

Prepared Written Testimony on Behalf of the

Futures Industry Association by

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Before the U.S. House Committee on Agriculture at a Hearing  
on Proposed Legislation to Amend the Commodity Exchange Act

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Mr. Chairman and members of the Committee, I am Mark Young, appearing on behalf of the Futures Industry Association. FIA appreciates the opportunity to present its views to the Committee on the pending legislation to address futures regulation and energy prices.

FIA regular member firms are registered with the Commodity Futures Trading Commission as futures commission merchants (“FCMs”). FIA’s FCM member firms execute customer orders for and provide the financial guarantees underwriting more than 90% of the futures contracts traded on U.S. exchanges. FIA member firms also play a substantial role in executing and clearing orders for customers world-wide in futures contracts traded on non-U.S. exchanges. As the leading trade association for the U.S. futures industry, FIA and its member firms have an acute interest in the many legislative proposals you are considering.

FIA has a long record with this Committee. We have supported every legislative reform of futures regulation dating back to the Commodity Futures Trading Commission Act of 1974 as well as each Reauthorization of the CFTC since 1978. As in the past, FIA is committed to working with this Committee on constructive legislation to modernize regulation and adapt to the ever quickening pace of change in futures trading around the world.

While I suspect FIA, led by John Damgard, is well known to many members of this Committee, I am sure I am not as well known. I am a partner in the law firm of Kirkland and Ellis, LLP in the Washington, DC office. In 1977, I joined the CFTC's legal staff when I graduated from law school. I then moved to Kirkland in 1982. I have represented clients in every CFTC reauthorization from 1978 to 2008. I now represent FIA on a variety of legislative, litigation and regulatory matters. I represent other clients as well on a variety of regulatory and litigation matters. I do not now represent any U.S. futures exchanges or foreign futures exchanges. Also, since 1991, I have taught a course in Derivatives Regulation as an Adjunct Professor at the Georgetown University Law Center.

FIA and its members have long believed that futures market price integrity is a paramount concern. FIA does not support higher prices or lower prices on any market. FIA does support having prices discovered openly and competitively on what the Commodity Exchange Act calls, "liquid, fair and financially secure trading facilities."

In 1974, this Committee described the Commodity Exchange Act as a "comprehensive regulatory structure to oversee the volatile and esoteric futures trading complex," a description the U.S. Supreme Court later called an "apt[] characteriz[ation]."<sup>1</sup> Amending this complex structure, under even the best of circumstances, can be a difficult challenge. FIA thanks this Committee for your thorough and thoughtful approach to deliberating on the benefits and costs of the many different legislative proposals before you.

FIA views each legislative proposal through the lens of seven basic principles.

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<sup>1</sup> *Merrill Lynch v. Curran*, 456 U.S. 353, 355-356 (1982).

1. Futures trading serves the congressionally-endorsed national public interests in commodity price risk management and commodity price discovery. Price manipulation robs futures markets of their ability to serve those public interests.
2. The Commodity Futures Trading Commission now has vast powers to prevent price manipulation, ranging from position limits and vigorous enforcement actions to transparent market surveillance and emergency powers . **The CFTC is an effective agency; it needs additional resources more than it needs additional powers.**
3. Speculators are essential for futures markets, as the Supreme Court and many commentators have found.<sup>2</sup> Without speculators, U.S. futures markets would not serve the national public interest. **Speculation is not price manipulation.** Those who claim it is would also equate oxygen with air pollution.
4. Congress should not enact legislation that would create disincentives for futures business to be conducted through U.S. firms and on U.S. markets, which could cost U.S. jobs. Congress should also not enact legislation that would hinder the CFTC's market oversight and price transparency.
5. The forces of globalization and technological innovation are linking economic and financial activities world-wide more every day. No legislation could repeal that market reality.
6. Loopholes are a misnomer. Congress made many deliberate and realistic policy choices from 1982 to 2000, many of which originated in this Committee. Each was intended to serve the public interest, not any special interest. Those choices have served the public interest well, resulting in strong growth, more transparency and less financial risk in U.S. derivatives markets.
7. The CFTC's legal authority over U.S. futures exchanges, traders and firms is and must be greater and more direct than its legal authority over foreign futures exchanges, traders and firms. **International cooperation and coordination is therefore an essential component of effective market surveillance for global markets.**

