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COMMODITY FUTURES TRADING COMMISSION

GLOBAL MARKETS ADVISORY COMMITTEE MEETING

Washington, D.C.

Wednesday, May 21, 2014

1 PARTICIPANTS:

2 For CFTC:

3 RIVA SPEAR ADRIANCE  
4 Senior Special Counsel, Division of Market  
5 Oversight, U.S. Commodity Futures Trading  
6 Commission

7 DAVID BAILEY  
8 Head of Department, Market Infrastructure & Policy  
9 U.K. Financial Conduct Authority

10 PHYLLIS DIETZ  
11 Deputy Director for Clearing Policy Division of  
12 Clearing and Risk, U.S. Commodity Futures Trading  
13 Commission

14 VINCENT MCGONAGLE  
15 Director, Division of Market Oversight, U.S.  
16 Commodity Futures Trading Commission

17 JUN MIZUGUCHI  
18 Assistant Commissioner for International Affairs  
19 Japan Financial Services Agency

20 SCOTT D. O'MALIA  
21 Commissioner

22 TED SERAFINI  
23 GMAC Designated Federal Official

24 DAVID VAN WAGNER  
25 Chief Counsel, Division of Market Oversight, U.S.  
26 Commodity Futures Trading Commission

27 BOB WASSERMAN  
28 Division of Clearing and Risk, CFTC

29 MARK P. WETJEN  
30 Acting Chairman

31

1 PARTICIPANTS:

2 Other Participants:

3 CHRIS ALLEN, Barclays

4 SAMARA COHEN, Goldman Sachs

5 ADAM COOPER, Citadel

6 PAUL HAMILL, UBS

7 GEORGE HARRINGTON, Bloomberg

8 ROBERT KLIEN, Citigroup Global Markets, Inc.

9 CLINTON LIVELY, RBC

10 RAJ MAHAJAN, Allston Holdings

11 JOHN NIXON, ICAP

12 STEPHEN O'CONNOR, ISDA

13 EMILY PARSONS, MIT

14 EMILY PORTNEY, JP Morgan Chase

15 MUTHUKRISHNAN RAMASWAMI, Singapore Exchange

16 DAVID ROTH, National Futures Association

17 YASUSHI TAKAYAMA, Nomura Securities International

18 KIM TAYLOR, CME Group

19 WALLACE TURBEVILLE, Demos

20 SUPURNA VEDBRAT, BlackRock

21 DAVID WEISBROD, LCH Clearnet, LLC

22 \* \* \* \* \*

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

2 (10:00 a.m.)

3 MR. SERAFINI: Good morning everyone.

4 As the GMAC designated federal officer and  
5 temporary chair of the committee, it is my  
6 pleasure to call the 16th Meeting of the Global  
7 Markets Advisory Committee to order.

8 Thanks everyone for being here today.  
9 We really appreciate it. I will turn it over to  
10 the acting chairman and sponsor of the GMAC, Mark  
11 Wetjen, for opening remarks.

12 CHAIRMAN WETJEN: Thanks, Ted. Thanks,  
13 everyone, especially the members for being here  
14 today. We've got a couple of newcomers. Welcome.  
15 And a special welcome to our two panelists from  
16 abroad, David Bailey and Jun Mizuguchi. We really  
17 appreciate you two taking the time to come all  
18 this way and help us work through some of these  
19 issues related to the two topics today, the first  
20 being a possible regime for foreign-located  
21 clearinghouses or CCPs. This is something that  
22 the staff has been actively working on now for a

1 number of months. And has come very, very close  
2 to providing a final recommendation to the  
3 Commission for our consideration. And so we're  
4 hoping to talk through some of the issues embedded  
5 in the proposal today just to make sure that we  
6 have a full understanding of possible consequences  
7 and technical things we need to be aware of.

8           And then the second topic is a regime  
9 for foreign- based swap trading platforms. And  
10 this is something that we've already done some  
11 work on at the Commission earlier this year. We  
12 had relief for London-based platforms, and  
13 (inaudible) David Bailey who is very critical in  
14 developing that proposal. It contained a  
15 considerable amount of input from the FCA, and so  
16 we want to follow on that effort with a more  
17 fulsome rulemaking, a more comprehensive  
18 rulemaking in terms of how we should recognize  
19 again trading venues overseas.

20           So a couple of very important topics.  
21 They're important to the overall harmonization  
22 efforts of the agency, as well as the

1 harmonization efforts of the other regulators,  
2 including our friends in Japan and Great Britain.

3 So with that, again, welcome, and I'll  
4 turn it over to Scott O'Malia for his opening  
5 remarks.

6 COMMISSIONER O'MALIA: Thank you, Mr.  
7 Chairman. Thank you for calling this meeting to  
8 discuss the importance of mutual recognition.  
9 Under the principles of international comity,  
10 markets and market structure are beginning to  
11 evolve in response to the varying regulatory  
12 tracks that different jurisdictions are taking in  
13 their approach to implementing the G20 OTC  
14 derivatives reforms. So in order to avoid shifts  
15 in the global swaps market business as a result of  
16 the regulatory differences that could impair  
17 liquidity and access, it is critically important  
18 that international regulators come together in  
19 events and forums like this to harmonize swaps,  
20 data reporting, exchange trading, and counterparty  
21 clearing before market fragmentation and  
22 contraction of liquidity hardens and becomes

1 permanent.

2           While it is interesting to think about  
3 the possibilities afforded by exempt DCOs and  
4 exempt SEFs, I believe we need to focus more  
5 closely on resolving the regulatory differences  
6 between our jurisdictions to enable full  
7 substituted compliance or equivalents based on  
8 mutual recognition under the principles of  
9 international comity. For example, in comparing a  
10 SEF, qualified multilateral trading facility, or  
11 possibly an exempt SEF proposal, it is not clear  
12 how any of these will provide a solution that is  
13 superior to mutual recognition of the existing SEF  
14 and MTF market structures in the U.S. and Europe.  
15 Using the QMTF framework as an example, I fear we  
16 are proceeding down a regulatory path that  
17 highlights our differences and does not recognize  
18 our commonalities. I will ask our panelists and  
19 the GMAC representatives to describe what they  
20 believe is the ideal regulatory path regarding  
21 mutual recognition of U.S. and E.U. exchange  
22 trading rules.

