation works.  
15 Believe me. The CFTC, Commissioner Gensler, his  
16 staff, the SEC, Commissioner Casey, I think the  
17 thin threads of discreet mutual cooperation that  
18 we started spinning a year ago are turning into a  
19 wide banner of international regulatory  
20 cooperation. It is no coincidence that there are  
21 so few differences between Dodd-Frank and between  
22 what Europe is coming up with, thus that wide

1 banner of international regulatory cooperation.  
2 The CFTC, the staff, the SEC, have been  
3 interoperating so much that I can tell you that  
4 the CFTC and the Commission offices by the staff  
5 is actually called the Concrete Financial  
6 Transatlantic Cooperation outfit, so you have a  
7 new terminology there, Chairman Gensler.

8 My fourth and final point is I've heard  
9 many regulators and stakeholders in the past 23  
10 years that I've been regulating banks, insurance  
11 companies and now market infrastructure. I've  
12 heard many regulators and stakeholders talk about  
13 regulatory cooperation and regulatory convergence.  
14 This is the first time in 23 years I've actually  
15 seen it happen and I'm proud to say that I think  
16 if you look at the texts, if you look at the  
17 approach that we've put on the table today, I  
18 think it will actually deliver the benefits that  
19 we're all looking for. Thank you.

20 COMMISSIONER SOMMERS: Thank you,  
21 Patrick, so much for your overview and your  
22 insights on that.

1 I'm now going to turn to our colleagues  
2 from the Japanese FSA and Mr. Sumi who is the  
3 Deputy Commissioner for International Affairs and  
4 Competitiveness at the Japanese FSA for an  
5 overview of their legislative proposals.

6 MR. SUMI: Thank you, Ms. Sommers,  
7 ladies and gentlemen. Somebody said that computer  
8 signals travel around the globe in split seconds  
9 but the Boeing 777 isn't that fast. I got off an  
10 airplane after a 13-hour flight 3 hours ago and  
11 I'm still operating on Japan Standard Time which  
12 is 3:00 a.m. in the morning. So please allow me  
13 not to quote Shakespeare, and I confess I didn't  
14 read Dodd- Frank on the plane either. I couldn't  
15 resist watching "Die Hard IV."

16 Let me start with the starting point,  
17 the Pittsburgh Summit. That was last September  
18 and after about 2 months' time of this Pittsburgh  
19 Summit declaration, we submitted a draft bill to  
20 the Parliament for the Financial Instrument and  
21 Exchange Act amendment of 2010 which was submitted  
22 to the Parliament sometime in March and passed in



1 May which was quite fast considering the Japanese  
2 political situation. This was not partisan and  
3 this was pretty much agreed upon in light of the  
4 importance to do our part and to contribute to  
5 global financial stability.

6           The Financial Instrument and Exchange  
7 Act by the way is in a sense omnibus legislation.  
8 It covers a broad range of financial activities,  
9 the amendment of which takes place almost every  
10 year so that we can't say that it's as shattering  
11 bookmaking as Dodd-Frank. It's a more or less  
12 annual housekeeping amendment, but nevertheless  
13 the content of the amendment was not routine.  
14 This 2010 amendment of the FIEA aimed at CCP  
15 clearings and mandatory clearing at domestic CCPs  
16 for derivatives transactions that are closely  
17 related to Japanese bankruptcy procedures. And  
18 related to this particular topic of today, we also  
19 strengthened the group-wide regulation and  
20 supervision of financial instruments or so-called  
21 SIFIs given the fact that the SIFIs is a new  
22 notion that encompasses not only the banks but

1 also the financial institutions regardless of  
2 legal form.

3           Also as you may be aware, in Japan which  
4 is pretty much similar elsewhere I believe, the  
5 law is stipulated in sort of broad-brush language  
6 and smaller more concrete details are usually  
7 provided by what we call cabinet office  
8 ordinances. Cabinet office ordinances sound  
9 somewhat strange, but in essence it's FSA's rule  
10 but before the FSA determines on that rule we  
11 usually welcome public comments and try to  
12 incorporate the public comments in the contents of  
13 these cabinet office ordinances. Although we have  
14 passed a law the content of which I'm going to  
15 explain, much work still needs to be done in the  
16 process of formulating these cabinet office  
17 ordinances and during the process we would like to  
18 listen to the industries as well as other  
19 regulators' comments in order to be compatible  
20 worldwide.

21           As to the first point of mandatory CCP  
22 clearing, we have a system to designate the

1 particular types of derivatives transactions. In  
2 essence we have a system of positive listing. I  
3 understand that U.S. regulations or E.U.  
4 regulations encompass the clearable or eligible,  
5 whatever the correct English language should be,  
6 but has a sort of exemption granted by the  
7 authorities. In a sense it's a negative listing.  
8 It takes up broad derivatives as a whole but  
9 allows some exemptions, a sort of negative list,  
10 but ours is a positive list. At this time of  
11 course in designation we will consider the market  
12 size and liquidity of that particular type of  
13 derivatives transaction and the regulatory  
14 approach is by other regulators. At this time the  
15 plain vanilla type in denominated interest rate  
16 swaps are sure to be included, but what else if  
17 any will be included or not will be determined  
18 like I said in light of market size and what the  
19 regulators do in the rest of the world.

20 Another particular feature is that we  
21 have one article which says certain types of OTC  
22 derivatives have to be cleared at domestic CCPs.

1 Usually although those derivatives transactions  
2 which are subject to mandatory CCP clearing can be  
3 cleared either by the domestic or foreign CCPs,  
4 but for those derivatives whose clearing criteria  
5 relates very closely to bankruptcy procedures  
6 under Japanese law, these are regarded as  
7 mandatory clearing at domestic CCPs. For example,  
8 at present the ITRUX Japan Index CDS is considered  
9 for inclusion. The rationale is that the  
10 CPSS-IOSCO consultative report on OTC derivatives  
11 on CCPs stipulates that, as I quoted here, "CCPs  
12 should consider establishing an internal  
13 determination committee that may determine the  
14 credit events where no decision was taken by  
15 market participants." This is one example of when  
16 we consider regulation we take CPSS-IOSCO very  
17 seriously, and in order to achieve the  
18 internationally compatible regulation we monitor  
19 very closely what's discussed, advised and  
20 recommended by CPSS- IOSCO.

21 The second point is strengthening of the  
22 infrastructure for central clearing. At this time

1 we do not have any minimum capital requirements  
2 for the CCPs, but as Mr. Pearson mentioned, we do  
3 need to avoid systemic risk or too-big-to-fail  
4 kind of phenomena for the CCPs so that we would  
5 like to ask the CCPs to have a solid financial  
6 base thereby asking the minimum capital  
7 requirements the exact amount of which will be  
8 determined -- the law doesn't stipulate the  
9 specific amount but, rather, the cabinet office  
10 ordinance -- or similar subset rules to the law  
11 determines the specific amount. Also in order to  
12 avoid the issue of conflict of interest, we would  
13 include the requirement for authorization for  
14 those who hold more than 20 percent of the voting  
15 rights of the CCPs.

16 Also the second point is that foreign  
17 CCPs will be allowed into the Japanese market. Of  
18 course foreign CCPs are welcome to establish a  
19 domestic Japanese subsidiary, but even without  
20 doing so the CCPs can provide central clearing  
21 services to Japanese financial institutions, A,  
22 through a linked system where a foreign CCP sets

1 up a linkage with a Japanese domestic CCP and  
2 provides service through that Japanese domestic  
3 CCP; or, B, direct revision of their service in  
4 which case we do request the CCPs to acquire a  
5 Japanese license, but the rationale for issuing  
6 the license is that as stipulated in the  
7 PowerPoint. We do ask the foreign CCP to maintain  
8 an adequate infrastructure to operate  
9 appropriately and reliably during Japanese market  
10 hours so that I think the only binding part of  
11 this requirement is the underlined portion during  
12 Japanese market hours. Also we do ask that the  
13 foreign CCP is subject to proper supervision by  
14 its home country regulator.

15 Page 5 pertains to the reporting and  
16 storing of trade information data. We've made it  
17 mandatory for financial institutions to store and  
18 report trade information data for OTC derivatives  
19 transactions. However, if financial institutions  
20 use trade repositories, then the responsibility  
21 will be transferred to the trade repositories and  
22 the financial institutions will be relieved of

1 that responsibility. If financial institutions  
2 use CCPs, again the reporting and storing  
3 responsibilities will be transferred to the CCPs  
4 and the financial institutions themselves will be  
5 relieved of such responsibility.

6           These are the issues stipulated in the  
7 law which passed May 18 of this year and the  
8 implementation schedule is stipulated on page 6.  
9 The strengthening of the infrastructure of CCPs  
10 including the minimum capital requirement and  
11 allowing entry of foreign CCPs will take effect  
12 within 1 year of promulgation of the law on May 18  
13 of this year meaning May 18 of next year, 2011.  
14 After that, the mandatory clearing and storing and  
15 reporting requirement will take effect within 2  
16 years and 6 months, meaning November 18, 2012,  
17 which of course takes into account the Pittsburgh  
18 Summit's mandate of starting mandatory clearing by  
19 the end of 2012. This is how we have set up our  
20 law in the 2010 amendment of the Financial  
21 Instrument and Exchange Act. Again, although the  
22 law is enacted, we still have work to do in order

1 to be implemented meaning that we do need to  
2 stipulate the cabinet office ordinances. But  
3 again, as we do that, we will be putting it out  
4 for public comment and in doing so we will try to  
5 incorporate the other regulators' actions or  
6 CPSS-IOSCO's recommendations to make it compatible  
7 with the other major jurisdictions and industries'  
8 comments will be also welcome at the public  
9 comment stage. Thank you very much.

10 COMMISSIONER SOMMERS: Thank you so  
11 much, Mr. Sumi, for being here and for that  
12 overview. I'd now like to open it up to our  
13 committee members or my colleagues if you have any  
14 questions for either Mr. Pearson or Mr. Sumi on  
15 either the European Commission or Japanese  
16 legislative proposals. Jiro?

17 MR. OKOCHI: Jiro Okochi from Reval.  
18 Thank you for enlightening us more on the  
19 international legislation coming down.

20 If we understand that the product may be  
21 the same at the end of the road, I still think it  
22 boils down to the very important details which in



1 derivatives details are everything. One clear  
2 difference may be how those on both sides of the  
3 Atlantic and across the Pacific define commercial  
4 risk. The hedging of commercial risk is used to  
5 net down positions by nonfinancial counterparties  
6 or for large positions, I think that's a big open  
7 question on how that would that would be objective  
8 viewed. Are there any comments on the approach to  
9 looking at how a counterparty may be hedging  
10 commercial risk?

11 MR. SUMI: The way the law is adopted at  
12 this moment, as long as the financial institution  
13 is a party to that derivatives transaction, then  
14 even though the other party is nonfinancial, this  
15 contract at this stage we consider it included in  
16 this mandatory CCP clearing. However, if you were  
17 to ask the nonfinancial institutions to be fully  
18 mandated to use the CCPs, then these corporations  
19 may be subject to too heavy a burden of  
20 maintaining the CCPs. Therefore, depending on  
21 other jurisdictions' actions and other IOSCO  
22 arguments, we may consider exempting these

1 nonfinancial corporations doing the transactions  
2 for hedging purposes from this mandatory  
3 requirement. So at this juncture we have the  
4 means to exempt them and we have not decided  
5 whether we are going to or we are not going to.