Along with other financial services trade associations, FIA has provided a list of measures Congress should enact to deal with the current market situation. Those

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<sup>2</sup> *Merrill Lynch v. Curran*, 456 U.S. at 390 (speculators play a "crucial role in an effective and orderly futures market"); *Economist*, "Don't blame the Speculators," July 5-11, (at.15-16 ("speculators provide a vital service"); Robert Samuelson, "Lets Shoot the Speculators," Newsweek, July 7-14, 2008 ("What makes the futures markets work is the large number of purely financial players—"speculators" just in it for the money—who often take the other side of hedgers' trades."); Richard W. Rahn, "Greedy Speculators," Washington Times, June 25, 2008 at A22 ("There are many...market speculators who provide liquidity to the market and fill the void if the numbers of short and long hedgers do not match up."); J. Nocera, "Easy Target, But Not The Right One," New York Times, June 28, 2008 at B1.

recommendations are included as Appendix A. For this hearing, the Committee has grouped the issues presented in the pending legislative proposals into six categories. FIA's thoughts on each area follow. We emphasize the foreign board of trade issue because it is the primary area of concern to the clearing firms that comprise our core membership.

## **FOREIGN BOARDS OF TRADE**

### **Background**

In 1982, Congress determined that futures contracts traded on an exchange "located outside the U.S." -- called a "foreign board of trade" -- would be excused from the requirement that futures contracts in the U.S. must be traded on a CFTC-approved exchange. That requirement remains the law today unless a statutory or regulatory exclusion or exemption is applicable. In 1982, Congress also specified that the CFTC could not directly regulate foreign boards of trade or their operations. For well over a decade, this provision was non-controversial and applied in a legally certain atmosphere: an exchange was considered to be "located" where its trading floor was located and U.S. customers accessed foreign boards of trade without incident.

In recent years, matching engines, trading terminals, servers and web access allowed any exchange anywhere in the world to access U.S. customers directly. Because issues were raised about whether these developments affected where an exchange was "located," the CFTC and its staff developed a no-action approach. Through the no-action process, the CFTC was able to condition the ability of a foreign board of trade to conduct business with firms and customers in the U.S. One important condition is the level of cooperation the CFTC could receive from a

foreign board of trade's foreign regulator, what the CEA defines as a "foreign futures authority." To date, the CFTC's web-site lists 20 of these no-action letters issued to foreign boards of trade.

As commodity markets have become more international in scope and electronic trade execution mechanisms have become predominant, U.S. and foreign exchanges have begun some level of direct competition. U.S. futures exchanges have attempted to engage in direct competition with certain foreign futures exchanges and foreign exchanges have attempted to engage in direct competition with certain U.S. exchanges. For example, in recent years the Chicago Board of Trade offered replicas of the German Bund, Bobl and Shatz futures contracts which trade successfully on EUREX, the German-Swiss Exchange. The New York Mercantile Exchange also trades a Brent Oil futures contract which is a cash-settled version of the same contract which first traded on what is now ICE Futures Europe. Competition is a two way street. ICE Futures Europe also has listed and trades a cash-settled clone of the bellwether WTI crude oil futures contract traded at NYMEX.

FIA strongly supports direct competition among trading facilities both within the U.S and globally. Competition leads to more liquidity, lower trading costs, tighter spreads, and more innovation. It does, however, complicate market surveillance. It is easier to know who is trading what futures contracts on one exchange, than on multiple exchanges. It is also easier for a single dominant designated contract market to discharge its statutory duty to prevent manipulation on its own market without having to worry about trading in the same commodity on the market of its competitor, the "challenger" exchange. The CFTC has determined that direct competition is important to promote and that the agency itself will bridge the gap in market surveillance among different exchanges trading the same product when these instances of direct competition arise. FIA has endorsed the CFTC's determination and actions to promote exchange competition.

Competition does promote innovation. For example, in response to the ICE Futures Europe decision to list a NYMEX-replica WTI crude oil futures contract and the immediate success ICE experienced through electronic trading in a contract that previously could only be traded on the NYMEX trading floor, NYMEX accelerated its efforts to allow electronic trading for its WTI contract. In response, the CFTC has taken a number of pro-active steps, with the cooperation of ICE's regulator, the UK Financial Services Authority, to make sure that the CFTC's market surveillance picture for both markets is clear and transparent. Again, FIA endorses the measures the CFTC has implemented and commends the agency for its leadership and initiative.