1                   With regard to exempt DCOs, I believe  
2                   that the Commission needs to think carefully  
3                   before proceeding on such a proposal. This is  
4                   especially important until we at least have an  
5                   understanding of the mutual recognition regimes  
6                   under which jurisdictions will recognize CCPs that  
7                   meet the standards set forth in the agreed upon  
8                   principles for financial market infrastructures,  
9                   particularly since so many jurisdictions have  
10                  already adopted the standards. Given that the  
11                  timeframe to mend a clearing under EMIR is  
12                  looming, international regulators need to make  
13                  progress in this front to avoid further market  
14                  fragmentation.

15                  Finally, let me make my plug as I do  
16                  frequently for harmonization of swaps data  
17                  reporting. Right now, the U.S. and the E.U. are  
18                  working separately to resolve data quality issues  
19                  that we could use the opportunity to work  
20                  together, and so far we are not making the  
21                  necessary steps to set the groundwork for an  
22                  agreement that would allow our jurisdictions to

1 share this critical swaps data. It is my sincere  
2 hope that negotiations will not only begin  
3 immediately, but that our jurisdictions will  
4 simultaneously engage in harmonization efforts  
5 that will allow us to access and share high  
6 quality and at low cost the data held by the swap  
7 data repositories.

8 In light of the discussion today, I am  
9 reminded of the path forward document agreed to in  
10 July 2013, and I believe we need to return to the  
11 spirit of cooperation embodied in that document  
12 before we undertake new and potentially confusing  
13 exempt regulatory structures. I certainly  
14 appreciate the work of the staff, both as  
15 witnesses and our chairman designate federal  
16 officer, Ted Serafini for his efforts to organize  
17 this, and I certainly appreciate all of the GMAC  
18 members for attending, and certainly, our  
19 witnesses who have come a long way and taken time  
20 out of your schedules to participate in this. So  
21 thank you very much for your participation today.

22 CHAIRMAN WETJEN: Thanks, Scott. Just

1 one quick point. I think I agree with  
2 Commissioner O'Malia, we need to come to a mutual  
3 recognition approach. Indeed, I think that's what  
4 contemplated here by these staff recommendations  
5 on these two rulemakings. The end result of that  
6 would be some recognition by the CFTC, and in  
7 return, the DCO or the SEF, whatever the case  
8 might be, would not have to fully register as a  
9 SEF or a DCO under our rulemaking.

10 So I agree we need to continue with this  
11 mutual recognition approach. We've started that  
12 last year with a number of different initiatives,  
13 including our substituted compliance  
14 determinations from late last year, as well as the  
15 more recent actions this year. So I think we all  
16 agree that's the appropriate way to approach these  
17 harmonization issues, and there's a lot of work  
18 left before us, and we look forward to the  
19 panelists today to help us through that. Thanks.

20 MR. SERAFINI: I know you guys are pros,  
21 but quick technology reminder. If you want to  
22 talk, you've got to press the button. Also, when

1       you're done talking, please turn the microphone  
2       off because only a limited number can be on at a  
3       certain time. And remember to keep your mobile  
4       devices away from the microphone because it might  
5       interfere with the sound quality.

6                       With that, Mark, would you like to  
7       introduce the speakers?

8                       CHAIRMAN WETJEN: Yeah. Again, thank  
9       you to June and David for being with us today. We  
10      also, for this panel, have Phyllis Dietz, who is  
11      with our Division of Clearing and Risk. And I  
12      turn over the panelists.

13                      MS. DIETZ: Thank you, and good morning.  
14      I'm Phyllis Dietz, and I head the Clearing Policy  
15      Branch in the Division of Clearing and Risk, and  
16      my group is responsible for DCO applications and  
17      has taken the lead on the DCO exemption proposed  
18      rulemaking.

19                      I have a distinct advantage over nearly  
20      everyone in this room today because I have  
21      actually seen the most current draft of the  
22      proposed rulemaking and you have not. So, with

1 that in mind, what I would like to do is to go  
2 over with you some of the key points of the  
3 current draft. It is still a staff draft. It is  
4 fairly well developed, but the good news is that  
5 this actually ends up being a fortuitous event  
6 because we all have the opportunity to get some  
7 pre- comments before any public comment period on  
8 a published document. The discussion I'm going to  
9 give, the overview, again, based on the current  
10 document, it has not been approved by the  
11 Commission yet. It is not on its way to the  
12 Federal Register, and it is subject to change. So  
13 I would invite you to provide any and all  
14 comments, ask questions. One of my goals for  
15 today is to listen and to take into account as we  
16 move forward with this process.

17 And what I'd like to do is start with  
18 the exemption provision in the Commodity Exchange  
19 Act. And you may be familiar with this, but let  
20 me just review it for you.

21 The Commission is authorized under  
22 Section 5B(H) of the CEA to exempt, conditionally

1 or unconditionally, a DCO from registration for  
2 the clearing of swaps. So it's not for futures,  
3 it's for swaps. If the Commission determines that  
4 the DCO is subject to -- and here's the important  
5 phrase -- comparable comprehensive supervision and  
6 regulation by the SEC, which we're not dealing  
7 with in this rulemaking, or the appropriate  
8 government authorities in the home country of the  
9 clearing organization. So such conditions may  
10 include -- and this is explicit in the statute --  
11 so it may include -- doesn't have to, but it may  
12 -- but that's always an invitation -- may include  
13 requiring the DCO to be available for inspection  
14 by the Commission and make available all  
15 information requested by the Commission.