6 MR. PEARSON: It's a very good question  
7 and this is where I think "Die Hard IV" and  
8 Shakespeare meet. I'll tell you why. You know  
9 that in "Die Hard IV" Bruce Willis always starts  
10 off with a clean undershirt and it's always white.  
11 Have you noticed that halfway through the film as  
12 if by miracle it always turns green and black and  
13 dirty? But in the end all actually works out  
14 well, there's always a happy end, it's a Hollywood  
15 film, and that brings to me to the question of how  
16 is it possible that Bruce Willis's shirt that's so  
17 clean at the beginning gets dirty in the end or  
18 halfway through and in the end it all works out  
19 well? You watched the film yesterday and I've  
20 seen all of them many times. I love Bruce Willis  
21 to bits.

22 But this brings me to Shakespeare

1 because Shakespeare of course wrote "All's Well  
2 That Ends Well." We studied this at school, at  
3 least I did and you should have. You know about  
4 "All's Well That Ends Well," it's all about the  
5 bed trick. Do you know the bed trick? I'll  
6 enlighten you a bit. In "All's Well That Ends  
7 Well" halfway through the story, the king allows  
8 Helena to marry the man of her choice and he  
9 chooses Bertram who's an old heart throb of hers.  
10 Bertram refuses and he says, "I will only marry  
11 you, Helena, if you meet two conditions. You get  
12 a wedding ring on my finger and you show me,"  
13 Bertram, "a child that I have fathered." So  
14 Helena embarks on her plot to pave the way to true  
15 happiness by using what's become to be known as  
16 the bed trick which is why you should really read  
17 this. This is really interesting.

18           Why am I making this point apart from  
19 bringing some culture to this side of the  
20 Atlantic? It's because we have a bed trick. We  
21 have a bed trick as well in Europe, you have a bed  
22 trick over here as well, because what is the point

1 in calculating the position, the exposure of the  
2 corporates? We need to strip out all of those  
3 positions that are directly linked to the  
4 underlying corporate activity. It makes absolute  
5 sense. We ran our impact assessments and it's the  
6 only sensible way forward. The problem is how to  
7 determine when a position is directly linked to a  
8 corporate activity of the firm in question and  
9 there's a huge potential obviously for arbitrage  
10 because any company will say I've taken this swaps  
11 position and I need it to cover my interest rate  
12 exposure or my currency exposure so it's  
13 underlying my international business.

14 Not true. The bed trick is that we had  
15 two options. The first was let's use the  
16 international accounting standards so that we  
17 looked at the European accounting standards  
18 hedging. No way, Jose. This was all over the  
19 place and it really didn't help us. So we looked  
20 to U.S. GAAP and what have you and we were even  
21 more shocked. That really didn't help us one bit.  
22 So we couldn't have a hedging requirement. You

1 can't refer to hedging in the accounting sense to  
2 determine if the position is directly linked to  
3 the corporate activity. So we had a cunning plan  
4 and that's our bed trick, and the bed trick is we  
5 will have to define this in further regulatory  
6 guidance?

7           Why is this a good bed trick? Because  
8 it makes no sense for us to come up with a  
9 different sense of regulatory guidance than the  
10 SEC and the CFTC on this side of the Atlantic,  
11 because believe me, people, the corporates I'm  
12 speaking to, they're the same corporates you know  
13 over here in the United States of America,  
14 Caterpillar, John Deere, Rolls Royce, Lufthansa,  
15 they're all international companies and if the SEC  
16 and if the CFTC come up with a different  
17 definition from us in Europe, it's very, very  
18 simple to see where this business will shift to  
19 and how the loopholes in the regulation will come  
20 around.

21           There you have it. That's how Bruce  
22 Willis in "Die Hard IV" and Shakespeare come

1 together, all's well that ends well.

2 CHAIRMAN GENSLER: I was going to say I  
3 don't know from Helena or Bertram or anything like  
4 that, but we working very closely with the  
5 Europeans and I'll try to learn my Shakespeare,  
6 Patrick.

7 COMMISSIONER DUNN: On my transatlantic  
8 flights, being of Irish descent, I tend to read  
9 Joyce. I have a little darker outcome. Yesterday  
10 I wasn't watching "Die Hard," I had one eye on the  
11 Ryder Cup and that wasn't such a good outcome for  
12 us as well. I commend the E.C. on their win.

13 Mr. Sumi, in your presentation there's  
14 an asterisk there in which you say that the  
15 licensed foreign CCP will be subject to inspection  
16 and business improvement by the Japanese FSA as  
17 well. This has been a great rub for us as we work  
18 internationally and that is adhering to the  
19 national sovereignty to those home regulators. I  
20 wonder how do you go about that inspection in  
21 business improvement orders. Is that directly  
22 with the CCP or are you looking at the home

1 regulator to make those inputs for you? Then I  
2 would ask the same thing of Mr. Pearson.

3 MR. SUMI: If I may answer your question  
4 first, we have a similar situation where say a  
5 bank sets up a branch in Tokyo and that branch is  
6 subject to our inspection and if there is a need  
7 we may issue a business improvement order as well.  
8 Of course in doing so, this is a new one so I am  
9 talking about the existing example of banks and  
10 say Citibank establishes a branch in Tokyo and  
11 then it's subject to both U.S. and Japanese  
12 regulations, of course when dealing with these  
13 institutions we have contact with the home country  
14 regulator and also for many of the things we can  
15 finish business just talking with the home country  
16 regulator and for some other things this is in a  
17 sense as long as we license somebody, we do need  
18 to retain the in a sense right to do on-site  
19 inspections and to order something. But in actual  
20 working, of course we do consult closely with the  
21 home country regulator.

22 COMMISSIONER DUNN: In your case then

1 that foreign CCP is required to allow you to come  
2 in and do the inspection and give that information  
3 directly to the FSA?

4 MR. SUMI: We do want to have the  
5 correct information reported to us so that if we  
6 think that information is necessary, we are going  
7 to ask that foreign CCP to provide us with that  
8 information.

9 COMMISSIONER DUNN: Patrick?

10 MR. PEARSON: I can be quite short and  
11 the reason is there is no Shakespeare quote  
12 referring to Japanese inspections. There are two  
13 questions here, Commissioner Dunn.

14 COMMISSIONER DUNN: Bubble, bubble, toil  
15 and trouble wouldn't work?

16 MR. PEARSON: There's probably in James  
17 Joyce. Is there equivalence and what is the  
18 consequence? That's how we would look at this in  
19 Europe. Is there equivalence? What we will do is  
20 have a comparison. The comparison will be carried  
21 out jointly, in the U.S. case between the European  
22 regulators and the U.S. regulators. We will



1     consult, we would compare regulation and  
2     regulatory practices and there will be a ruling  
3     from the European Commission that there is  
4     equivalence or not, but in our case we work on the  
5     presumption there's equivalence.

6             The question is then what is the  
7     consequence? The consequence from our perspective  
8     is no inspections, but the consequence is what we  
9     call mutual recognition so that we recognize the  
10    quality of the way in which regulation is carried  
11    out in a third country, in this case in the United  
12    States of America. The only thing we would  
13    require is a bilateral MOU of understanding  
14    between the European regulators and the Japanese  
15    regulators of the U.S. Regulators on mutual  
16    exchange of information but not the inspection  
17    part.

18            COMMISSIONER SOMMERS: Commissioner  
19    O'Malia?

20            COMMISSIONER O'MALIA: Thank you. Mr.  
21    Pearson, in your statement you'd laid out the  
22    issue of segregation and providing for both an

1 omnibus account and an individual account. I want  
2 to get a sense from you regarding would you leave  
3 that up to the FCM, the clearinghouse, to set  
4 those rules and get a little bit of input from our  
5 panel as to what they think how that might be  
6 implemented and if that's feasible? And Mr. Sumi,  
7 if you have any thoughts on this, I'd appreciate  
8 those as well.

9 MR. PEARSON: You're absolutely correct,  
10 Commissioner. The way we've put this out is very  
11 simple. As to segregation, we would require a  
12 clearinghouse or CCP to have the option of omnibus  
13 segregation. We're not requiring them to apply  
14 one or the other. It's just the option so there  
15 is a choice for the clients. And in implementing  
16 this option we would require the clearinghouse to  
17 give full transparency as to the extra risks you  
18 would run or not run when as a client you opt for  
19 one of the other permutations, and obviously the  
20 costs because the client will in almost all cases  
21 find it cheaper to go for an omnibus rather than  
22 segregation. But the choice is up to the client.

1 We can't regulate that choice into being. We can  
2 only regulate the need for there to be an option,  
3 so that's how we would approach it.

4 MR. SUMI: If I may, we will probably  
5 not the specific rules regarding that, but since  
6 CPSS-IOSCO has certain rules for this segregation  
7 and portability, we do ask the CCPs to establish  
8 their own business rules in which if I find  
9 something incompatible with CPSS-IOSCO we would  
10 ask them to correct that and to make it comply  
11 with CPSS- IOSCO. So is probably the way we'll  
12 work. Does that answer your question?

13 COMMISSIONER O'MALIA: It does. Thank  
14 you. I'd be interested in any of the panelists or  
15 committee members as to their thoughts they have  
16 on the European proposal.

17 COMMISSIONER SOMMERS: Roger?

18 MR. LIDDELL: Just a comment related to  
19 it which is that interest rate swap client --  
20 model allows for either and we see no demand at  
21 all for the omnibus and it is for the issue of  
22 portability, it's very, very hard to guarantee

1 portability with omnibus, in fact it's impossible  
2 unless you port the entire defaulting member's  
3 portfolio in one block to a single -- so we feel  
4 strongly as an organization that individual  
5 segregation for OTC derivatives is the way to go.

6 COMMISSIONER SOMMERS: Richard?

7 MR. BERLIAND: I think there is an  
8 important distinction to be made between the  
9 client demand and over-the-counter derivatives  
10 which I think Roger correctly represents and for  
11 listed derivatives. I think the pricing  
12 sensitivity on clearing is very different in the  
13 listed space and particularly for some market  
14 participants whether they're in the high frequency  
15 or at least they were heavy users of the market,  
16 the costs of the transaction is an extremely  
17 important part of their ability to participate in  
18 the market. I think, A, I strongly endorse the  
19 European approach to being a matter of choice, and  
20 secondly, I would say that I think it is important  
21 that we maintain a recognition that there is a  
22 difference in client preference in listed and

1 over-the-counter derivatives.

2 CHAIRMAN GENSLER: If I could ask a  
3 question for Roger, Jeff and Tom and I think maybe  
4 there are others here representing clearinghouses.  
5 When you think about the clearing rules that may  
6 emerge in Europe which you've already seen in  
7 Dodd-Frank but we're embarking on rule- writing,  
8 what is your perspective? You manage  
9 multinational platforms all of which at some point  
10 will be regulated here in the U.S. by the SEC and  
11 CFTC, Roger is here so that it will be just the  
12 CFTC, but nonetheless you'll be regulated here in  
13 the U.S. and you may well be regulated in Europe  
14 and Japan. It would be helpful to gain your  
15 perspectives on clearinghouse rules.

16 MR. SPRECHER: I think the three  
17 entities that you mentioned, while we do compete,  
18 we compete with very high standards and have  
19 generally adopted the IOSCO standards. Certainly  
20 in the case of ICE we welcome having some  
21 harmonized high standards for work management  
22 because we don't want to compete on that level and

1 I think as I've mentioned the companies that are  
2 present today have already internally adopted  
3 those and we would welcome regulators harmonizing  
4 that.

5 Secondly, we have long seen between the  
6 U.S. and Europe, the FSA and the CFTC, cooperation  
7 in the case of our business so that there is very  
8 little difference in the current offerings that we  
9 have for both OTC and listed futures between the  
10 U.S. and Europe in terms of membership  
11 requirements and risk-management requirements and  
12 such. The only differences that exist are there  
13 because of the different bankruptcy regimes, but  
14 we see you helping to harmonize those even though  
15 there will continue to be different bankruptcy  
16 regimes. I think we view the efforts between the  
17 agencies that are here as being quite positive.