### **Current Proposals**

We understand that many want to codify in the CEA the CFTC's market surveillance protocols where a foreign-based and regulated exchange attempts to compete with a U.S. exchange for market share in a particular futures contract. FIA supports that goal. **Competition should not compromise market surveillance.** When two exchanges, no matter where located, compete for trading volume in the same product, the CFTC has heightened market surveillance responsibilities and its traditional market surveillance tools need to be adjusted to make sure that the CFTC has any and all data to prevent price manipulation or other major market disturbances.

As this Committee understands well, with most CEA proposals it is particularly important to target the legislative language to address the specific problem at issue and to avoid triggering legal and business consequences that would undermine the intended policy goal or have other unintended repercussions. In this instance, it is essential that any proposal adopted by the Committee not unintentionally harm the CFTC's efforts to enhance its surveillance

capabilities by pushing more market activity to less transparent venues where the trading data the CFTC may need would not be readily available.

FIA has reviewed the pending proposals and our list of concerns with each proposal is found at Appendix B to this testimony. Overall, **FIA fears that the proposals in the FBOT area that have been introduced to date would inadvertently harm both the CFTC's ability to prevent manipulation and the competitiveness of U.S. brokerage firms, while potentially leading to trade-war type retaliation from foreign governments against U.S. exchanges.**

Some of these proposals are drafted in a circular manner so that only foreign exchanges otherwise excused from CFTC oversight by statute would be subject to the heightened surveillance requirements. Other proposals enable FBOTs to evade the contemplated mandated CFTC regulation of FBOT self-regulatory operations by simply refusing to deal with U.S. traders and firms, while welcoming the business of any overseas affiliates of these same traders and firms. This has happened before in the context of security futures products and other trading instruments. In fact, some U.S. clearing firms have moved or may be compelled to move their operational and processing facilities out of the U.S. for just this reason. The results? No direct CFTC transparency for these FBOT trades, leading to increased manipulation risk and increased systemic financial risk on the clearing side, and a weakened business base for U.S. traders and firms (which creates a disincentive to even start such a business in the U.S.).

FIA also believes that any legislation in this area should be symmetrical because competition is global and U.S. exchanges do try to wrest market share from foreign boards of trade in various products, a competitive trend we hope will continue. Foreign futures authorities have as much interest in preventing price manipulation in their jurisdictions as the CFTC does here. None of the introduced proposals addresses this market and regulatory reality.

As mentioned earlier, FIA shares the policy goals of many of the introduced FBOT proposals: to enhance CFTC surveillance where warranted to deal with competition among foreign and U.S. exchanges in energy futures trading and to prevent market manipulation. To achieve those objectives, FIA recommends that the Committee consider the following type of provision:

When a foreign board of trade lists for trading an energy futures contract that is linked to the settlement price of an energy futures contract trading on a U.S. futures exchange (or vice versa) and when the CFTC (or its foreign regulatory counterpart) believes enhanced market surveillance is necessary or appropriate, then the CFTC and its foreign counterpart should immediately consult on, develop and implement heightened surveillance measures to prevent price manipulation and ensure transparent, coordinated market surveillance.

This approach will not only codify and strengthen the process and procedures the CFTC already has implemented with respect to ICE Futures Europe and its coordinated efforts with the FSA, it would build upon the CFTC leadership in this area to promote international consultation and coordinated regulatory responses. We would be leading the world in a common and important mission -- the prevention of price manipulation any time, anywhere. We would not be telling the world how that mission must be accomplished or that every CFTC or U.S. exchange requirement must be replicated in every instance. We would be leading, not dictating.

FIA also is very concerned that some legislative proposals in the FBOT area would operate to impose prohibitions on U.S. futures commission merchant firms that accept and execute customer orders on FBOTs. Unintentionally and inadvertently, these proposals would make U.S. firms liable if an FBOT fails to comply with U.S. law. They could also be read to allow customers to sue U.S. firms to void or rescind foreign futures contracts if the FBOT fails to comply with the CFTC-imposed regulatory conditions. **When executing and clearing orders**

**for U.S. or foreign customers, U.S. FCMs should not be guaranteeing the regulatory compliance of FBOTs.** Specific statutory safe harbors and exemptions are needed to prevent CFTC-registered professionals from bearing the legal risk of FBOT non-compliance. Otherwise investment banks and other clearing firms will simply and sensibly decide to run their futures brokerage and clearing businesses through overseas affiliates to avoid that potential liability.