16           So this is the -- this sets up the  
17 framework for what would be the exempt DCO  
18 regulation. The purpose of the regulation is to  
19 set forth standards and procedures that would  
20 apply to all DCOs interested in becoming exempt.  
21 There would also be at the conclusion of the  
22 application process, as with the conclusion of the

1 DCO application process, an order issued by the  
2 Commission so that there would be an order of  
3 exemption which could, depending on the facts and  
4 circumstances, include additional conditions, but  
5 at this point we have not really given any thought  
6 to what those conditions might be. They would be  
7 tailored to the individual exempt DCO. So the  
8 conditions that I'm going to talk about here today  
9 are ones that would apply to any exempt DCO.

10 So just to give you the highest level  
11 overview, the way the proposal is organized at  
12 this point, there are three basic components.  
13 There are eligibility requirements which will, as  
14 I'm sure is no surprise, focus on the CPSS-IOSCO  
15 principles for financial market infrastructures.  
16 There will be conditions which include certain  
17 reporting requirements. And then the last part is  
18 procedures which are going to outline the  
19 exemption application process, very similar to the  
20 registration process, and then a process for  
21 termination of an exemption, either at the  
22 initiation of the Commission because the

1 clearinghouse perhaps is no longer eligible, or at  
2 the initiation of the clearinghouse because of a  
3 change in business, or perhaps they're going to  
4 register as a DCO.

5           The proposal as it stands now will also  
6 include a proposal for certain conforming  
7 amendments for part 48, which is registered FBOTs  
8 to update it based on the PFMIIs and exempt DCOs.  
9 Amendments to part 50 along the same lines,  
10 technical conforming amendments, and then it will  
11 also include a series of questions about part 1  
12 and part 23 relating to obligations of swap  
13 dealers and MSPs. But those are matters that are  
14 related to the exemption, and today we're going to  
15 focus on the exemption draft.

16           Eligibility requirements, we go back to  
17 the statutory standard. Comparable comprehensive  
18 supervision and regulation by the home country  
19 regulator. So the emphasis is on the legal and  
20 supervisory framework, not per se what the  
21 clearing organization does. But, of course,  
22 implicit in that is that the clearing organization

1 will be held to and will comply with the  
2 regulatory and statutory framework in the home  
3 country.

4           So the first requirement -- and the  
5 eligibility requirement are really pretty compact.  
6 The clearing organization has to be organized in a  
7 jurisdiction where the home country regulator  
8 applies legal requirements consistent with the  
9 PFMIs. The clearing organization itself observes  
10 the PFMIs and is in good regulatory standing in  
11 its home country, and the home country regulator  
12 will provide a written representation as to good  
13 regulatory standing.

14           Now, that concept has been used with  
15 respect to foreign boards of trade and their  
16 clearing organizations. We actually propose a  
17 definition of what is good regulatory standing,  
18 and we can -- I think it speaks for itself, but we  
19 can, if you want, we'll flag that. We can go back  
20 to that. But I'm just going to proceed. So it's  
21 PFMI observance, good regulatory standing, and  
22 then the clearing organization completes the

1 application form which is primarily the submission  
2 of the PFMI disclosure framework.

3 Another requirement for eligibility, and  
4 this really isn't within the control of the  
5 clearing organization but it's very important to  
6 us, and that is that there is a memorandum of  
7 understanding or similar arrangement between the  
8 CFTC and the home country regulator because even  
9 though the clearing organization is going to be  
10 exempt, we still have an interest in the  
11 activities of the U.S. persons clearing through  
12 that clearing organization and the swaps that are  
13 being cleared. So it's very important that we  
14 still have a MOU. We always have that when there  
15 is a DCO that is registered, and even more  
16 important, where we don't have a full window into  
17 the operations of the DCO. So those are the  
18 eligibility requirements.

19 Then there are conditions, and that's  
20 what a lot of people have been talking about and  
21 are interested in. So let me go through that  
22 quickly. Some are of greater complexity than

1 others. Some people care more about than others,  
2 but let's go through all of them.

3 As is no surprise, and I think most  
4 people, you've been hearing speeches, you've been  
5 reading things, having conversations, there will  
6 be a limitation as it is currently drafted that  
7 there will be no customer clearing. That means  
8 proprietary clearing as we define it, U.S.  
9 persons, and I'll just paraphrase for you, U.S.  
10 clearing members can clear for themselves and for  
11 affiliates anyone that would be listed within our  
12 definition of proprietary account. A non-U.S.  
13 Clearing member can clear for a U.S. affiliate.  
14 And then an FCM, just to clarify, a registered  
15 FCM, as long as it is clearing proprietary  
16 positions only, could also be included.

17 By way of clarification, we are aware of  
18 the fact that we define proprietary and customer  
19 differently. Perhaps in some other foreign  
20 jurisdictions were are going to apply our  
21 definition, and we specifically refer to the  
22 proprietary account definition, so that even if an

1 affiliate were a "customer" in the foreign  
2 jurisdiction, as long as it is within our  
3 definition of proprietary, it is proprietary.

4 Second condition would be economic  
5 equivalency and nondiscriminatory clearing. It's  
6 the same provision. It's sometimes referred to as  
7 open access. It codifies CEA section 2(h)(1)(B),  
8 but for easy reference it's actually incorporated  
9 into our regulation for registered DCOs 39.12 B2  
10 and B3. So you can read that. It's the same  
11 provision.

12 Then, some administrative matters. The  
13 DCO has to consent to jurisdiction in the U.S. and  
14 designate an agent for service of process. That's  
15 routine. They have to comply with and be able to  
16 demonstrate compliance with all the requirements  
17 that were going to apply to them. They have to  
18 make documents, books, records, and reports  
19 related to their operation as an exempt DCO. So  
20 that is constrained, open to inspection by the  
21 CFTC. And I would just parenthetically add, one  
22 of the goals for the staff in discussing and

1 discussing again and discussing again potential  
2 reporting requirements and other conditions is  
3 what is it that we really have a strong  
4 supervisory interest in and what is it that we're  
5 just going to have to let go. And so with each of  
6 these conditions, a lot of thought has gone into a  
7 determination, and there actually were any number  
8 of conditions that we needed up not applying  
9 because we thought, you know, it's either we're  
10 not going to use the information or is it really  
11 necessary? And can this be handled by the home  
12 country regulator? So just to give you a little  
13 insight into the thought process behind some of  
14 these requirements.