18 CHAIRMAN GENSLER: As you continue, do  
19 you envision having within an asset class one  
20 clearinghouse or one in Europe, one in here, one  
21 in France or one in London? That's a tough  
22 question.

1           MR. SPRECHER: I think it would be nice  
2 if we could live in a world where a CCP could be  
3 located anywhere and recognized globally. It's  
4 going to take a while to get there. In the case  
5 of credit default swaps which is a very  
6 complicated product and to a certain degree has a  
7 prerogative view given what we've come through in  
8 2007, we thought it was best to have independent  
9 clearinghouses that were locally regulated.

10           In the case of listed products, it seems  
11 rational to have a single-domicile clearinghouse  
12 that has a global standard. That seems more  
13 acceptable. For example, our U.K. futures  
14 clearinghouse has a DCO status here in the U.S.  
15 and with all the work that's been done between the  
16 FSA and the CFTC with respect to at least ICE's  
17 listed products, it does feel like that can work  
18 well. I think we're at the first inning of the  
19 OTC market. I suspect that we'll potentially  
20 evolve toward the listed model but it'll take a  
21 while to get there.

22           MR. LIDDELL: I think the only

1 difference is the requirement under Dodd-Frank for  
2 the safety regime for U.S. Clients which on the  
3 one hand is a fairly difference, on the other  
4 hand, we'd already decided for our own reasons  
5 that that was the model that we wanted to adopt in  
6 any case so it actually isn't an issue for us.

7 CHAIRMAN GENSLER: Did you say the  
8 segregation regime or FCM?

9 MR. LIDDELL: The FCM. And we  
10 absolutely see the biggest benefit being having a  
11 single clearinghouse globally rather than  
12 different ones regionally. I think the credit  
13 derivatives product is an exception to that and I  
14 think that was rightly identified by the JFSA  
15 because of local bankruptcy issues and also  
16 sovereignty issues and sovereign credit default  
17 swaps and things like that. I think having  
18 regional clearinghouses for credit products has  
19 some logic to it, but for the rest I think it  
20 would be a very, very significant backward step if  
21 we went down that path.

22 The adoption of our model for the U.S.



1 regime could become a little bit of a precedent.  
2 For example, there is not the equivalent in the  
3 Japanese market that I'm aware of, but I think if  
4 we are going to be successful at working with  
5 colleagues in Japan to achieve our ambitions, it's  
6 quite likely that we would have some regime that  
7 would result in domestic end-user clients having  
8 their collateral held onshore under local  
9 agreements subject to local bankruptcy codes so  
10 that I think adopting a global model for regional  
11 differences is the right way to go.

12 MR. CALLAHAN: This is Tom Callahan from  
13 NYSE Euronext. We're in a bit of a unique  
14 position because of course we are as we speak  
15 today simultaneously constructing three new  
16 clearinghouses in three different regulatory  
17 jurisdictions around the world, one here in the  
18 U.S., New York Portfolio Clearing, we're also  
19 building a new clearinghouse in London and  
20 simultaneously a clearinghouse in Paris so that  
21 for us harmonization of the rules and protocols  
22 between the regulatory jurisdiction not only makes

1 our lives easier in terms of how we construct  
2 these new clearinghouses, but we believe a  
3 competitive advantage of our global exchange group  
4 will be ultimately to tie these together so that  
5 bankruptcy issues that Roger raises are certainly  
6 real and our initial plans are to have products  
7 siloed within an individual clearinghouse but to  
8 the degree that we're able to evolve through these  
9 bankruptcy issues and draw them together, for us  
10 it's a competitive advantage.

11 COMMISSIONER SOMMERS: Thank you.

12 COMMISSIONER CHILTON: I have one real  
13 quick one. I'm sorry for slowing us down.

14 I'm exceedingly encouraged by the  
15 parallel policies that you've talked about. Mr.  
16 Pearson, I have one quick one for you, and maybe  
17 there is a distinction within a difference, but  
18 thought as you were talking about clearing that  
19 there might be a little bit more texture there but  
20 maybe I'm wrong. Were you suggesting that we  
21 should perhaps have higher standards as we  
22 implement our regulations that would go even

1 further than Dodd-Frank? Like others, we can put  
2 more meat on the bones of the laws, we have some  
3 discretion and the law restricts us in some  
4 regards, but were you suggesting that maybe we  
5 would want to go a little bit further?

6 MR. PEARSON: No, Commissioner Chilton.  
7 I think the point as to the meat on the bones is  
8 make sure the threads are there in the fabric and  
9 Dodd-Frank gives the SEC and the CFTC the locus  
10 and the jurisdiction to put that meat on the bones  
11 so that we're interested to see how that pans out.

12 COMMISSIONER CHILTON: Thank you.

13 COMMISSIONER SOMMERS: Now we're going  
14 to brief updates on international organizations  
15 that are taking certain issues in their agenda  
16 items coordinating global regulatory issues, and  
17 I'm going to turn first to Commissioner Casey for  
18 an update on last week's FSB meeting in Paris.

19 COMMISSIONER CASEY: Thank you very  
20 much, Commissioner Sommers and, again, thank you  
21 for allowing me to join you today.

22 As has been noted by yourself and

1 colleagues here in the Commission at the CFTC and  
2 our colleagues from the European Commission and  
3 Japan, consistency with respect to international  
4 standards in this area is going to be critical. I  
5 would tell you that a tremendous amount of effort  
6 is underway, not least of which has already been  
7 articulated here. One of the other key places  
8 where this is being coordinated at the FSB level.  
9 As you all are very well aware, the FSB has been  
10 asked to play a central role in coordinating the  
11 implementation of international standards across  
12 jurisdictions and so they play a key role in this  
13 area as well.

14           The focus of the Paris meeting was to  
15 talk about and to take stock in a lot of the  
16 progress that's being made on the reform agenda,  
17 in particular with respect to the G-20 commitment  
18 to central clearing, trading and trade reporting.  
19 At the initiative of the FSB back in April 2010,  
20 they established a high-level working group which  
21 was intended to help facilitate this consistency.  
22 Much of the meeting in Paris was focused on

1 hearing and reviewing some of the draft  
2 recommendations that the working group has put  
3 forward and we would anticipate that that paper  
4 would be approved and considered by the leaders in  
5 November. I think that this paper in particular  
6 is going to be really quite helpful in providing a  
7 framework for consistency across jurisdictions.  
8 Again, I've been really pleased at the engagement  
9 that you have. I know Patrick Pearson is one of  
10 the primary authors of the report, we're engaged  
11 with our CFTC colleagues and other jurisdictions  
12 such as Japan as well. I think that this will be  
13 a great contribution to helping to facilitate some  
14 of the issues that are being discussed here today.

15 I would also note some of the other  
16 items that the FSB discussed on the reform agenda  
17 were obviously welcoming the Basel work, talking  
18 about seeking consistency in helping to reduce  
19 regulatory reliance on credit rating agencies to  
20 address some of the cliff effects that we saw with  
21 respect to ratings being embedded in statutes and  
22 regulatory rules. That was the central focus of

1 the FSB meeting in Paris, and SIFIs as well also  
2 dealing with too big to fail and trying to come up  
3 with principles for addressing systemically  
4 important financial institutions again in an  
5 internationally consistent manner. I would  
6 anticipate again that the work that we'll see  
7 coming out of the FSB working group will be an  
8 important contribution to ensuring consistency in  
9 this area.

10 COMMISSIONER SOMMERS: Thank you, Kathy.  
11 I'm now going to turn to Jackie Mesa who's our  
12 Director of our Office of International Affairs  
13 for an update on the IOSCO agenda.

14 MS. MESA: Thank you, Commissioner  
15 Sommers, and thank you for inviting me to provide  
16 an update on IOSCO matters to this group.

17 I have to say when Commissioner Sommers  
18 asked me to provide an update on IOSCO initiatives  
19 I thought I might just put this group to sleep  
20 right before a break. But I have to say, and  
21 maybe it's my roots coming from the Midwest part  
22 of America, I never thought to infuse Shakespeare

1 as to keep it a more interesting and lively  
2 presentation. That said, you're going to get a  
3 plan vanilla presentation from me today.

4 As you can imagine, a lot of the  
5 initiatives happening internationally as  
6 Commissioner Casey just presented are around OTC  
7 regulation and ensuring that we have consistent  
8 approaches going forward. Just last week in India  
9 the Technical Committee of IOSCO approved a task  
10 force on OTC derivatives. That task force is  
11 chaired by the U.S., the CFTC and the SEC, the  
12 U.K. and India. The three chairs put together a  
13 mandate and a lot of that mandate is to take  
14 forward what is anticipated from the FSB report  
15 that you just heard about from Commissioner  
16 Sommers. The group is going to take forward  
17 additional analysis of exchange on electronic  
18 platform for OTC derivatives. It's going to  
19 separately work on data reporting and aggregation  
20 requirements so that there is a consistent  
21 approach on that front. And then the task force  
22 is going to endeavor to develop consistent

1 international standards relating to OTC  
2 derivatives regulation and clearing, trading,  
3 trade data collection reporting and oversight of  
4 certain market participants. It's quite detailed  
5 and as Commissioner Casey knows, we had a long  
6 discussion in Chennai, India last week about what  
7 do standards mean as opposed to principles and I  
8 think I can tell you that the idea is that we go  
9 even beyond principles in this area because it's  
10 so important to harmonize and that we come up with  
11 a set of standards here. Finally, this task force  
12 is going to serve as a central point where members  
13 can consult with each other in going through their  
14 own rule-writing and the U.S. Of course will  
15 heavily use this group for its own consultation  
16 during the rule-writing process.

17 That sounds like a lot of work for an  
18 international group and so you guys are probably  
19 thinking 5 years from now we're going to have a  
20 report from IOSCO. We're trying to reshape  
21 ourselves into something that moves a little  
22 faster so that we're going to do these reports



1 separately and in a phased approach, but it is a  
2 very tight timeframe, so we're hoping to turn  
3 these out before any country is finalized in their  
4 rules.

5           As to other IOSCO projects that touch on  
6 the OTC world, there is an ongoing project on  
7 suitability standards in connection with complex  
8 financial products. This of course includes  
9 swaps. The project grew out of European and Asian  
10 concerns on the Lehman minibonds so that it's a  
11 project that we support here in the United States  
12 and is an interesting one to go forward  
13 internationally. There is also a project on  
14 capital requirements, and that is limited at this  
15 point to comparability of capital standards  
16 throughout the world and not setting up a standard  
17 of capital requirements at this point, but a  
18 comparability approach. Also of course during the  
19 financial crisis what came to light is that  
20 regulators and securities regulators with the  
21 prudential regulators weren't all feeding together  
22 in a process to identify systemic risk so that

1 IOSCO in June 2010 developed a new principle and  
2 approved a new principle which regulators must  
3 implement on systemic risk. It states that  
4 securities and futures regulators must contribute  
5 to a process to monitor, mitigate and manage  
6 systemic risk appropriate to its mandate. IOSCO  
7 is now working on what does this mean. It seems  
8 very lofty, but what is the role of securities and  
9 futures regulators in identifying risk in the  
10 system and how will it contribute to a process to  
11 identify risk?

12           Some non-OTC projects I would say but  
13 will be of interest to you and IOSCO is just last  
14 week another approved mandate on high-frequency  
15 trading. The Technical Committee approved this  
16 project to address concerns presented by such  
17 trading and to consider the regulatory responses.  
18 What this group will look at is the impact of  
19 high-frequency trading technologies and strategies  
20 on market operators, participants, investors and  
21 regulators, and the possible impact of  
22 high-frequency trading on the orderly functioning

1 of markets including unique aspects that might  
2 facilitate manipulative practices. It's not per  
3 se manipulative of course to conduct  
4 high-frequency trading, but whether there are  
5 things that high-frequency traders might be doing  
6 that others are taking advantage of. Finally, of  
7 course, IOSCO will not forget the benefits of  
8 high-frequency trading, so have no fear that that  
9 will be a part of the report and analysis of what  
10 high-frequency trading brings to the market.