The foreign board of trade issue is vitally important to the future commercial viability of the U.S. FCM community which comprises the core of the FIA's membership. We would be happy to consult with the Committee and its staff on specific legislative language to achieve the objectives of much of the FBOT legislation proposed to date without the adverse consequences outlined above.

#### **Swaps: Treating Energy Commodities Like Agricultural Commodities**

Under the Commodity Futures Modernization Act of 2000, Congress prescribed different levels of CFTC oversight and regulation for different trading systems, different market participants and different commodities. Generally, Congress determined that trading on multilateral trading facilities, where many market participants may execute trades with other market participants (so-called "many to many" markets), replicated the trading structure of traditional futures trading pits and should not be excused from CFTC regulation. Also trading among only Eligible Contract Participants, essentially well-capitalized, sophisticated or regulated entities, might not require full CFTC regulation and oversight because each ECP would be capable of protecting itself. And transactions in financial, energy and metals commodities did not implicate the same historical CEA regulatory concerns about market manipulation as did futures on agricultural commodities, which are the only commodities subject to CFTC-set

speculative limits for futures trading on an exchange. Building on those concepts, Congress extended legal certainty to non-agricultural commodity transactions among ECPs by excluding or exempting those transactions from the CEA when the transactions were not executed on a trading facility.<sup>3</sup>

Agricultural options and swaps transactions, however, may still be exempted from the CEA's exchange-trading requirement, among other regulatory provisions, under a CFTC exemption found in Part 35 of its Rulebook and adopted under Section 4(c) of the CEA, as enacted in 1992. Under the Part 35 rules, non-standardized and non-fungible derivatives transactions among Eligible Swap Participants (again, well-capitalized, sophisticated parties) are generally exempt from the CEA unless traded on a multilateral transaction execution facility or submitted to a futures-style clearing system. These otherwise exempt agricultural transactions are still subject to the CEA's anti-fraud and anti-manipulation prohibitions.

The CFMA exemptions and exclusions in the energy area represented an attempt statutorily to increase price transparency and remove systemic financial risk in over-the-counter energy transactions. And those provisions have worked as intended. ICE and other market innovators have developed methods of increasing price transparency for energy swaps in less than fully multilateral electronic trading systems. It is uncertain whether those swaps would be eligible for exemption under Part 35. What is certain is that none of those energy swaps could be subject to a futures-style clearing system unless the CFTC adopted a new exemption. Treating

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<sup>3</sup> This summary oversimplifies the web of CEA exclusions and exemptions enacted in 2000. But it captures the essence of CEA §§ 2(c), 2(d), 2(e), 2(g) and 2(h). Notably, parties engaged in exempt transactions in energy commodities under section 2(h) could still be subject to CFTC prosecution for energy price manipulation.

energy commodity swaps like agricultural commodity swaps therefore would likely diminish price transparency and increase financial risk for these transactions.

In the 2008 Farm Bill, Congress addressed the legitimate concern that exempt energy transactions under Section 2(h) that are traded electronically and develop into significant price discovery transactions should be regulated more like futures contracts than Congress envisioned in 2000. Once fully implemented by the CFTC, this reform will enhance price transparency and market oversight. Its valuable benefits will be lost, however, if energy commodities are treated in the same ways as agricultural commodities and removed from the transactions eligible for exemption under Section 2(h)(3) of the CEA. Like most quick fixes under the CEA, equating energy commodities with agricultural commodities will disserve the public interest. FIA would not recommend its adoption or the approval of any substantive amendments to CEA §§ 2(g) and 2(h). Instead, the reforms in the Farm Bill should be allowed to take full effect and monitored to determine whether any adjustment is warranted in the near future.

### **Resources for the CFTC**

FIA strongly supports the proposals for additional resources for the CFTC, including at least 100 new CFTC employees. Those numbers are commensurate with the CFTC's scope of responsibilities and ever expanding authority in a global and changing market place. The bulk of the CFTC's new resources we would expect to be used to hire attorneys in the Enforcement Division to investigate and root out any alleged price manipulations the CFTC staff may uncover. Manipulation should not be tolerated and enforcement actions for past misconduct are the best means to deter future misconduct.

