

COMMITTEE ON AGRICULTURE
SUBCOMMITTEE ON GENERAL FARM COMMODITIES
AND RISK MANAGEMENT

IMPLEMENTATION OF TITLE VII OF THE DODD-FRANK
WALL STREET REFORM AND CONSUMER PROTECTION ACT

ORAL STATEMENT OF JOHN M. DAMGARD, PRESIDENT

FUTURES INDUSTRY ASSOCIATION

FEBRUARY 15, 2011

Chairman Conaway, Ranking Member Boswell, members of the Subcommittee, I am John Damgard, president of the Futures Industry Association. On behalf of FIA, I want to thank you for the opportunity to appear before you today.

Since many members of the Subcommittee are new, I would like to take a minute to explain who we are. FIA is a principal spokesman for the commodity futures and options industry. FIA's regular membership is comprised of approximately 30 of the largest futures commission merchants or FCMs in the United States. Among FIA's associate members are representatives from virtually all other segments of the futures industry, both national and international. FIA estimates that its members effect more than eighty percent of all customer transactions executed on U.S. contract markets.

As the principal clearing members of the U.S. derivatives clearing organizations, our member firms play a critical role in the reduction of systemic risk in our financial system. Our member firms commit a substantial amount of our own capital to guarantee the futures and options transactions that our customers submit for clearing. We take justifiable pride that the U.S. futures markets operated extremely well throughout the financial crisis. No FCM failed and no customer lost money as a result of a failure of the futures regulatory system.

Today I would like to highlight four major concerns about the Dodd-Frank rulemaking process. First, some of the proposed rules have gone well beyond the intent of Congress. Given the intense pressure that we all face in bringing down the level of government spending, it would make more sense to focus on the regulatory requirements that are mandated by Congress, and set aside other regulatory initiatives for a future date.

Second, the rules have been published for comment in an order and at a pace that makes meaningful analysis and comment difficult, if not impossible. We encourage both Congress and the Commodity Futures Trading Commission to take the time necessary to fully analyze all the costs and benefits of the proposed rules and allow sufficient time for implementation.

Third, the costs of complying with Dodd-Frank will discourage participation in the markets and force certain firms out of the business. You have already heard similar concerns from many groups that represent the end-users of derivatives; I would only add that the potential costs could lead to a loss of competition among clearing firms and liquidity providers.

Fourth, I encourage Congress to consider the international dimensions of the rulemaking process. In particular, FIA believes that the Commission should use its exemptive authority to avoid duplicative and perhaps conflicting regulatory requirements for activities that take place outside the United States.

Let me now turn to the rulemaking process. Our member firms believe that the CFTC should implement the reforms envisioned by the Dodd-Frank Act in a deliberate and measured way. We recognize that the Commodity Futures Trading Commission and its staff are working night and day to comply with the very tight timeframes set out in the Dodd-Frank Act. We also appreciate that the Commission has repeatedly invited affected parties to provide input into the rulemaking process. And we have responded. As of today, we have filed comment letters on 17 proposed rulemakings, we have participated in three CFTC roundtables and we have met with CFTC staff on many occasions to discuss matters of particular concern.

I regret to say, however, that providing meaningful analysis and comment is extraordinarily difficult due to the tremendous number of rules that have been proposed in such a short period of time. To give you one example, the Commission has proposed a myriad of rules that taken together would completely overhaul the

recordkeeping and reporting requirements for clearing firms, exchanges and clearing organizations. These proposals include: (i) the advance notice of proposed rulemaking regarding the protection of cleared swaps customers before and after commodity broker bankruptcies; (ii) core principles and other requirements for designated contract markets; (iii) risk management requirements for derivatives clearing organizations; (iv) information management requirements for derivatives clearing organizations; (v) position limits for derivatives; (vi) core principles and other requirements for swap execution facilities; and (vii) swap data recordkeeping and reporting requirements. These rulemakings cannot be considered in isolation. All of the pending recordkeeping and reporting requirements must be evaluated collectively, not individually. Otherwise it is impossible to determine whether the pending rules are complementary or conflicting. Nor is it possible to calculate the financial and operational burdens these proposals will impose on the industry and its customers.