15           Okay. So now digression over. On an  
16 annual basis, we would like a recertification by  
17 the clearing organization that it complies with  
18 the PFMIs, and likewise, from the foreign home  
19 country regulator that the clearing organization  
20 remains in material compliance.

21           There are then going to be some  
22 reporting requirements which actually was the area

1 where there was the greatest discussion about what  
2 do we really need and what don't we need. There  
3 are general reporting requirements, such as when  
4 the Commission asks for information you provide  
5 it. There are daily reporting requirements that  
6 we believe are important for our continuing risk  
7 surveillance of U.S. Clearing members and their  
8 affiliates, as well as swaps markets in general so  
9 that on a daily basis we would want reporting of  
10 initial margin requirements and initial margin on  
11 deposit for U.S. persons with respect to swaps,  
12 and the same for variation payments, U.S. persons  
13 with respect to swaps.

14 Quarterly activity reports. These would  
15 be following fiscal quarters. Information as to  
16 U.S. business and what's going on in the  
17 marketplace. So, the quarterly reports would  
18 include aggregate clearing volume of U.S. Persons  
19 during the fiscal quarter, again related to swaps.  
20 The average open interest of U.S. persons. Again,  
21 related to swaps. And then a list of U.S. persons  
22 and FCMs that are either clearing members or

1 affiliates of a clearing member with respect to  
2 the clearing of swaps. And that would actually be  
3 one piece of information that probably isn't going  
4 to change much.

5           Then there would be event-specific  
6 reports. And I would add for those of you who are  
7 familiar with the part 39 reporting requirements,  
8 we're proceeding along the same legal construct,  
9 so there's daily, quarterly, annual, and then  
10 event-specific. We have many event-specific  
11 reports that are required of registered DCOs. We  
12 have significantly paired down that list only to  
13 those that we really feel are important and that  
14 are closely related to our continuing interest in  
15 the activities of the exempt DCO. It would be  
16 things like change in the home country regulatory  
17 regime that are going to be material, an  
18 assessment of the exempt DCOs or home country  
19 regulators' compliance with PFMI's or examination  
20 reports. If those become available to the exempt  
21 DCO, we would want to see copies of those. Any  
22 change with respect to the exempt DCOs licensure

1 or registration, if they've been deregistered.  
2 Any default, and this goes to the risk  
3 surveillance part. Any default by a U.S. person  
4 or an FCM, or a notice of any disciplinary action  
5 that's taken against a U.S. person or an FCM.

6 There would also be swap data reporting  
7 requirements. And these requirements, I'll just  
8 refer you to some of our recent no action letters  
9 because those outline part 45 swap data reporting  
10 requirements. So we envision something along  
11 those lines.

12 In terms of procedure, as I mentioned,  
13 there will be an application form. It's not very  
14 long. The primary focus is on the disclosure  
15 framework. The application is submitted. It's  
16 reviewed. And certain parts of it will be made  
17 public. And the Commission, there's no timeframe  
18 for issuing an order. But it is our hope that  
19 because of the abbreviated application process,  
20 the timeframe would be abbreviated as well.

21 There are also provisions for  
22 termination, either at the initiation of the

1 Commission or at the initiation of the clearing  
2 organization, and this is akin to the registered  
3 DCO's ability to vacate its registration or the  
4 Commission's ability to terminate a registration  
5 of a registered DCO.

6 So I think that hits on the highlights  
7 of what is the current proposal, again, subject to  
8 change. We have tried to think of everything.  
9 The references I made earlier to part 48, part 50,  
10 we're trying to think of any other provisions of  
11 our regulations that might be impacted by it, so I  
12 would welcome any thoughts that other people have,  
13 either not necessarily today but as part of a  
14 future formal comment period to let us know if  
15 there's anything that we haven't thought of. I  
16 think we've got the kitchen sink here.

17 So with that, rather than taking  
18 questions right now, perhaps I'll just move on to  
19 our next panelist, if that's okay.

20 CHAIRMAN WETJEN: Phyllis, let me just  
21 add a couple other points if I could.

22 The other -- a couple of other key

1       considerations the Commission will have to take  
2       into account include general international comity  
3       principles, which is not something specifically  
4       mandated by the Commodity Exchange Act, but  
5       nonetheless, something that the Commission I think  
6       is cognizant of. I know that's something that  
7       Commissioner O'Malia thinks about quite a bit as  
8       well. And then the other thing is that the  
9       Commodity Exchange Act itself does require that we  
10      consider competitiveness impacts of our  
11      policymaking. That's something specifically  
12      mentioned in the statute itself, and so I think  
13      that's another thing that we need to understand  
14      and appreciate whenever we make policy, but it  
15      seems especially true in this instance as well as  
16      in the case of a regime for offshore trading  
17      platforms. So I just want to add those two quick  
18      points.

19                   MR. BAILEY: Okay. Good morning,  
20      everyone. And thank you very much to the acting  
21      chairman, chairman of the event and commissioner  
22      for inviting the FCA to participate in what

1       promise to be very important discussions with  
2       respect to overseas DCOs and SEFs.

3               Before tackling the important questions  
4       at hand, I'd just like to get on record the  
5       mandate of my organization just so everyone is  
6       clear of that, the UKFCA. From the UK  
7       perspective, we are the market's regulator. With  
8       respect to infrastructure, we are responsible for  
9       the supervision of trading venues, but not  
10       clearinghouses, which fall within the reign of my  
11       colleagues at the Bank of England. However, from  
12       an FCA perspective, we do have a very keen  
13       interest in clearing-related conduct issues. And  
14       in preparing my remarks today, I've collaborated  
15       very closely with my colleagues at the Bank of  
16       England.