11 One topic that IOSCO has been working on  
12 that has been a subject of debate in this group in  
13 the past has been direct electronic access. Some  
14 of you will remember that at the last meeting  
15 there was quite a lively conversation about this.  
16 IOSCO did finalize its report in the meantime so  
17 that I wanted to highlight some principles that  
18 might be of interest to you. The principles for  
19 direct electronic access say that regulators  
20 should have appropriate policies and procedures in  
21 place to ensure that direct electronic access  
22 trades placed directly on to the exchanges by a

1 customer do not pose undo risk to the market and  
2 to the relevant intermediary. I think the two  
3 most critical principles that I'll point out  
4 including Principle 6 on markets that says that a  
5 market should not even permit direct electronic  
6 access unless there is in place an effective  
7 system and controls to enable risk management for  
8 fair and orderly trading. Then Principle 7 for  
9 intermediaries, that intermediaries, and this  
10 includes as appropriate clearing firms, should use  
11 both regulatory and financial controls including  
12 automated pretrade controls which can limit or  
13 prevent a direct electronic access customer from  
14 placing an order that exceeds existing positions  
15 or credit limits on such a direct electronic  
16 access customer. As you know, this goes a little  
17 bit beyond where the CFTC is at the present  
18 moment, but this is giving direction to  
19 regulations who haven't taken steps in this space  
20 before.

21 A task force that the CFTC has  
22 co-chaired since 2008 and that we are actively

1 doing work on is the Commodity Futures Markets  
2 Task Force. This started after the G-20  
3 expressing concern over volatility in agricultural  
4 and oil markets and asked IOSCO to do work in this  
5 area. We issued a report in March 2009, but the  
6 G-20 came back and said please do more work.  
7 We're still concerned, but at this time we're  
8 particularly concerned about oil market  
9 volatility. And in the Pittsburgh Communiqué they  
10 gave us very specific instructions on going  
11 forward and what IOSCO needed to do. One was that  
12 all regulators should collect data to identify and  
13 monitor large concentrations on their markets,  
14 that they should collect related OTC oil market  
15 data, that the regulators should be taking active  
16 steps to combat market manipulation and that  
17 regulators around the world needed to publish more  
18 information to market participants.

19 In these four areas this group has been  
20 taking forward this work in the past year. I  
21 think one of the more interesting areas was on the  
22 OTC market where regulators around the world did

1 not have authority to on their own necessarily  
2 collect data. We have participants in this group  
3 from Saudi Arabia, Dubai, major Europeans, Canada  
4 and Brazil, et cetera. We worked with ISDA in  
5 this area to do a voluntary survey of the OTC  
6 market in oil. We had 41 participants and the  
7 participants included the G-14 major dealers, but  
8 also producers and buy side firms participated.  
9 It's a snapshot of results and it is voluntary and  
10 unchecked by the regulators. So with all those  
11 conditions, I wanted to preview some of the  
12 results that will later be in a report to the G-20  
13 for its November meeting.

14 I think it's fairly interesting that 19  
15 percent of the trades, and this is by deal count  
16 and not by volume, were conducted with a G-14  
17 counterparty. I think what this tells us is that  
18 in the oil space you're seeing something very  
19 different that you're not seeing in interest rates  
20 and other financial derivatives, and that is that  
21 much of the trading is being done by the non-big  
22 dealers and they're being done by non-G-14 to

1 non-G-14, a huge amount of trading. About half  
2 the trades, 55 percent, are done on exchange of  
3 all the participants. Nineteen percent of those  
4 OTC trades are cleared, but 27 percent remain  
5 uncleared which I think is quite large because  
6 there is available clearing in this space as  
7 opposed to a lot of the other products so that you  
8 can see that a lot of it remains uncollateralized  
9 and noncleared. There is more on-exchange trading  
10 of the G-14 members, there is more clearing of the  
11 G-14 members than there is of the non-G-14, so  
12 that I think those are interesting.

13           Beyond the survey that we will provide  
14 to the G-20 to provide that transparency, the CFTC  
15 held a training program to provide information on  
16 how we put out our commitment of trader report to  
17 foreign regulators. There is very positive  
18 reception of that training and we think that  
19 several regulators will follow with a similar  
20 commitment to trader report on certain markets.

21           Additionally, the task force is working  
22 with cash market regulators, with price reporting

1 agencies and specifically Platts and Argus who do  
2 put out prices that the exchanges use, so we're  
3 working on how these price reporting agencies  
4 affect the price of oil and whether there is  
5 proper oversight of them.

6           Finally, I want to note future work of  
7 this task force. There is a lot of press I think  
8 in Europe and Patrick and Peter can speak to this,  
9 but around the world about ag markets. It shifts  
10 back and forth whether it's oil or ag or both, but  
11 there is a great fear in the prices of ag markets  
12 being volatile and how that affects global  
13 economic recovery. I can anticipate at the  
14 upcoming G-20 in November that this will be on the  
15 agenda for world leaders, and not only will they  
16 focus on what's happening in production and  
17 capacity, et cetera, but I am sure they will also  
18 focus once again on financial markets in this  
19 space. So there is more work to come and we look  
20 to industry to help us think through some of these  
21 problems.

22           COMMISSIONER SOMMERS: Thank you,



1 Jackie. I'm going to ask now if there are any  
2 final questions or discussion on this part of our  
3 agenda, and I might ask Mike Dawley who is on the  
4 phone if he has any questions and is able to break  
5 in.

6 MR. DAWLEY: I'm good, Jill. Thanks.

7 CHAIRMAN GENSLER: Peter, no  
8 Shakespeare, one of the things that we have in  
9 Dodd-Frank is business conduct standards. Those  
10 business conduct standards go both to lowering  
11 risk of the swap dealers to the financial system,  
12 a lot of back office, and there are also business  
13 conduct standards on what I might call sales  
14 practices, how you interface with customers.  
15 Could you give us a sense? I think some of that  
16 you may have taken up and some might be in later  
17 MIFID reform, but that would be helpful.

18 MR. KERSTENS: We are indeed looking at  
19 this. This is part of the MIFID directive which  
20 is up for review at the beginning of next year,  
21 and also a separate piece of legislation,  
22 something that is called the marketer views

1 directive. Of course we have plenty of  
2 directives. The advantage is that each  
3 individually are much more readable than  
4 Dodd-Frank together.

5 CHAIRMAN GENSLER: Is the answer is that  
6 on sales practices you're taking that up in these  
7 other directives and on the back office some of  
8 those risk-mitigation techniques might be in this  
9 package here? Thanks.

10 COMMISSIONER DUNN: For a number of  
11 years I've pushed our international group very  
12 hard to get involved at both the IOSCO level with  
13 full membership and to have input into what goes  
14 on with the FSB after the G-20 had indicated that  
15 that was the mechanism that they were going to  
16 use. I want to publicly thank Commissioner Casey  
17 for her work on that area who did an outstanding  
18 job at representing us here. I'm wondering what  
19 opportunities does the public have for input as  
20 these things are being hammered out? It would  
21 appear to me that this group here has a great deal  
22 at stake, and what type of input and when can they

1 get their input into this process?

2 MS. MESA: I'll speak to IOSCO and maybe  
3 let Commissioner Casey talk about the FSB. IOSCO  
4 has traditionally put out reports always in a  
5 consultative form first so that we can receive  
6 public comment from industry. But about a year  
7 ago, or it's now been 2 years ago, we heard from  
8 industry that that wasn't sufficient, that  
9 sometimes these reports went by and they wanted to  
10 have early input into IOSCO's work and IOSCO then  
11 set up a group that would meet I think twice a  
12 year to have outreach to IOSCO into even what they  
13 look at and what they should prioritize as work,  
14 but also to provide face-to-face feedback to the  
15 people leading the working groups. That has been  
16 going on for some time, but of course it can't be  
17 the world because it's a face-to-face meeting and  
18 it's supposed to be representative bodies of  
19 certain classes of industry. It's worked but it's  
20 not perfect. Individual regulators like myself  
21 sometimes will shove these reports out and ask for  
22 feedback and among everyone here who is so busy

1 sometimes we get that and sometimes we don't  
2 depending on the topic.

3 COMMISSIONER CASEY: I think again it's  
4 a really important point that you make and I know  
5 that with the evolution of the work that's been  
6 undertaken by the FSB, there's been a tremendous  
7 amount of focus on the question of transparency.  
8 As Jackie has noted, within IOSCO and other  
9 standard-setting bodies like IOSCO or the Basel  
10 committee or IAIS, you have these processes which  
11 are intended to help facilitate putting out  
12 consultative reports, getting input from key  
13 stakeholders, having outreach efforts, all  
14 intended again to help inform the standard-setting  
15 bodies as they take these judgments.

16 I would say in the context of the  
17 ongoing work that the FSB is undertaking and the  
18 working group on OTC derivatives in particular,  
19 again the working group itself is comprised of the  
20 standard-setting bodies, CPSS and IOSCO, and then  
21 also with the leadership of the E.C. as well. So  
22 to the degree that you have standard-setting

1 bodies also informing the higher-level principles  
2 that are being articulated by the FSB and you have  
3 a mechanism whereby the work that's taken forward,  
4 the standard-setting work, is ultimately  
5 undertaken by the standard-setting bodies, you  
6 ensure that you have that kind of input at the  
7 technical level. I think that going forward  
8 though it's going to be an important balance to  
9 keep in mind with respect to the very critical and  
10 important role that the FSB plays in terms of  
11 coordinating the efforts of standard- setting  
12 bodies in helping to direct and foster  
13 facilitating reform efforts in a consistent  
14 manner, but I think it's also going to be  
15 important therefore that the standard- setting  
16 bodies themselves because those processes ensure  
17 that you get that consultation and that  
18 transparency, that they also continue to play that  
19 frontline role. But what I anticipate from  
20 hearing from a lot in the industry, and I know  
21 that letters have been sent to the FSB and  
22 otherwise, is to try to ensure that there is some

1 greater transparency and input into this processes  
2 so that I think in a forward- looking way it's  
3 going to be really important that those issues  
4 continue to be addressed appropriately.

5 COMMISSIONER DUNN: Are there any  
6 suggestions or comments by the GMAC on this  
7 particular issue?

8 COMMISSIONER SOMMERS: If there are no  
9 further questions, we're going to take about a  
10 15-minute break, but I want to thank Commissioner  
11 Casey for being here with us. I think it's really  
12 important as we are trying to coordinate closely  
13 with the SEC to have her here as we listen to our  
14 counterparts globally. Thank you. We'll take  
15 about a 15-minute break.

16 (Recess)

17 COMMISSIONER SOMMERS: I'm going to turn  
18 to our General Counsel Dan Berkovitz for an update  
19 on Dodd-Frank rulemaking. In the packet of  
20 information that we sent to all of you there is a  
21 comparison chart that compares Dodd- Frank to the  
22 European Commission proposal, to the legislation

1 from the Japanese FSA, and if you have any  
2 questions regarding that side-by-side on the  
3 Dodd-Frank issues, please direct them to Dan as  
4 he's the best person to answer those questions.  
5 As well as I think most all of you know that we  
6 have set up 30 rule-writing teams to assist with  
7 our rulemaking process in implementing Dodd- Frank  
8 and you have any specific questions regarding  
9 those 30 rule-writing teams, Dan also is the  
10 appropriate person to ask those questions to. I'm  
11 going to have him focus more on international  
12 issues that are in the implementation of  
13 Dodd-Frank and he has a presentation with regard  
14 to that.

