



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

December 18, 2003

Ms. Jean A. Webb
Secretary
U.S. Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

Dear Ms. Webb:

Pursuant to section 2(a)(9)(B)(ii) of the Commodity Exchange Act, 7 U.S.C. § 2(a)(9)(B)(ii), the Commodity Futures Trading Commission has solicited the Board's comments on the application for contract market designation by U.S. Futures Exchange, L.L.C. The Act requires the Commission to deliver to the Board of Governors and the Department of the Treasury for their comment a copy of any application by a board of trade for designation or registration as a contract market or derivatives transaction execution facility involving transactions for future delivery of any security issued or guaranteed by the United States or any agency thereof. U.S. Futures Exchange has indicated that it intends to trade products involving such securities. The Commission delivered a copy of the application to the Board by letter dated November 5, 2003, and solicited the Board's comments on the application.

The Board believes that trading of derivative instruments on contract markets and over the counter are important complements to the cash-market trading of Treasury securities. Derivative and cash markets are linked through the trading and hedging of market participants. Expanded venues for the trading of derivatives could offer opportunities for traders and investors more readily to assume and hedge their positions in Treasuries, thereby contributing to market liquidity. The Board is supportive of steps that have the potential to improve liquidity in Treasury markets. Treasury securities also serve as important hedging vehicles in corporate bond and mortgage markets, and incremental improvements in the liquidity of Treasury securities could have benefits in these markets, too.

As described in the application, U.S. Futures Exchange is an indirect subsidiary of a non-U.S. firm, Eurex Frankfurt A.G. Questions have been raised as to the appropriateness of the ownership of U.S. Futures Exchange for a contract market operating in the United States. The Board believes that competition, including competition from non-U.S. firms, serves our overall economy and our financial markets well. Competition enhances efficiency and fosters innovation.

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The Commission has indicated in congressional testimony that it is committed to providing a level regulatory playing field and that U.S. Futures Exchange's application will be evaluated against the same core principles for designation as are applied to other contract markets. Concerns about potential adverse effects of U.S. Futures Exchange's foreign ownership can be addressed in terms of any implications for the exchange's compliance with those core principles.

The Board believes that the process the Commission has described is appropriate. In many segments of our economy and financial markets, competition has been enhanced by non-U.S. firms establishing a direct presence in the United States. The process for contract market designation laid out in the Commodity Exchange Act and implemented by the Commission provides a mechanism to address any concerns regarding foreign ownership; such concerns do not require erecting barriers to foreign entry. In this way, U.S. financial markets can benefit from the competition afforded by entry of new contract markets, including entry by markets owned by non-U.S. firms.

Very truly yours,

A handwritten signature in cursive script, appearing to read "Jennifer J. Johnson", with a long horizontal flourish extending to the right.

Jennifer J. Johnson
Secretary of the Board