17               So turning to the topic at hand, I  
18       thought the two areas I'd briefly like to cover at  
19       a relatively high level, firstly, I think it's  
20       very important we don't lose sight of why we need  
21       an exempt DCO or overseas regime for  
22       clearinghouses, both from the U.S. perspective,

1 but importantly other jurisdictions as well. And  
2 secondly, I'd just like to give some brief views  
3 on how we think that regime should work which will  
4 respond to some of the questions that FTC has  
5 quite rightly put on the table for us to discuss  
6 today.

7           So on the first point, I won't give a  
8 long reminder to the Committee of the important  
9 role that derivatives markets play within the  
10 broader global economy, but I would focus on the  
11 fact that over 50 percent of that trading takes  
12 place on a cross-border basis. And therefore, for  
13 that trading, we can't retreat behind national  
14 boundaries, otherwise, business is not going to  
15 get done, risk is not going to get hedged.  
16 Effective cross-border access for and to  
17 clearinghouses is therefore an essential component  
18 of the regulatory architecture that we put in  
19 place.

20           We need to find a way in which firms can  
21 interact across borders. We recognize there are  
22 risks associated with that. We recognize that

1 financial risk can move quickly through the  
2 markets and it can flow across borders, and  
3 therefore, regulators have a real and legitimate  
4 interest in business done outside of their direct  
5 jurisdiction. So we need to find solutions which  
6 meet the G20 mandate from 2009. We need to make  
7 sure that systemic risk is managed effectively and  
8 that markets are transparent with the appropriate  
9 level of transparency both to regulators and to  
10 the market as a whole.

11 But importantly, that has to be a shared  
12 endeavor. My organization, I'm sure like the CFTC  
13 and the Japanese FSA, we neither have the mandate,  
14 nor do we have the desire or even the resources to  
15 oversee the entire global derivatives market on  
16 our own. We, therefore, need to collaborate to do  
17 so in an effective manner.

18 The FSB has long warned about the risks  
19 of regulatory overlaps, of conflicts and gaps  
20 between our respective rules, especially if  
21 different regulators insist their rules apply to  
22 the same firms or the same transactions. These

1 aren't speculative issues. They're actually live  
2 and practical real issues. Clear conflicts of law  
3 exist with respect to the reporting of trades to  
4 SDRs or trade repositories in different  
5 jurisdictions, and with respect to customer  
6 account segregation in the clearing space. In  
7 these instances, there's a real risk that firms  
8 will be placed in a position where they have to  
9 break one set of law, one set of laws as they  
10 can't be conflicting legal or regulatory  
11 requirements, and that just can't be a good  
12 outcome.

13           And that's why the G20, the FSB, and  
14 other groups, like the ADC derivatives regulators  
15 group have all given us the answers how we can  
16 achieve effective cross-border regulation of the  
17 swaps and derivatives market, which entails, and I  
18 paraphrase, a whole range of reports. It entails  
19 avoiding the application of conflicting  
20 requirements by deferring to our respective  
21 regimes where they provide for equivalent  
22 outcomes.

1                   This is something that all of the  
2 regulatory authorities present have signed up to,  
3 and we are committed to working on, and it's fully  
4 consistent with the path forward document that  
5 Commissioner O'Malia mentioned in his introductory  
6 remarks that the European Union and the CFTC  
7 signed last year.

8                   So turning to my second point, how can  
9 we actually make this happen in practice? And  
10 this requires two steps in my view, which largely  
11 overlap with what Phyllis has already introduced.  
12 We need an assessment of equivalents or  
13 substituted compliance, which is based on an  
14 outcomes-based assessment, and we need effective  
15 collaboration arrangements between the regulators  
16 across the various jurisdictions involved.

17                   So taking those two points in turn, from  
18 an equivalents assessment to be outcomes-based,  
19 and that's a phrase that's been bantered around a  
20 lot, what does that actually mean in practice?  
21 From our perspective it means performing an  
22 assessment of the jurisdiction, not the individual

1 DCO level, and assessing whether it meets similar  
2 standards based on the international benchmarks.  
3 As Phyllis has already said, that is the  
4 CPSS-IOSCO PFMI. We should look to those first  
5 and over and above as the first port-o- call.

6 Most PFMI are extensive. We do  
7 recognize there are some areas where perhaps they  
8 could have gone into some additional granularity,  
9 so it could be envisaged that it's in the mutual  
10 interest of the relevant jurisdictions to level up  
11 on a small number of key issues and create the  
12 same and harmonize on some of the granularity, but  
13 any additional conditions should absolutely be  
14 kept to a minimum, and they must always be applied  
15 at the jurisdiction, not at the firm level.

16 And then the second part of how this  
17 regime should work requires excellent  
18 collaboration between the relevant regulators so  
19 that a host authority can easily access the  
20 information. They need to be comfortable that the  
21 CCP is being held to the relevant standards. And  
22 these were some of the points that Phyllis was

1 talking about earlier. This is distinctly better  
2 than juror supervision or even one supervisor  
3 supervising another supervisor. It can be done  
4 bilaterally, but we found that it's most effective  
5 when all of the relevant authorities get together  
6 to share their views on an individual clearing  
7 organization in a college-style arrangement, and  
8 that's the mechanisms we've already put in place  
9 for the major UK CCPs to clear on a cross-border  
10 basis.

11 The approach I've described is broadly  
12 consistent with the one that we're following from  
13 a European Union perspective. A critical element,  
14 and it's also the basis on which the U.K. has  
15 operated for many years with our recognized  
16 overseas clearinghouse regime whereby we've  
17 allowed overseas clearinghouses, notably a number  
18 of U.S. Clearinghouses to operate within the  
19 U.K., and we have deferred to the oversight of,  
20 for example, the CFTC, and we've looked at them as  
21 the primary supervisor, and that has worked  
22 extremely effectively.