15 I also would be remiss if I didn't say  
16 thank you because the side-by-side was a big  
17 effort on behalf of the staff of the Office of  
18 International Affairs and the General's Counsel's  
19 Office, so thank you so much for putting that  
20 together for us.

21 MR. BERKOVITZ: Thank you, Commissioner,  
22 and I'd also like to thank Terry, Jackie and DCIO

1 for the help on the presentations.

2 As you've mentioned, we had prepared the  
3 side-by-side of the Dodd-Frank and the E.C.  
4 legislation and the Japanese legislation, but the  
5 previous speakers, Mr. Pearson and Mr. Sumi,  
6 covered it extremely well and I don't think  
7 there's a need to go into additional detail. But  
8 I have to say on that point it did bring to mind a  
9 quote from Shakespeare and the quote from  
10 Shakespeare is from "Macbeth" and I forget exactly  
11 who said it but it's the scene where Lady Macbeth  
12 is urging Macbeth to kill the king. That quote  
13 came to mind not because of the references to  
14 maybe the duplicative, ungrammatical words in the  
15 Dodd-Frank legislation or the ponderous way it was  
16 written, but it the quote comes to mind as a  
17 complement to the presenter's, "If it were done  
18 when 'tis done, then well it were done quickly."  
19 So I'm not going to go into the side-by-side, but  
20 we'd be happy to answer questions about it.

21 I'm going to highlight some of the  
22 international issues in the legislation, some of



1 the issues with probably most interest to the  
2 members of the GMAC. I'll cover the  
3 extraterritoriality issue, when does Dodd-Frank  
4 have application extraterritorially? And then  
5 mention some of the specific rulemakings that may  
6 touch upon international interests and that would  
7 be the clearing and trading requirements, the swap  
8 data repositories and the foreign boards of trade.  
9 I would note that David and Duane will follow me  
10 on the panel and give the presentation on the  
11 foreign boards of trade so I will mention that  
12 that's an issue without getting into it and that  
13 will be the following presentation.

14 On extraterritoriality, generally the  
15 rule of statutory construction and application of  
16 U.S. law is that a statute will not apply  
17 extraterritorially unless there is an explicit  
18 statement of extraterritoriality within the  
19 legislation. We do have that statement in  
20 Dodd-Frank. The legislation itself states in  
21 Section 722(d), and this is in the presentation,  
22 "The law shall not apply to activities outside the

1 United States unless those activities, (a) have a  
2 direct and significant connection with activities  
3 in or effect on commerce of the United States; or  
4 (b) contravene CFTC rules issued to prevent  
5 evasion of the Dodd-Frank Act." So the second  
6 prong is you can't conduct your activities  
7 overseas to evade the domestic requirements.

8           The first prong, direct and significant  
9 connection with activities in or effect on  
10 commerce of the United States, is very similar to  
11 a provision that's in U.S. antitrust laws, direct  
12 and substantial connection with interstate  
13 commerce. So in looking to the reach of the U.S.  
14 law, we look to precedents in antitrust law and  
15 see what the application of that standard has  
16 been. Our reading of the law is that it's a very  
17 broad application. This is a standard that the  
18 courts have granted U.S. Authorities fairly  
19 significant extraterritorial application so the  
20 precedents are for a wide reach and a broad reach  
21 of U.S. law under Dodd-Frank.

22           The question is does this require

1 application of Dodd-Frank in every instance to the  
2 maximum extraterritorial reach possible under the  
3 statute or not. There is no bright-line rule that  
4 says that the statute applies to its fullest  
5 extent in every single possible application. It  
6 could apply or the agency may have, and we're  
7 looking at the very specific circumstances each  
8 individually, application or the Commission may  
9 apply it extraterritorially in those situations.  
10 So we're looking at the two questions for the  
11 various provisions in Dodd- Frank, does the  
12 extraterritorial provision permit application of  
13 U.S. law and should U.S. law apply in all those  
14 circumstances.

15           There are some circumstances where the  
16 statute provides clearer guidance than others on  
17 how a particular provision should apply  
18 extraterritorially. For example, there is no  
19 exemptive authority from swap or swap dealers so  
20 we wouldn't be able to say for example swaps  
21 extraterritorially are exempt from Dodd-Frank.  
22 There is no specific authority in the statute.

1 Similarly with respect as we'll talk about a  
2 little later facilities, for example, DCOs or  
3 trade repositories, whether the U.S. could or  
4 could not exempt a DCO from a registration  
5 requirement on the presence of a comparable  
6 regulatory scheme. So the two facilities where we  
7 would have that authority would be SEFs and DCOs  
8 and expressly not for trade repositories but it is  
9 for SEFs and DCOs that we could consider whether  
10 to exempt from registration based on a comparable  
11 foreign regulatory scheme. So we're looking at  
12 Dodd-Frank as we go through the individual  
13 rulemakings on a rule-by-rule basis on a  
14 provision-by-provision basis in Dodd-Frank  
15 regarding extraterritoriality and that  
16 determination will really be made on a  
17 rule-by-rule basis. We don't have a blanket rule  
18 to apply extraterritorially.

19           Some of the rules that have  
20 international application or interest and the  
21 speakers, Patrick talked about the clearing  
22 requirement for example in particular, the word

1 clearable. I think too bad Patrick has left the  
2 room although the word may not have existed prior  
3 to Dodd- Frank. I think maybe 30 or 40 years from  
4 now when the next addition of the Oxford English  
5 Dictionary comes out it's going to be in there and  
6 the first reference to clearable is probably going  
7 to be a speech by Chairman Gensler sometime in  
8 2009 and that will be the first entry into the  
9 OED.

10 CHAIRMAN GENSLER: Are you suggesting  
11 that I brought this, I don't know what you want  
12 Patrick would say, but distortion of the English  
13 language?

14 MR. BERKOVITZ: The English language is  
15 very flexible with all sorts of new words and new  
16 terms all the time.

17 COMMISSIONER O'MALIA: At least you're  
18 not credited with strategery.

19 MR. BERKOVITZ: 723(a)(3) contains a  
20 clearing requirement and clearable swaps must be  
21 submitted for clearing to a derivatives clearing  
22 organization registered with the CFTC and the CFTC

1 is to determine whether clearing is mandatory for  
2 a swap. This is similar to the process that was  
3 outlined for the E.C. The Dodd-Frank legislation  
4 provided that upon enactment all the swaps  
5 currently being cleared by DCO are automatically  
6 submitted to the CFTC for a determination of  
7 whether clearing should be mandatory and the CFTC  
8 had to make a determination within 90 days. We  
9 have been granted extensions by a number of the  
10 clearing organizations, by all the clearing  
11 organizations that were clearing as of the date of  
12 enactment to make those determinations but the  
13 agency hopefully intends to at this point proceed  
14 expeditiously and have as many of those  
15 determinations as possible on the effective date  
16 of the Act which would be 360 days after enactment  
17 so that these clearable determinations, a number  
18 of these swaps have already been submitted to the  
19 agency, and the agency will be working toward  
20 making those determinations in a timely manner.

21 The trading requirement follows from the  
22 clearing requirement that clearable swaps must be

1 traded on or through an exchange, a designated  
2 contract market or a swap execution facility that  
3 is registered with the CFTC. We're doing  
4 rulemakings as well on the trading requirement and  
5 the SEF requirement, the SEF core principles, what  
6 the core principles that a SEF needs to operate  
7 by, and what is a SEF is one of the fundamental  
8 questions in those rulemakings and we have had a  
9 roundtable on that and we are receiving many  
10 comments and the goal is to out with a proposed  
11 rule on that sometime in the fall of this year.

12           The commercial end user exception from  
13 the clearing requirement, entities are accepted if  
14 they're not financial, if they're using the swap  
15 for hedging commercial risk and if they inform the  
16 CFTC of how they are managing their risk. We  
17 shorthand refer to it as the commercial end user  
18 exception but it's really an exception for  
19 entities that are not financial entities that meet  
20 the other two prongs of the test and we're working  
21 on a rulemaking on that as well and that will give  
22 more definition to exactly under what

1 circumstances swaps do not have to be cleared.

2 As I mentioned, the exemptive authority,  
3 this is one instance where Congress has spoken in  
4 terms of giving some guidance, not definitive, on  
5 the extraterritorial application of the  
6 registration requirements for DCOs and SEFs. The  
7 international expressly provides that we have  
8 exemptive authority for a non-U.S. derivatives  
9 clearing organization or a SEF from registration  
10 if it finds that the SEF is subject to comparable  
11 comprehensive supervision and regulation by the  
12 appropriate governmental authorities in the home  
13 country. It doesn't require the exercise of that  
14 authority but it provides the CFTC with  
15 discretionary authority and the exempt DCO under  
16 those circumstances were the CFTC to grant such an  
17 exemption would be required to make available for  
18 inspection by CFTC and to be inspected by CFTC and  
19 make information available upon request. I would  
20 note that for swap data repositories there is no  
21 similar exemptive authority so that the test  
22 really would be did Congress intend the swap data



1 repository registration provision to apply  
2 extraterritorially? To what extent is the CFTC  
3 required to register a swap data repository that's  
4 located in a foreign jurisdiction? Another issue  
5 with the swap data repositories located in foreign  
6 jurisdictions is the access to the data, to what  
7 extent can foreign regulatory authorities get  
8 access to the data in the swap data repository?  
9 Can they get it directly or should perhaps they  
10 get it through the CFTC? That's another issue  
11 that we are working through in the rulemaking  
12 process.

13 I will leave the foreign board of trade  
14 issue for subsequent CFTC staff for David and  
15 Duane to discuss. As an outline of some of the  
16 key issues, there are obviously a lot of issues  
17 embedded in these general topics. We have as  
18 Commissioner Sommers mentioned 30 rulemakings and  
19 many of them touch upon these areas in one way or  
20 the other. Thank you.

21 COMMISSIONER SOMMERS: Now is your  
22 opportunity to ask Dan anything you want to know

1 about Dodd-Frank and our rulemaking process. Does  
2 anybody have any questions? Don?

3 MR. WILSON: I have some questions and  
4 comments. One of the opportunities that's  
5 presented by this extensive rejiggering process  
6 that we're going through is to increase the number  
7 of market participants in these markets so, first  
8 of all, in my view a swap which is cleared becomes  
9 economically equivalent to a future and as I think  
10 everybody knows, there are a lot of market  
11 participants like my firm like DRW which are very  
12 significant liquidity providers in the futures  
13 markets. I think that if in this process we miss  
14 the opportunity to encourage firms like mine to  
15 participate, we've missed an opportunity to reduce  
16 systemic risk and to reduce the reliance on  
17 too-big-to-fail institutions. In order to do that  
18 I think that you have to focus on issues related  
19 to access which cuts across a bunch of different  
20 rulemakings and one of the issues is making it  
21 viable for independent FCMs to participate as  
22 clearing members in these clearinghouses in these

1 products.

2 I was wondering if you'd like to comment  
3 on that. One of the issues that keeps on being  
4 brought up on both sides of the Atlantic is that  
5 there is a strong preference for FCMs to also be  
6 in the dealing process, in other words, to be able  
7 to participate in the default process. It's my  
8 view that by precluding independent FCMs from  
9 participating as clearing members because they  
10 don't trade themselves that you're potentially  
11 eliminating an entire group of market participants  
12 from coming in. I was wondering if you could  
13 comment on that.

14 CHAIRMAN GENSLER: Don, I'm not replying  
15 to your question, I'm asking you a question.  
16 Would you as a potential market maker be willing  
17 to participate in any forced allocation if a  
18 clearinghouse had a defaulted member and for the  
19 public there are a number of ways for the  
20 clearinghouse to deal with it, but one fail-safe  
21 is to say amongst their 20 or 30 or 50 members  
22 that they just force the allocation on some pro

1 rata basis of the defaulted member's positions?