## **Pension Funds and Index Trading**

FIA strongly opposes banning any collective investment vehicles, whether they are pension funds, mutual funds, commodity funds or hedge funds, from participating in futures markets. When the funds' professional trading managers determine it is in the best interests of the funds' investors or beneficiaries to diversify their portfolio by trading in futures markets, that new speculative capital and liquidity should not be shunned. The CFTC is wisely investigating to determine whether index traders or any one else has engaged in price manipulation. FIA has every confidence that the CFTC (along with staff from other, less directly interested, federal agencies) will analyze the right data and will make public its conclusions on or about September 15, 2008. FIA will be interested to evaluate the Commission's analysis under that accelerated time table. Until the facts are known and analyzed, however, FIA would urge all interested parties not to pre-judge the price effects of index trading, swap dealer net offsets in futures or pension fund activities.

## **Speculative Limits**

Some observers believe that swap dealers should not be considered to be hedgers when they enter into futures market transactions to offset the price risk of their swap transactions with non-physical commodity counterparties. To the extent the CFTC study will consider this issue, FIA would withhold final judgment. But it seems to make no difference from the perspective of the swap dealer whether its futures position is designed to manage a price risk incurred with a physical counterparty or a financial counterparty. Price risk is price risk. Swap dealers in energy commodities use futures to reduce their net market price risk on transactions with financial and physical counterparties. If a swap dealer entered into a long swap transaction in crude oil with a

notional amount equal to 10 futures contracts with a financial counterparty and then entered into a short swap transaction in crude oil with a notional amount equal to 5 futures contracts with a physical counterparty, the dealer could then go short 5 crude oil futures contracts on NYMEX to manage its net outstanding price risk. Some proposals would disallow treating the dealer's 5 short futures position as a hedge; instead those proposals would insist the dealer has a 5 short speculative position in futures, a result which distorts both the economic reality of the swap dealer's risk and any CFTC surveillance of that position. That approach also could make it more costly for the dealer to margin its futures position (a cost the dealer would likely pass along to its swaps counterparties).

The better way to handle this situation is to allow the CFTC as well as the NYMEX and other exchanges to establish position accountability standards and to look behind the positions when appropriate to see whether the swap dealers or other large traders are engaged in any transactions that would raise surveillance concerns, without worrying about the classification of a position as hedge or speculative. Current law and DCM core principles accomplish that kind of flexibility. Indeed, under NYMEX rules, the hedge vs. speculation classification only really matters for position limit purposes during the last three trading days in every contract when speculative position limits first become applicable.

## **Margin**

U.S. futures exchanges should set margins, not the U.S. government. Exchanges and their clearing entities set margins to balance credit risk considerations against other market interests. It is a delicate business judgment that goes to the heart of exchange operations and should be left to the exchanges. In the context of crude oil prices, there is no evidence that

NYMEX has abdicated its authority in any way in this area. To the contrary, from January 2, 2007 through July 3, 2008, NYMEX has increased its margin for WTI crude oil futures for non-member speculators by about 270% in absolute terms and about 50% when compared to the notional amount per contract.

## **Conclusion**

Record high gasoline prices are creating challenges and hardships in our national and international economy. If FIA believed that some reform to futures regulatory surveillance practices would reduce those challenges and hardships, we would not hesitate to recommend those reforms. But FIA is not aware of any proposed change to the CEA that is likely to result quickly, automatically and permanently in a decline in the price of crude oil. We are aware of statutory proposals that would substantially and adversely affect U.S. futures firms and markets, price transparency, systemic risk, and competition. These proposals threaten the viability of many services our member firms now provide to customers in the U.S. and overseas. Those proposals should not be adopted by this Committee and Congress.

FIA respectfully requests that the Committee continue to proceed with caution in considering the pending proposals. We look forward to working with the Committee and its staff to fashion meaningful, realistic and targeted legislation to enhance market surveillance for energy futures markets and to strengthen the CFTC's regulatory muscle over the ever changing dynamic of futures trading activities.