FIA also believes that some of the Commission's proposed rules go well beyond Congressional intent. One example is the rulemaking on governance and ownership of clearing organizations, contract markets and swap execution facilities. Although the House version of the financial reform legislation contained provisions that set specific ownership limits for these entities, those provisions were removed when the legislation reached the conference committee, and the Dodd-Frank Act in its final form simply authorizes the Commission to adopt rules with respect to ownership and governance. Furthermore, the Act states that any such rules should be adopted only after the Commission first determines that such rules are necessary or appropriate to improve the governance, mitigate systemic risk, promote competition, or mitigate conflicts of interest. Although the Commission has not made the required determination, the Commission nonetheless has proposed specific rules on governance and ownership that effectively would implement the very provisions that were removed in conference.

Let me now turn to the third of our major concerns. The Commission has acknowledged that its proposed rules will increase the costs of effecting transactions in swaps, but it has stated that the benefits outweigh any additional costs that may be imposed on customers. We believe the Commission may well have underestimated these additional costs. For example, in the proposed OCR rule, the CFTC estimated the cost of compliance of the reporting entity and did not estimate the cost to the FCM where most of the data would originate. FIA estimates that the median firm would face total costs of \$18.8 million per firm to implement and maintain the data.

Moreover, the additional costs will not be imposed solely on swap market participants. They are certain to affect participants in the exchange-traded markets as well. FCMs will have little choice but to pass these costs on to their customers. Furthermore, the potential increase in costs could have the counterproductive effect of reducing competition by causing existing FCMs to withdraw from

registration and discouraging other firms from entering the FCM business.

This past year, we formed a new division of the FIA comprised of firms that trade their own capital and provide an increasingly important source of liquidity in a wide variety of exchange-traded markets. Some members of the FIA PTG may choose to provide liquidity to the cleared swaps markets that are expected to emerge after Dodd-Frank takes effect. Their willingness and ability to do so will depend, however, on a number of factors, not the least of which will be the costs of complying with the requirements of Dodd-Frank.

It has been suggested that the Commission should move forward with adopting final rules within the Dodd-Frank Act timeframes, but set effective dates that will afford participants sufficient time to come into compliance. Although this is certainly one alternative, we believe the better choice is to delay adopting final rules until all affected participants have a reasonable opportunity to fully analyze

and understand the scope of the complex and far-reaching regulatory regime that the Commission has proposed.

It should be noted that the rulemaking process that we are discussing today does not take place in a vacuum. The European Union is developing a comprehensive regulatory regime for swaps, including clearing through EU clearing organizations. Chairman Gensler has taken great pains to consult with his European colleagues on the rulemaking process. Nevertheless, there is no escaping the fact that the process on this side of the Atlantic is proceeding more rapidly than on that side of the Atlantic. That is all the more reason to proceed carefully as we move ahead on these rulemaking and avoid locking ourselves into conflicting regulations. Furthermore, it is our view that the Commission should be encouraged to use its exemptive authority to assure that market participants and transactions taking place outside the U.S. are not subject to duplicative or conflicting regulatory requirements.

In closing, I want to note that we were pleased that Chairman Gensler has indicated that he intends to rely more heavily on the National Futures Association. Self-regulation has worked extremely well in the futures markets, and we see no reason why the success of these programs cannot be transferred to the swaps markets. Importantly, NFA is funded entirely by futures market participants, thereby relieving additional strain on the federal budget.

We urge the Subcommittee to take whatever action it deems appropriate to encourage the Commission to shift regulatory obligations to NFA and, through NFA, to the other industry self-regulatory organizations. As discussed above, for example, the Commission could delegate to NFA the responsibility to adopt rules for chief compliance officers.

Thank you again for the opportunity to appear before you today. I would be happy to answer any questions you may have.