2 MR. WILSON: In the Lehman process that  
3 the CME conducted, I think that we saw how a  
4 competitive auction process should function. We  
5 participated in that process and were the best  
6 bidder for three of the five Lehman futures  
7 portfolios so we're very comfortable participating  
8 in that process. That's a free-market process,  
9 but that process should work.

10 CHAIRMAN GENSLER: You've disclosed it  
11 publicly and I knew it privately that you  
12 participated in that, but would you also be  
13 willing if the auction failed to take your pro  
14 rata portion in a forced allocation among members?  
15 I think that's one thing clearinghouses have  
16 raised, some of them sitting at this table. If  
17 you were able to it might loosen this discussion  
18 up quite a bit, loosen it up among you and the  
19 clearinghouses because for the public the  
20 clearinghouses' membership is exclusionary to  
21 or 30 members and there are some like Don Wilson's  
22 firm that would like to become members of future

1 clearinghouses.

2 MR. WILSON: To be clear, again, our  
3 view of the world as things become more cleared is  
4 not necessarily that we want to self-clear.  
5 Certainly if we wanted to self-clear we're fine  
6 participating with whatever process is decided  
7 including the possibility of taking parts of  
8 portfolios in the event of a failed auction. But  
9 we think that the better model is to encourage the  
10 FCM model and in that case we're happy to work  
11 with FCMs in that default process. I'm not  
12 exactly sure what a failed auction means. Does  
13 that mean that nobody bid on the portfolio?

14 CHAIRMAN GENSLER: I don't know, but  
15 some of the clearinghouses around the table have  
16 said that that's a possibility.

17 MR. LIDDELL: A failed auction would be  
18 in which the clearinghouse wasn't able to dispose  
19 of a portfolio for a price that was commensurate  
20 margin it was holding from the defaulting member.  
21 In other words, it would have run out of initial  
22 margin if it accepted the best offer that they

1 got. But it really the underlying issue here is  
2 centered around the massive difference between  
3 handling the defaulter's portfolio on listed  
4 markets where you've got access to a market that's  
5 deep, it's liquid, it's well established, as  
6 opposed to handling large portfolios of illiquid  
7 positions where the clearinghouse is completely  
8 dependent upon a competitive auction process. For  
9 the purposes of the failed allocation, Mister  
10 Chairman, actually is not really to use it, the  
11 purpose of that is that it's a massive weapon at  
12 our disposal and the reason that we need that is  
13 because that forces the members who are handling  
14 the default to make sure the auction works. It  
15 was actually really interested in practice to see  
16 what happened with the Lehman portfolio because  
17 while that was all going on over the first few  
18 days, most of the members started to become  
19 really, really frightened and quite anxious and  
20 there were some heated moments actually because  
21 they couldn't see what we were doing, they  
22 couldn't see what the people that they had

1 deployed -- were doing in terms of hedging the  
2 portfolio so they didn't know what the PNR was  
3 done and they knew what the markets were doing  
4 because they're in the markets so that the  
5 possibility of exceeding the initial margin in  
6 their eyes was very, very high and they become  
7 really, really scared about this and I'm actually  
8 convinced that that dynamic was what caused us to  
9 have a very competitive auction so that the  
10 purpose of it is not to use it, it's to encourage  
11 appropriate behavior.

12           We're having some fascination  
13 discussions with some of the same firms around  
14 credit derivatives at the moment. I think Jeff  
15 has already passed this line, where because of the  
16 different nature of the credit derivatives markets  
17 in terms of its concentration and in particular in  
18 terms of its concentration around certain single  
19 names that only a few firms trade or they market  
20 in, the general view of our members is that that  
21 forced allocation can't be part of our armory  
22 because it just doesn't work, it just wouldn't be

1 fair and it's just hard to make that happen  
2 accepts in fact that there needs to be some  
3 weapon. What's being discussed now, and the banks  
4 seem to be strongly in favor of this at the moment  
5 at least is that we'll calculate what we need for  
6 a default fund, we do our normal initial margin  
7 calculations, we'll size our default fund  
8 appropriately for the credit default swap offering  
9 it separately, and then on top of that we'll stick  
10 a significant extra big lump in the default fund.  
11 In other words, the members would have to put  
12 quite a lot more of their capital on the line and  
13 directly at risk and it's that risk and that  
14 weapon that would create the behavior that we'd  
15 otherwise get through the forced allocation.

16 I'm sorry for the long answer to your  
17 question, but it's a massively important piece of  
18 behavioral inducement that we really need and you  
19 can get it one or two different ways, but if we  
20 don't have that then we are very nervous at  
21 relying on an auction just running its course.

22 CHAIRMAN GENSLER: I interrupted Dan.



1 He can answer the legal question. I was trying to  
2 help you two talk to each other across this public  
3 meeting.

4 MR. WILSON: Just a couple of comments  
5 on that. I think that a lot of these markets are  
6 extremely liquid and that's one of the things  
7 that's said to justify this is that they're  
8 illiquid but I think that one of the markets that  
9 we're interested in is the vanilla interest rate  
10 swap market which obviously LCH clears quite a lot  
11 of and I think that everybody knows that's a very  
12 liquid market. A lot of the CDS markets are  
13 liquid too. There are certainly some illiquid  
14 components of that as well, but I think that in  
15 these liquid markets a traditional auction process  
16 should be very effective. And to the extent that  
17 the initial margin doesn't cover the price, there  
18 are other ways of dealing with that. A forced  
19 allocation isn't the only way.

20 COMMISSIONER SOMMERS: Dan, do you have  
21 any comments?

22 MR. BERKOVITZ: I have nothing to add to

1 the discussion that's already occurred.

2 MR. WASSERMAN: It seems like we're  
3 trying to balance two things. On the one hand, it  
4 is appropriate and indeed necessary and part of  
5 the core principles that clearinghouses have  
6 appropriate participant eligibility requirements.  
7 On the other hand, we want to avoid barriers to  
8 entry, and it seems to me that part of the way to  
9 maybe square this to the extent that there is  
10 conflict in this is to make sure that we're  
11 looking at this with appropriate imagination to  
12 say what are the alternative ways? So to the  
13 extent that it's necessary to have forced  
14 allocation of a means of socializing, then you  
15 need to look and ask how can that be accomplished?  
16 Must it be at that particular clearing member?  
17 Can a clearing member for instance outsource that  
18 to perhaps another member under the supervision of  
19 the clearinghouse? Or as you mentioned there are  
20 other ways of accomplishing it besides forced  
21 allocation so I guess we're hoping to see that  
22 folks are attacking this imaginatively rather than

1 saying either you have this capability or you  
2 don't qualify, go away.

3 COMMISSIONER SOMMERS: Conrad?

4 MR. VOLSTAD: I'm a bit away from  
5 running big organizations but when I was working  
6 for one of the big investment banks among other  
7 responsibilities I had responsibility for futures  
8 and futures clearance was an extraordinarily  
9 competitive business and I would imagine that  
10 clearing of OTC derivatives is going to become  
11 extraordinarily competitive as well. Recently  
12 Barclays took on \$200 billion of derivative  
13 clearing for Monte dei Paschi in Italy and I  
14 would have thought that the cost of being a client  
15 clearer, clearing through a clearing member,  
16 should not be very onerous as competition sets in  
17 and that one could make markets by being a client  
18 of a clearing member. I don't know the pricing  
19 right now but I think it's got to emerge down  
20 toward what you will pay above and beyond being a  
21 clearing member, you save by not having to have  
22 the capital at risk.

1                   MR. WILSON: We're not concerned about  
2 the pricing so much. It's the actual access. For  
3 instance right now, LCH has worked on coming out  
4 with this new client model but the way that the  
5 workflows work are defined if we wanted to trade  
6 with a nondealer and clear that, in other words,  
7 provide liquidity to a nondealer and then clear  
8 that trade at swap clear, my understanding is the  
9 way that it's structured right now is specifically  
10 to preclude that type of activity which we think  
11 is not in the best interests of the overall  
12 functioning of the market. I'll also highlight at  
13 the CME that the CME has a CDS product which  
14 hasn't really taken off but we've been unable to  
15 come to a clearing arrangement with any of the  
16 dealer clearing members who are able to offer that  
17 product and it's not a question of price.

18                   COMMISSIONER SOMMERS: Jeff?

19                   MR. SPRECHER: You have another  
20 alternative for that clearing.

21                   MR. WILSON: We've also had a hard time  
22 figuring out a way to access that market through

1 that alternative, but thank you, Jeff.

2 MR. SPRECHER: We can talk afterwards;  
3 \$300 million worth has come in already.

4 CHAIRMAN GENSLER: This is not so much a  
5 legal question, but the statute does have a number  
6 of access provisions. One is that clearinghouses  
7 give nondiscriminatory open access to trading  
8 platforms. One is that the trading platforms have  
9 impartial access. That's in the statute. But  
10 also you're raising the question of access through  
11 participant edibility and I think Bob Wasserman  
12 said it very well that these participant  
13 eligibility rules should not become barriers to  
14 entry and what Don Wilson I guess is highlighting  
15 is maybe right now, am I correct, your sense is  
16 they are barriers to entry.

17 MR. WILSON: Yes, that's correct, at  
18 this time they are.

19 COMMISSIONER SOMMERS: Laurie?

20 MS. FERBER: If I may, I think certainly  
21 it is our view that there they are barriers to  
22 entry. I think we'll be very interested to see

1 where the Commission goes with this and where  
2 other regulators go, the gap or potential gap  
3 between Bob's comment of encouraging the  
4 clearinghouses to think creatively, I think  
5 imaginatively about approaches to this, and  
6 whether the CFTC is going to put real teeth in the  
7 fair and open access criteria. I think having  
8 been at the hands of the clearinghouses for quite  
9 a while we'd like to see the playing field set by  
10 the Commission and not just by the clearinghouses  
11 and members.

12 CHAIRMAN GENSLER: Is it your view,  
13 Laurie, that the playing field is not level right  
14 now?

15 MS. FERBER: Yes. I think the barriers  
16 to entry do not track to the actual products and  
17 there's much room for approaches that would open  
18 up the FCM clearing community and that's what  
19 we're hearing from buy-side clients who want to  
20 have a different choice of access.

21 MR. WILSON: We think that the ownership  
22 restrictions are not the way to solve this

1 problem. We think that the ownership restrictions  
2 may actually prevent competition rather than solve  
3 this problem. We think it's more of a governance  
4 issue and a specific rulemaking issue.

5 COMMISSIONER SOMMERS: Does anyone else  
6 have any questions or comments with regard to the  
7 rulemaking in Dodd-Frank, legal questions that Dan  
8 may be able to answer?

9 MR. OKOCHI: I have more of a step-back  
10 broader question. The E.C. proposals have some  
11 rules that could be used in your rulemaking  
12 process. Are there any thoughts on the approach,  
13 for example, the information threshold, clearing  
14 threshold could be used to define major swap  
15 participants. There are penalties for SDRs that  
16 are defined in the proposal. Is there a general  
17 approach that the CFTC will take on taking that  
18 into consideration?

19 MR. BERKOVITZ: On all the rulemaking  
20 teams where we've identified an international  
21 component or potentially international interest,  
22 Jackie has got a member of the team and that is

1 being factored into each of the rulemaking teams  
2 what is the international approach. Is it a good  
3 idea? Where should we consider harmonization?  
4 And there have been a number of standards  
5 specifically on clearing where these have been  
6 really factored in very heavily into the  
7 rulemaking team process, so, yes.

8 MS. MESA: I would not something that  
9 Chairman Gensler said publicly last week so that  
10 I'm taking your words, once the European  
11 Commission proposal came out, the rulemaking teams  
12 were given instruction from him to implement  
13 whatever we could take from the European  
14 Commission's proposals so that you couldn't get a  
15 stronger recommendation than that and the  
16 rulemaking teams are trying to actively implement  
17 wherever we can and wherever it makes sense.