1           A critical element of an overseas regime  
2           is having a reciprocal arrangement in place  
3           between the relevant regulators. Indeed, from a  
4           European perspective that is enshrined within the  
5           EMIR legislative text, and that's why I'm very  
6           pleased we'll have the opportunity to discuss the  
7           scope of the exempt DCO proposal that Phyllis has  
8           outlined today. From our perspective, a regime  
9           that applies only to member and not client trades  
10          would not be reciprocal, and it wouldn't resolve  
11          the issues I've outlined. But I'm confident that  
12          these are issues we can work together to overcome.

13                 So to conclude, it's clear we need a  
14                 comprehensive exempt DCO regime based on an  
15                 equivalence-based assessment and excellent  
16                 regulatory cooperation and collaboration.  
17                 Largely, we already have that in place. The  
18                 building blocks are already there in Dodd Frank  
19                 and EMIR in the relevant legislation and a number  
20                 of jurisdictions and we're keen to work to make it  
21                 happen.

22                 That concludes my remarks, and I'm very

1 much looking forward to questions from the  
2 Committee later.

3 MR. MIZUGUCHI: Thank you. My name is  
4 Jun Mizuguchi from FSA Japan.

5 First of all, it's my great honor to be,  
6 and also the pleasure to be here with you, and  
7 thank you for the Acting Chairman and also  
8 Commissioner O'Malia and the distinguished members  
9 from the GMAC. I really thank you for my being  
10 invited here.

11 I have just a set of slides and with  
12 just some permitted time, I just would like to  
13 take us through these slides very quickly.

14 Before I start I just want to give a  
15 small disclaimer that any views presented here  
16 today are attributed to myself and not to the  
17 views of the JFSA.

18 Well, actually, David and also  
19 (inaudible) they made some points already, but the  
20 various efforts are currently underway for the  
21 international coordination to resolve the  
22 conflicts and consistency gaps and the duplicative

1 requirements on the OTC derivatives because most  
2 of the OTC derivatives transactions are taking  
3 place at a cross-border basis and it really needs  
4 international coordination.

5 So the G20, FSB, and also the ODRG, OTC  
6 derivatives (inaudible) which the CFTC and also  
7 JFSA are members of, we are working on how to make  
8 sure (inaudible) coordination is taking place and  
9 also on the bilateral basis we are making progress  
10 where appropriate. At the G20 summit last year in  
11 St. Petersburg, (inaudible) should be able to  
12 defer to each other when (inaudible) of their  
13 respective regulatory (inaudible) regimes based on  
14 similar outcomes in a nondiscriminatory way,  
15 paying due respect to the home country (inaudible)  
16 regimes. I think basically a statement was we  
17 affirm (inaudible) G20 ministers and financial  
18 ministers and central governors meeting in  
19 February.

20 Then actually, ODRG, they sent out in  
21 March this year kind of a report to the G20, the  
22 (inaudible) G20 (inaudible) issues and the current

1 status and the schedule how to address it. So  
2 ODRG as a whole, we are still addressing any  
3 issues toward sending a final report to the G20 by  
4 the November Brisbane Summit.

5 Well, when I talk about the cross-border  
6 issue on the CCP regulation, well, actually, I  
7 just decided one example for the Japanese CCPs --  
8 well, actually, under the current circumstances,  
9 no single CCP is licensed or registered in both  
10 Japan and the U.S. So as a result, (inaudible)  
11 will not be able to enter into transactions  
12 without breaching regulations with either Japan or  
13 the U.S. unless CCP -- a CCP is licensed or  
14 registered in both jurisdictions or exempt in one  
15 of the jurisdictions.

16 So that's why a Japanese CCP, Japan  
17 Securities Clearing Corporation is now currently  
18 seeking CFTC registration as a U.S. DCO and given  
19 the lead time needed, the CFTC actually granted  
20 the JCC no-action relief from DCO registration  
21 until the end of this year.

22 Well, the number of U.S. requirements

1 currently applicable or if a foreign CCP has been  
2 registered as a DCO, well, it's including  
3 financial resources, like financial resources to  
4 cover the exposure or risk management (inaudible)  
5 annual reporting as she said and recordkeeping of  
6 all the activities on the DCOs, and also subject  
7 to the CFTC inspection.

8           Then, I just basically (inaudible) just  
9 half of it but (inaudible) exemption close on the  
10 CEA and CFTC may exempt conditionally or  
11 unconditionally foreign-based CCP from DCO if the  
12 CFTC determined that such CCP is subject to the  
13 comparable comprehensive supervision regulation by  
14 the home authorities. Then it goes on to say that  
15 such condition may include but not limited to  
16 requiring the DCO is available for inspection and  
17 also they made available all information requested  
18 by the CFTC.

19           So at this stage, I think further  
20 (inaudible) or details will, however, be needed to  
21 be provided. For example, including the condition  
22 for granting exemption and the regulatory

1 requirements which may still be applicable to  
2 exempt a DCO. Some of the idea and the staff  
3 label has been explained by (inaudible), I think  
4 they already had publication of many (inaudible)  
5 documents to set out this kind of issue could be  
6 very much appreciated to give any clarity or  
7 predictability to the markets on this issue.

8 Well, exemption from DCO (inaudible), I  
9 think there is a broader two issues. One is for  
10 the assessment method of comparability and the  
11 comprehensiveness of the home country regime.  
12 Then (inaudible) basically international rate of  
13 standards or PFMI will be a very useful benchmark.  
14 I agree with that. And also I think flexible and  
15 outcome-based approach, taking into account any  
16 differences in the regulatory framework and the  
17 market (inaudible) jurisdiction because while the  
18 U.S., Japan, and maybe in Europe, we are operating  
19 a different market structure. So a so-called "one  
20 size fits all" may not be workable in this field.