## APPENDIX A

### WHAT CONGRESS SHOULD DO

- Congress should call on the President to immediately send a request for emergency appropriations to allow the CFTC to increase oversight, improve the Commission's information technology, and hire at least 100 new full time employees.
- Congress should instruct the Commission to add at least 100 new full time employees in order to increase surveillance of the market, improve enforcement and otherwise carry out the purposes of the Act.
- Congress should require the CFTC to obtain all necessary market surveillance information to prevent market manipulation.
- Congress should require the CFTC to report to Congress regarding the effectiveness of its expanded information-sharing arrangement with the FSA, and the results of its review of the scope of commodity index trading in the futures market, and its recommendations for any changes to its authority or rules, including any modifications to the Commitment of Traders reports as necessary to provide increased transparency in energy derivative markets.
- Congress should instruct the Commission to undertake a comprehensive report, in conjunction with other futures and options regulators world-wide, relating to differences in regulatory regimes worldwide as well as the role of institutional investors, speculators and other participants in the markets.

## Appendix B

### Futures Industry Association -- Concerns Relating to Foreign Board of Trade (“FBOT”) Legislative Proposals

1. HR 6284 (Mattheson), HR 6334 (Etheridge), S2995 (Levin), S3044(Reid), S3129 (Levin), S3130 (Durbin) -- CFTC may grant § 4(a) relief only for FBOT with comparable regulation and willing to submit trading data to CFTC
  - (a) “Located outside.” Applies only to foreign boards of trade which, by definition, are located outside the U.S. and therefore do not need § 4(a) relief. Because FBOTs need no § 4(a) relief the provision is ineffective and self-defeating.
  - (b) “Cash-settled.” Applies only to FBOTs “with respect to an energy commodity that is physically delivered in the U.S.” FBOT contracts that are cash-settled would not be covered by the provision. ICE Futures Europe’s WTI futures contract is cash-settled and does not call for physical delivery of any energy commodity.<sup>1</sup>
  - (c) Attempts to impose direct CFTC regulation on FBOTs in a number of areas. In response and to avoid duplicative regulatory oversight, FBOTs are likely to close off foreign markets from U.S. market participants and firms. FBOTs will simply refuse to take orders from US firms and traders. FBOT business may not suffer; firms and traders will

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<sup>1</sup> HR 6349 (Marshall) is substantially similar to the six enumerated bills except it does not have the physical delivery limitation. It would apply if an FBOT’s energy contract refers to the price of a physically delivered energy contract traded on a US exchange and the contract contemplates a “primary physical delivery point” in the U.S. This formulation would allow CFTC regulation to apply to FBOT contracts that are cash-settled, although the concept of a primary US delivery point is not well established and may not be easy to apply in all circumstances. Other than cash-settlement, HR 6349 raises all of the same issues as the six other bills listed.

continue to trade on the FBOT, but will trade through their overseas affiliates.

- (d) If FBOTs are made subject to affirmative US statutory requirements, US FCM firms could be liable under § 4(a) for an FBOT's non-compliance because of the way § 4(a) is structured. FCMs should not be insuring FBOT compliance with US law.
  - (e) No coordination role provided for foreign futures authority with jurisdiction over the FBOT.
2. HR 6341 (Van Hollen) -- Disqualifies boards of trade from being considered to be foreign if they have US ties and trade SPDCs in energy.
- (a) Harms CFTC Surveillance Transparency. Any FBOT could avoid US jurisdiction by not affiliating with an entity in the US or not having any infrastructure in US. FBOTs could set up matching engines outside the US, with servers outside the US and no direct US presence. FBOTs would not need any CFTC relief. CFTC would lose all possible leverage in trying to obtain surveillance information.
  - (b) If CFTC determines an exchange with US ties trades a Significant Price Discovery Contract (a new statutory term designed to serve a very different purpose) in any energy commodity, then that contract becomes illegal to trade in the US unless the FBOT becomes a DCM. Making illegal a contract that others are using for price discovery -- theoretically world-wide -- will harm the price discovery process and may cause serious commercial harm in the energy markets.
  - (c) It is unclear how to apply the SPDC criteria from the Farm Bill to an international market. The SPDC criteria were developed to discern price discovery contracts in the U.S.,

not in overseas markets. Is the CFTC supposed to make a national or international SPDC determination?