18 COMMISSIONER SOMMERS: Richard?

19 MR. BERLIAND: I think one of the  
20 takeaways from today's session is that if we look  
21 at the clearing process and we look at the trade  
22 repository process, the timing of the European,



1 Japanese and American processes are sufficiently  
2 on top of each other that we've had that  
3 opportunity to go back and check what the other  
4 guys bring to the table and then put that into the  
5 process. I think as Patrick highlighted, the  
6 differences between the two in those areas or  
7 three if we include the Japanese version as well  
8 are relatively limited and for all intents and  
9 purposes I think where the differences are they  
10 are capable of being ironed out and there is a  
11 process to do so.

12 The area that I think we've discussed  
13 very little today is the trading side and that is  
14 where our timelines are out of synch because the  
15 MIFID review isn't really going to get going until  
16 the American process is reasonably far advanced  
17 and I think it's going to be a lot harder to back  
18 up. I appreciate that this may be more a  
19 discussion of policy than a specific legal  
20 process, but I'm interested as to what your view  
21 is on the process to ensure we don't get so far  
22 out of synch on the trading side, in particular

1 definitions of SEFs, and it's my view that there  
2 are higher risks of philosophical differences of  
3 opinion on the trading side than has been the case  
4 on clearing not least where we had the statement  
5 from the G-20 which made clearing one of I would  
6 say the less controversial areas compared to  
7 trading. But I'd be interested in your view on  
8 how we stay in synch given that the Europeans are  
9 a little bit behind or actually quite a long way  
10 behind given the separation of the processes.

11 MR. BERKOVITZ: I will start out with  
12 the answer and then I'm going to hand off to  
13 Jackie as to how we can integrate the two on the  
14 different timelines. I would emphasize that our  
15 timeline is statutorily mandated. At CFTC we  
16 virtually no flexibility in the timeline for  
17 completing these rules. In order to meet the  
18 deadline for July 16, 2011, 360 days after  
19 enactment, we're working diligently on the  
20 proposed rules right now. We've had three come  
21 out last Friday and it's the intent to have a  
22 number of others proposed in the upcoming weeks.

1 We have virtually no flexibility on the speed at  
2 which we're going as it's dictated to us by  
3 Congress so that within that timeframe we'll be  
4 taking into account what Europe is doing and I'll  
5 let Jackie answer that.

6 MS. MESA: I think Patrick said earlier  
7 that it's not a surprise that the European  
8 Commission's proposal came out largely in line  
9 with Dodd-Frank and it wasn't because they just  
10 looked at on paper once Dodd-Frank was out and  
11 then just picked it up and implemented it, there  
12 were conversations before even Dodd-Frank was  
13 passed with the European Commission as there is on  
14 the trading bit of it. Patrick's team isn't  
15 handling it on the European Commission. On that  
16 side it's Maria Valensa but we've had regular  
17 calls with Maria Valensa and her staff and our  
18 staff working here on the trading requirement to  
19 take on ideas that they're thinking about and to  
20 share with them where we're going.

21 You're right that this issue is highly  
22 controversial even in Europe and Peter can talk

1 about that. This is a hotly debated issue, but  
2 we're taking ideas from them and they're taking  
3 ideas from us and I think we're going to see some  
4 of the similar results that we saw on the trading  
5 and clearing part of it.

6 COMMISSIONER SOMMERS: Are there any  
7 other comments before we move to the foreign board  
8 of trade issue? If not, we'll move to two of our  
9 CFTC staff from the Division of Market Oversight,  
10 Duane Andreson and David Van Wagner to present to  
11 us on the foreign board of trade issues that are  
12 within the Dodd-Frank and the rulemaking that  
13 we'll have to do on this issue.

14 MR. VAN WAGNER: Good afternoon. This  
15 is just by way of introduction to Duane getting  
16 control of the PowerPoint. Dodd-Frank authorized  
17 the Commission to establish a new market category,  
18 registered foreign boards of trade. While the  
19 rulemaking to establish rules around the process  
20 and standards for registered foreign boards of  
21 trade was discretionary and not mandatory, the  
22 Commission has decided to go ahead with the

1 rulemaking because we thought it was important to  
2 bring more transparency to the process and the  
3 standards by which foreign boards of trade come  
4 and get access to U.S.-based traders and to  
5 replace the current process that we use which is a  
6 staff-driven no action process which has been in  
7 place or 14 years or so. By way of ticking  
8 through the Dodd-Frank provisions and some of the  
9 issues that we're thinking about in the context of  
10 the rulemaking, Duane will take you through that.

11 MR. ANDRESEN: Thanks, David. Good  
12 afternoon. There's the famous disclaimer, and  
13 this slide looks at lot like the one that was just  
14 up there for a few minutes during the last  
15 discussion.

16 The Dodd-Frank bill provides that the  
17 Commission may require registered for foreign  
18 boards of trade. They want to permit identified  
19 members and other participants in the United  
20 States with direction access to their trading  
21 system. It also says the CFTC can adopt rules and  
22 regulations prescribing the procedures and

1 requirements applicable to that registration and  
2 that's the duty of the current rulemaking team.

3           The registration requirement as David  
4 mentioned will replace the current practice of  
5 issuing staff no action letters. Currently we  
6 have 20 active letters, 20 exchanges, that have  
7 active no action letters of whom 14 are showing  
8 volume from within the United States. In adopting  
9 these rules and regulations, the Commission shall  
10 consider whether the foreign board of trade is  
11 subject to comparable comprehensive supervision  
12 and regulation by the appropriate governmental  
13 authorities in the FBOT's home country. I  
14 understand from earlier today that was all  
15 whittled down to whether the FBOT is subject to  
16 equivalent regulation in its home country.

17           Some other things that would be looked  
18 at during the context of the registration  
19 requirement are these seven areas probably because  
20 we're not really certain at this point, but these  
21 are the seven areas that perform the basis of the  
22 review for the no action process, in particular,

1 the trading system, does it comply with the IOSCO  
2 principles, settlement and clearing, the same  
3 kinds of things that the Commission would look at  
4 as part of the DCM registration.

5 The Dodd-Frank bill also has special  
6 provisions for linked contracts, that is, the  
7 Commission cannot permit a foreign board of trade  
8 to provide direct access to its trading system  
9 unless the Commission determines that the foreign  
10 board of trade does the following with respect to  
11 any linked contract, that is, a contract that  
12 settles against any price of a contract listed in  
13 a U.S.-registered entity. The foreign board of  
14 trade must make available daily trading  
15 information that's equivalent to that of the  
16 linked contract, it must establish equivalent  
17 position limits, it or its regulatory authority  
18 must have the capability to require position  
19 adjustments, it must provide information to the  
20 Commission, large trader information, that is  
21 comparable to that provided for the linked  
22 contract and it must provide the Commission

1 information for the aggregate trader positions.

2 Those are the provisions in the  
3 Dodd-Frank Act. Some of the considerations that  
4 would impact a rulemaking with respect to  
5 registration for a foreign board of trade are on  
6 the next three slides. That is, as we said, the  
7 registration requirement replaces the current  
8 practice of no action letters. To what extent  
9 should the registration submission requirements  
10 match those, the requirements of the no action  
11 letters? And should registration be viewed as a  
12 codification of the current no action policy or  
13 something different? Secondly, what standard  
14 should the Commission use to determine if a  
15 foreign board of trade should be eligible for  
16 registration? The four standards that are listed  
17 here are those that were published in the  
18 Commission's policy statement in 2006 in which the  
19 Commission endorsed the no action policy.

20 Another set of provisions that are  
21 considered would be considered in any rulemaking.  
22 What should constitute comparable comprehensive



1 supervision and regulation by appropriate  
2 government authorities in the foreign board of  
3 trade's home country? To what extent does that  
4 mean that the foreign board of trade is subject to  
5 comprehensive supervision and regulation that is  
6 comparable to that the CFTC provides in overseeing  
7 its DCMs? Secondly, how should the registration  
8 requirements affect foreign boards of trade that  
9 current have no action relief? Should the 20  
10 foreign boards of trade be grandfathered and not  
11 have to apply for registration at all? Should  
12 there be some kind of limited registration based  
13 on the fact that they've already been reviewed  
14 once and determined to be adequate for the no  
15 action process? Or should they be treated like a  
16 brand-new applicant?

17 Finally in terms of the consideration,  
18 the Dodd- Frank bill defines direct access for  
19 purpose of foreign board of trade registration to  
20 refer to an explicit grant of authority by a  
21 foreign board of trade to an identified member or  
22 other participant located in the U.S. to enter

1 trades directly into the trade-matching system of  
2 the foreign board of trade. We are well aware  
3 that there are many different methodologies for  
4 electronic transmission of orders that are not  
5 exactly like this but are very similar to this.  
6 For instance, if a 3010 firm allows orders to be  
7 routed to it and they simply pass through the  
8 risk- management filter without any additional  
9 interface with the infrastructure, is that not  
10 direct access? And what about a firm that  
11 authorized its clients to connect directly to the  
12 foreign board of trade under the firm's mnemonic  
13 or password referred to IOSCO as sponsored access?  
14 To what extent are those kinds of access to a  
15 trade-matching engine equivalent to direct access  
16 such that the Commission should consider requiring  
17 those foreign boards of trade to register?

18 The proposed registration rules will be  
19 published in the Federal Register before the end  
20 of the year. We would certainly welcome your  
21 comments on any area of the proposed rule. And  
22 the rulemaking is on a 1-year timeframe and even

1     though it's discretionary it's on a 360-day  
2     timeframe and if you wish to make comments there  
3     is a way to make comments including the FBOT  
4     registration team page if you wish to make  
5     comments before any proposed rule hits the street.  
6     Thank you very much.

7             COMMISSIONER SOMMERS:   Thank you, Duane.  
8     Richard?

9             MR. BERLIAND:   Duane, thank you.   I  
10    think as Chairman Gensler has said, the process of  
11    the no action letters is something that grew up  
12    over the years.   I'm sure we wouldn't have  
13    introduced it if we'd known it had grown into  
14    something that it is today.   But my main concern  
15    is that to have a process that is one way, i.e., a  
16    process where a foreign board of trade wanting to  
17    grant access to U.S. participants goes under this  
18    process is going to lead inevitably to a whole  
19    load of bilateral arrangements that exist around  
20    the world, so whether it's ICE or any of the  
21    entities that exist in the U.S. that was to  
22    provide access to other countries, I think it

1 would be great whether it's using IOSCO or  
2 otherwise to a process where we could come up with  
3 a global standard and I think undoubtedly these  
4 are going to incorporate a lot of best practices  
5 to do just that. But much as I think the Part 30  
6 process which had so much of this mutual  
7 recognition and sharing of information, whether we  
8 could come up with something similar I think it  
9 would be a tremendous step forward of efficiency  
10 in trying to achieve what will be a better and  
11 more regulated process. But I would strongly  
12 endorse the idea that we try to use IOSCO to come  
13 up with a multilateral process rather than  
14 everybody putting their own access rights in  
15 place.

16 COMMISSIONER SOMMERS: Tom?

17 MR. CALLAHAN: My question is how do we  
18 ensure that as the Commission moves forward with  
19 this discretionary rule-writing that there are not  
20 unintended consequences, to take some of Richard's  
21 comments a bit further, that create trade  
22 barriers? Liffe has been subject to this no

1 action regime since 1998 and our experience is  
2 that it's worked exceptionally well; that although  
3 informal it's a very robust process that was  
4 further strengthened in 2008 to give further  
5 requirements around foreign contracts linked to  
6 U.S. markets; certainly requires a high level of  
7 coordination between international regulators but  
8 certainly from everything we've heard today that's  
9 happening. Our concern given that one-third of  
10 the volume on our European Liffe Exchange comes  
11 from U.S. Clients which is a direct result I  
12 think of the success of the current no action  
13 regime, that if this causes foreign jurisdictions  
14 to retaliate and force their own registrations  
15 although it may be helpful as Richard said if  
16 there are some standards but there will be no  
17 requirement that those are followed, there could  
18 be very severe unintended consequences. We have a  
19 process right now that I think has been  
20 exceptionally effective and it sounds from the  
21 proposal that we're formalizing processes in many  
22 instances that are happening right now anyway.