21 The second broader issue (inaudible) and  
22 what kind of regulatory requirements are still to

1 be applied to the exempted DCOs compared with  
2 those for DCO (inaudible). I heard from CFTC's  
3 staff's explanation that they were -- the  
4 conditions or regulatory requirements were to be  
5 reduced compared with those for the DCO, but would  
6 like to see, well, clearly (inaudible) regulatory  
7 comment ought to be alleviated or to be added in  
8 the very near future.

9 Well, then perhaps the possible elements  
10 to be considered by the CCP, because the CCP is  
11 the one who is applying for this exemption if the  
12 CFTC (inaudible) are finalized. Well, for  
13 example, there are maybe two issues -- the scope  
14 of the (inaudible) business. Of course, it is  
15 important for the foreign CCPs to get to know what  
16 kind of scope of business is permitted on that  
17 exemption vis-à-vis the permitted business on a  
18 DCO because (inaudible) U.S. Customers are taking  
19 the client clearing may not be permitted on an  
20 exemption. But maybe there might be some other  
21 differences in the scope of the business. So it  
22 should be made very clear on this. And also, the

1        comments need to be applied to the exempt DCO.

2                    Well, inspection reporting requirement,  
3        it's clearly stated in the CEA, but further  
4        requirements may be applied. So this is also the  
5        important consideration for the CCP whether to  
6        apply it to the DCOs or exemption.

7                    So anyhow, it will depend on how the CCP  
8        will judge these benefits on the cost (inaudible)  
9        on their business strategy and the models, but in  
10       order for the CCP to have a right decision, early  
11       publication of this proposal will be very much  
12       appreciated.

13                   Well, then, again, for the regulator  
14        side, the CFTC staff said that, well, it's also  
15        very important for the home and host supervisors  
16        to collaboratively work on this issue. Well,  
17        JFSA, we supervise all the Japanese CCPs and  
18        register the regulatory framework of Japan,  
19        including our supervisor guideline, so close  
20        coordination will be really critical for the  
21        effective CCP supervision. And actually, in that  
22        regard, actually, on March 10th, the JFSA and the

1 CFTC established a so-called memorandum of  
2 cooperation for the cross-border regulated  
3 entities, including CCPs. So I think that will  
4 pave a very good basis for the further cooperation  
5 on this exemption (inaudible) CCP or DCO  
6 registration.

7 Well, basically, well, this is the  
8 (inaudible) just going through. There are a few  
9 slides, and I think CFTC is in the process of  
10 addressing some of the issues which I just  
11 mentioned, and we do hope that while we work  
12 collectively and in good faith to achieve the  
13 common goal. Thank you.

14 CHAIRMAN WETJEN: Thanks, Jun. Thanks,  
15 David.

16 Now we're going to open it up for  
17 discussion, broader discussion.

18 Phyllis, would you mind taking us  
19 through some of the questions that we proposed to  
20 the Committee?

21 MS. DIETZ: Before we proceed with some  
22 questions about --

1                   CHAIRMAN WETJEN: Phyllis, excuse me,  
2                   can you pull that mike?

3                   MS. DIETZ: Is that better? Okay.  
4                   Before we proceed with some of the more detailed  
5                   questions about eligibility requirements and  
6                   conditions, I would like to see if anyone would  
7                   like to comment more broadly on the concept of the  
8                   exemption. And this is because we have had this  
9                   authority since the Dodd-Frank Act became  
10                  effective in 2011, and we haven't issued any  
11                  exemptions to date. We have engaged in this  
12                  no-action process, but that has been pending  
13                  either application approval or registration  
14                  approval, or now we've been talking a little bit  
15                  about the possibility of an exemption. So the  
16                  no-action relief is time limited and is not  
17                  viewed, at least at this point, as a permanent  
18                  resolution. So I just wonder if there are any  
19                  comments about generally whether or not the  
20                  exemption proposal is a good idea, bad idea, or  
21                  let's propose it and see what people think.

22                  So are there any just general comments

1 before we get to the specifics?

2 MR. TURBEVILLE: Thank you. Wally  
3 Turbeville from Demos.

4 Just on the general tenor of the  
5 discussion, Mr. Bailey used the term "retreat  
6 behind national boundaries," and I was struck by  
7 the fact that what he said about it, I'm concerned  
8 about retreating behind national boundaries and I  
9 interpret this whole situation completely in the  
10 opposite way I've got to say.

11 If you talk to major regulators who are  
12 concerned with international regulation right now,  
13 the biggest concern they have is that home country  
14 regulators in certain places are more and more  
15 intent on husbanding information about the  
16 financial utilities and also the financial  
17 institutions within their boundaries, being  
18 concerned that if they share information more  
19 broadly it would harm their home country financial  
20 sector. So when I see outcomes based regulation  
21 that's all about let us husband information and  
22 you concern yourself with the outcomes, and let's

1 remember, this is about registration only. This  
2 is about registration, and this is not about  
3 registration of a foreign border trade that just  
4 matches transactions. This is about managing the  
5 risks of \$100 trillion a year swaps market where  
6 risk is concentrated in clearing organizations,  
7 which if managed well will put us in a better  
8 position, but which if managed poorly could be the  
9 mechanism for transmitting risk throughout the  
10 international markets for another crisis. So this  
11 is not trivial.

12           Most of the reporting information is  
13 actually -- that you discussed, was actually about  
14 our institutions that are trading over there. I'm  
15 much more concerned about their institutions  
16 trading over there and how they're doing and how  
17 that might affect our country. So to that extent  
18 I would like to, if I don't get to ask it in the  
19 future, ask the question whether at a minimum we  
20 are requiring stress tests using the test  
21 standards that we have developed here which are  
22 extreme but plausible conditions, requiring stress

1 tests for each and every one of the clearinghouses  
2 that we're going to subject our economy to the  
3 risk of going forward. That's my specific  
4 question, but I'd really like to change the tenor  
5 of this away from, you know, retreating behind  
6 boundaries is all about total comity as opposed to  
7 making sure that we all get the information shared  
8 and reaching those boundaries.