- (d) Would encourage foreign exchanges to bar US traders and firms from participating in their markets. Congress may want US parties to participate in energy price discovery rather than leave price discovery just to parties in the Middle East and other parts of the world.
  - (e) Requires ICE Futures Europe to become a US designated contract market. Could spark trade-war style retaliation.
3. HR 6330 (Stupak) -- Makes illegal non-DCM energy futures if delivery point in US or “transacted” on a terminal in US.
- (a) Would not apply to cash-settled transactions on an FBOT.
  - (b) Exchanges now rely less on dedicated terminals for trading. Modern technology and web-access make trading easier to access from anywhere in the world. FBOT do not need to have terminals in the US. If FBOTs don’t have terminals in the US, the CEA doesn’t apply to those FBOTs’ contracts.
  - (c) Excuses an energy contract from coverage under the CEA unless it calls for delivery point in the US or is transacted on a US terminal. An FBOT could list a cash-settled energy contract and allow US traders access from web-sites in the US and not be subject to the CEA. May actually cut back on CFTC authority, making transparency and market surveillance harder to achieve.
  - (d) Misapprehends that CFTC FBOT no-actions have relied on Section 4(c) exemptions (which bill seeks to nullify absent public comment). No-actions are not 4(c) exemptions.
4. HR 6130 (Barton) -- Requires CFTC within 6 months to determine whether to adopt a rule regarding how the CFTC determines a

foreign futures authority regulates its exchanges and markets in a way comparable to the CFTC.

- (a) Developing regulatory standards for determining comparability in different regulatory structures may limit CFTC discretion. But providing notice to market participants and FBOTs of the factors the CFTC would take into account in making a comparability determination may not be problematic.
  - (b) May remove CFTC flexibility by requiring FBOTs to have certain specific regulatory tools to achieve comparability. Better approach would be to determine whether anti-manipulation protections are adequate and how well sharing of surveillance data on competing contracts could work.
5. HR 6279 (Chabot) -- Same as bills covered under Part I above, but adds that FBOT margin requirements must be comparable to US and “sufficient to reduce excessive speculation.”
- (a) DCMs in US have considerable flexibility in imposing margin, as they should. They operate under core principles subject to CFTC oversight.
  - (b) Under US law, margin is not generally designed to curb excessive speculation. Margin is largely a credit risk issue. FBOTs should not be held to a different, higher standard.
6. HR 6372 (Hill) -- No board of trade may be an FBOT if it has a US affiliate, trades a commodity other than an exempt commodity or trades a significant price discovery contract.
- (a) No “US affiliate” test artificially restricts cross-border exchange mergers with US entities. Why limit the commercial maneuverability of US trading facilities when foreign counterparts are not similarly restricted? Also allows board of trade a fairly painless way to evade U.S. law.

- (b) Energy and metals are exempt commodities. Trading in those kinds of commodities would not be affected by this bill. Trading in agricultural commodities and financial commodities (excluded commodities) like interest rates, currencies and equities would be affected. Not sure that was intent.
  - (c) SPDC determination in Farm Bill was not developed with foreign or global markets in mind. Not sure how well SPDC determination can be adapted to this context. Also SPDC is not self-executing; it requires an affirmative CFTC determination. Why would Congress want to make it illegal to trade a contract that businesses are relying on for significant price discovery.
7. S3122 (Cantwell) -- Makes into a DCM any trading facility that a) “operates 1 or more trading terminals” in US; b) trades contracts that serve a price discovery function for a commodity delivered in the US and c) is regulated by a foreign regulatory agency. Terminates existing exemptions from DCM registration.
- (a) FBOTs today operate under a CFTC-approved no-action process, not Section 4(c) exemptions.
  - (b) FBOTs do not need to operate “trading terminals” in the US. Web access is world-wide. Also servers that facilitate the pace of execution of US customer orders on FBOTs are not considered to be trading terminals. Servers are not trading terminals.
  - (c) Price discovery function is an undefined, new term. To the extent it is different than the “significant price discovery contract” definition from the 2008 Farm Bill, it is not clear why a new phrase is needed. To the extent it is the same as the Farm Bill formulation, it is not self-executing, adds administrative cost to CFTC regulation, and may not be

applicable to energy markets traded overseas. Also has the perverse consequence of penalizing a foreign exchange for developing an energy contract (Brent) which a US exchange later copies.