1 How do we guard against those unintended  
2 consequences that could really hurt global flows  
3 of capital?

4 MS. MESA: If you look around the globe  
5 at other countries' mutual recognition regimes,  
6 they have a registration process in place. It's  
7 sort of what we're contemplating at the CFTC. I  
8 think the process that this is embedded in a  
9 statute should give the foreign exchanges more  
10 comfort because a staff no action today could just  
11 be ripped out by staff at any time. So this is a  
12 formal in- statute recognition process which will  
13 grant access to U.S. Customers. I think you  
14 rightly point out that we're codifying what's  
15 there now on an informal basis. There will of  
16 course be some adjustments to keep in line with  
17 raising the bar, but we hope those won't be out of  
18 synch with what other regulators are doing around  
19 the globe.

20 CHAIRMAN GENSLER: Tom and Jeff might  
21 want to comment on this. One of the things that  
22 I've found is, and it was even in my confirmation

1 process, this whole concept that a regulatory  
2 body, the CFTC, over some 14 years has done 20 of  
3 these at the staff level and weren't necessarily  
4 at the full Commission level even though sometimes  
5 they went through what was called an absent  
6 objection process. That lacks some credibility to  
7 certain members of Congress and the public so that  
8 here is a very transparent process. The public  
9 will be able to comment on the set of proposed  
10 rules and I'm sure we'll adjust them in some way  
11 before we get to the final rules because that's  
12 the process. I'm encouraged by this. I think it  
13 brings greater transparency and public input and  
14 hopefully uniformity. Again I sense what you're  
15 saying is you're a little nervous because  
16 something has worked and so what you know has  
17 worked and you're worried for New York Stock  
18 Exchange Liffe as to what might come.

19 MR. CALLAHAN: I think that's exactly  
20 right in that we are formalizing a process that's  
21 been in place for 14 years, it's tried and true  
22 and it has worked.

1                   CHAIRMAN GENSLER: I would say that it  
2 hasn't fully worked. It hasn't gained the full  
3 confidence and credibility of the public.

4                   MR. CALLAHAN: That's a perception issue  
5 which may be valid, but the technical details of  
6 how this process worked before and after are going  
7 to be largely unchanged at least from what I  
8 understand from the proposal so that I'm just  
9 worried again about the unintended consequences,  
10 that if the facts aren't changing we're just  
11 formalizing this through this formal registration  
12 process, how do we guard against this becoming a  
13 trade barrier? And I think that's a hard question  
14 to answer and we're not going to know until the  
15 rule goes into affect.

16                   COMMISSIONER SOMMERS: Mike?

17                   COMMISSIONER DUNN: If I may enter in  
18 here with a couple of thoughts. First of all,  
19 Tom, I understand your concerns but in my opinion  
20 this gives much greater legal certainty as to what  
21 is taking place because it is codified now and we  
22 have had recent situations where a chairman or a



1 division director has said I'm going to change  
2 that no action letter and just like that with no  
3 rhyme or reason. Under our regulations they don't  
4 have to tell you why they're going to be changing  
5 that, they can just yank it and I feel this gives  
6 a great deal more uncertainty.

7           The second aspect is uniformity and  
8 during my tenure as I see things evolving here on  
9 these no action letters, that initially there were  
10 a couple of points said we have to have these in  
11 there, later on three or four more points were  
12 added and now we're up to seven points that to be  
13 added. All of those originally were in there and  
14 the no action letter only applies to those that  
15 had that no action letter to them and not  
16 uniformly across the entire industry, so that in  
17 my opinion this really does give an opportunity  
18 for everybody to be on a level playing field.

19           COMMISSIONER SOMMERS: I would say that  
20 I agree with codifying and formalizing the  
21 process, but in doing so to take into  
22 consideration some of the concerns of the people

1 who have been operating under the no action  
2 process and a process that has not had problems  
3 besides the linked contract issues that we've  
4 dealt with separately.

5 I do have a question for Jackie. Is  
6 there is an IOSCO work stream on mutual  
7 recognition?

8 MS. MESA: There was, and maybe Duane  
9 knows the date, of the screen-based project in  
10 IOSCO which came up with a mutual-recognition  
11 regime for foreign boards of trade. It's  
12 something that we at the CFTC use as the basis for  
13 a no action process and it's what other countries  
14 modeled their regimes on mutual recognition on.  
15 It's been quite some time since we've looked at  
16 that, so maybe what I'm hearing is it's time to  
17 take another look at it in IOSCO, but there is  
18 something that tried to harmonize this process  
19 really early on.

20 COMMISSIONER SOMMERS: Thank you.  
21 Bonnie?

22 MS. LITT: Duane, you mentioned that

1     there was some talk about what direct access from  
2     the U.S. means and you talked about sponsored  
3     access and access through firm- provided filters.  
4     Is there any thought that this new provision is  
5     going to change the way you thought about what  
6     presence in the U.S. means under the no action  
7     letters versus under this statutory and regulatory  
8     regime?

9                   MR. ANDRESEN:   It's hard to say now but  
10    I wouldn't think so.

11                   MS. LITT:    You wouldn't think that it  
12    would change?

13                   MR. ANDRESEN:   No.   The idea that the  
14    direct access is from the United States is in the  
15    definition.   It's just what is encompassed within  
16    that definition in the real world in terms of  
17    order routing systems, but there would still be  
18    players from within the United States who would be  
19    impacted.

20                   MS. LITT:    Having been around for the  
21    first time we talked about this stuff, it was a  
22    very big issue because obviously when FCMs provide

1 access through their own trading systems, that  
2 doesn't necessarily make the exchange present in  
3 the United States and this is another place where  
4 there is some room for mischief because if you  
5 overly broadly define what presence in a country  
6 means, and in an electronic world what in the  
7 world does that mean anyway, you worry about  
8 having too many people cross-registering across so  
9 that I think it's something we have to be  
10 conscious of. Obviously the no action regime has  
11 worked well in this regard so that it's a place  
12 where we would vote thumbs up for those  
13 interpretations.

14 MR. VAN WAGNER: I'd add that Congress  
15 had some decent wordage on this. There is wording  
16 in there about the exchange itself being the actor  
17 which gives explicit authority which is helpful.  
18 But as with all things I think in Dodd-Frank, we  
19 are concerned about the possibility of evasion  
20 where an exchange might encourage direct access  
21 because they don't want to bother coming to us. I  
22 think it's fair to say on this issue there will be

1 a number of questions regardless of how the  
2 Commission proposes the rule so I would definitely  
3 watch the Federal Register space.

4 CHAIRMAN GENSLER: Anthony?

5 MR. BELCHAMBERS: I think that the shift  
6 from no action is entirely right and I think it's  
7 an unacceptable concept in the post-crisis climate  
8 to say that it's no action, it sounds rather  
9 negative so that I think the idea of going to an  
10 overseas licensing regime which is where most of  
11 the jurisdictions are moving toward is entirely  
12 right. I think the risk is, and I think Bonnie  
13 touched on it, will this be a vehicle for  
14 redefining what is a U.S. Exchange and I think  
15 there is a certain nervousness because as you know  
16 we had this debate 3 or 4 years ago. Was it  
17 longer? I'm getting older and I feel my memory is  
18 no good anymore.

19 The other thing is whether or not there  
20 are going to be additional rules that if you like  
21 are brought under this new title of describing the  
22 way in which exchanges can do business in the

1 U.S., and I think those are the worry areas. But  
2 my understanding is that there isn't going to be  
3 raft of new rules sitting under this and that it's  
4 going to be more of the way of describing it as a  
5 positive regime for the purposes of the Hill  
6 particularly rather than a negative regime.

7 CHAIRMAN GENSLER: Poor Duane is trying  
8 to answer the questions. He doesn't really know  
9 there are five independently Senate confirmed  
10 Commissioners, so I want to get Duane off the hook  
11 for a little bit, and as David Wan Wagner said,  
12 you'll have to wait for the Federal Register  
13 release. We have a lot to debate and discuss. I  
14 note that because the old foreign board of trade  
15 no action regime was about futures and now we have  
16 this product called swaps and so one of the things  
17 I've at least been briefed on is how does this  
18 relate to swaps? That may not go to Bonnie's  
19 question, but I wouldn't put Duane in the box of  
20 saying nothing is going to change because I think  
21 that would be unfair to Duane, and we have the  
22 whole world of swaps in here too.

1                   MR. ANDRESEN: I would certainly  
2 encourage you to comment. Your comments will be  
3 taken into account, believe me. There are some  
4 areas that we're really interested in how the  
5 industry feels about it and how our approach  
6 should go and I promise you we will consider all  
7 comments.

8                   COMMISSIONER SOMMERS: If there are no  
9 other comments on specifically foreign board of  
10 trade issues, I think I'll ask if any of the  
11 members have any general comments and we can wrap  
12 up the meeting unbelievably early today. Do any  
13 of my fellow Commissioners have any closing  
14 comments? I want to say thank you again to not  
15 only the CFTC staff that put together the  
16 presentations that are on the agenda today, but to  
17 all of you for being here, and especially to Peter  
18 and Patrick for being here and for Mr. Sumi and  
19 Mr. Mori from the Japanese FSA, thank you so much  
20 for traveling. I'm sure it's been a very long day  
21 for you and we appreciate you sitting through this  
22 almost 4-hour meeting to talk about these very

1 important issues. Do you have any closing  
2 comments?

3 CHAIRMAN GENSLER: I was going to thank  
4 Jill for her leadership of this. These  
5 international issues are so important. And to all  
6 five the Commissioners I also thank them for their  
7 work and the full panel for the discussion. I'm  
8 glad to see that Roger and Don got closer to this  
9 participant membership thing, but it seems like  
10 there's a little bit more work to be done there.

11 COMMISSIONER DUNN: I'd like to thank  
12 all of the participants and all our presenters.  
13 Mister Chairman, I thought you were very artful in  
14 getting that exchange of ideas there, and I wish  
15 everyone a pleasant movie on their flight home.

16 COMMISSIONER SOMMERS: Thank you to  
17 everyone and especially to my staff, Mike Otten  
18 who is our new designated federal official for the  
19 Global Markets Advisory Committee and Marcia Blase  
20 and my assistant Sharon Floyd who put together all  
21 the specific details for this. If you have any  
22 further questions with regard to this meeting,



1 don't hesitate to call my office. Thank you.

2 (Whereupon, at 4:25 p.m., the

3 PROCEEDINGS were adjourned.)

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## 1 CERTIFICATE OF NOTARY PUBLIC

2 I, Carleton J. Anderson, III do hereby  
3 certify that the witness whose testimony appears  
4 in the foregoing hearing was duly sworn by me;  
5 that the testimony of said witness was taken by me  
6 and thereafter reduced to print under my  
7 direction; that said deposition is a true record  
8 of the testimony given by said witness; that I am  
9 neither counsel for, related to, nor employed by  
10 any of the parties to the action in which these  
11 proceedings were taken; and, furthermore, that I  
12 am neither a relative or employee of any attorney  
13 or counsel employed by the parties hereto, nor  
14 financially or otherwise interested in the outcome  
15 of this action.

16 /s/Carleton J. Anderson, III

17

18

19 Notary Public in and for the

20 Commonwealth of Virginia

21 Commission No. 351998

22 Expires: November 30, 2012