9 MS. DIETZ: If I may just respond to the  
10 question about the conditions. These conditions,  
11 while similar to those imposed on registered DCOs,  
12 these are conditions that the foreign-based exempt  
13 DCO would have to meet. And the concept of  
14 holding the clearing organization and its  
15 regulator to the PFMI is that there is  
16 comparability. We're not going to find any  
17 regulatory regime that is identical to ours  
18 because each nation has their own set of  
19 regulations and certainly having been a primary  
20 author of our part 39 requirements, I know that we  
21 have some very particular requirements that aren't  
22 found elsewhere. But I think that we see the

1 PFMIs as being a sufficient standard. We do not  
2 have an explicit stress testing requirements. We  
3 are not going to look at the margin methodologies  
4 under the current proposal because that is going  
5 to be left to the home country regulator under the  
6 PFMIs. So I think that also raises another  
7 question that we had posed, which is what do  
8 people think about the PFMIs as the standard.

9 MR. TURBEVILLE: You're answering the  
10 question by saying we're going to do this, and  
11 just so everybody understands, I'm saying that's  
12 foolish. We shouldn't do that.

13 MS. DIETZ: And just to clarify, it is  
14 not my intention to say we are going to do this.  
15 We are working off of a staff draft now.  
16 Ultimately, this is a Commission decision. As the  
17 acting chairman mentioned earlier, there are  
18 certain considerations that are outside of the  
19 rule text -- competitive issues. These are the  
20 kinds of things -- policy. There are a number of  
21 policy decisions that have to be weighed that are  
22 wholly aside from whether we want something

1       quarterly or every six months. So just to be  
2       clear, this is a staff draft, and one of the  
3       benefits of this meeting being today is that we  
4       have the opportunity to discuss it.

5                     So, thank you. I guess, Bob, did you --

6                     MR. KLIEN: Yeah, I'd like to go back to  
7       your initial question and say that I think this is  
8       a long overdue concept, and one that is actually  
9       quite pressing, and it's pressing for a couple of  
10      reasons in particular. One is that while the U.S.  
11      led the regulatory reform timetable in terms of  
12      implementing mandatory clearing, other  
13      jurisdictions are rapidly catching up and there  
14      are now mandatory clearing rules either in place  
15      or about to be put in place in Europe and in a  
16      number of Asian jurisdictions. And when that  
17      happens, market participants are going to face the  
18      exact kind of clear conflict that we talked about  
19      at the beginning. In other words, if you have a  
20      U.S. participant trading with a non-U.S.  
21      participant, each one of which is subject to a  
22      mandatory clearing determination and each one of

1       which is subject to clear in a clearinghouse  
2       regulated by their home jurisdiction, there really  
3       aren't a lot of choices you have. Either one of  
4       those parties can decide to break the law, which  
5       isn't going to happen, or they won't do the  
6       transaction, which I think is unfortunate. Or  
7       we're going to have to find a way of providing  
8       mutual recognition of clearinghouses so that both  
9       parties can clear the trades at a clearinghouse of  
10      their choice.

11                 The second thing that I think is worth  
12      mentioning in terms of how critical this is is  
13      that it's been widely reported that the Commission  
14      is now considering a mandatory clearing  
15      determination for FX NDFs. That hasn't happened  
16      yet, but if the press reports are accurate, it's  
17      certainly under active consideration. And I think  
18      the NDF market is largely dominated by local  
19      transactions involving potentially cross-border  
20      counterparties who provide liquidity. And if  
21      they're subject to a mandatory clearing  
22      determination in the U.S., unless there is a

1 comparability or recognition regime in place, I  
2 think the kind of conflicts that we've talked  
3 about and that exist potentially already are going  
4 to be exacerbated.

5 I'd also like to go back and respond to  
6 some of the comments from my fellow committee  
7 member. I think the Commission and its foreign  
8 colleagues are quite capable of sharing  
9 information. They do it routinely. They do it in  
10 the enforcement context. They do it in other  
11 contexts. And I think you can work out the  
12 details of that information sharing. I think  
13 what's more troubling is what appears to be the  
14 premise behind the remarks, which is that there's  
15 U.S. regulation and there is inadequate  
16 regulation. I think that's a false premise to  
17 begin with. I think there are multiple regulatory  
18 regimes. We have a number of participants in the  
19 G20 standards. I think they're all working in good  
20 faith to implement those standards, and I think in  
21 order to achieve the policy directives behind  
22 those standards of fostering clearing of what is a

1 global market, it's going to require a lot more  
2 coordination among regulators in order to make it  
3 work in a seamless manner.

4 CHAIRMAN WETJEN: Let me just make one  
5 point of clarification. For the sake of the group  
6 and discussion on the issue of the NDF mandate,  
7 it's probably most accurate to say that it's being  
8 actively recommended to the Commission, but we're  
9 still mulling that over.

10 MR. DIETZ: David?

11 MR. WEISBROD: So in answer to your  
12 question, Phyllis, I represent LCH Clearnet. We  
13 are -- I don't want to say unique, but we have  
14 been and are duly regulated both by the CFTC and  
15 the Bank of England, that is to say LCH Clearnet  
16 Limited. So we have experience in a dual-  
17 registered environment.

18 In answer to Phyllis's question, I would  
19 commend your initiative here. I think also, as  
20 Rob has just said, it is long overdue. We feel  
21 that the PFMIs are a good basis for which to make  
22 these determinations. We think that the dual

1 registration has been challenging. While it works  
2 and it has certain benefits, the notion of an  
3 exempt DCO category is one that has merit, the  
4 details of which need to be worked out between the  
5 regulators. We would also agree with the concept  
6 of the MOU as you've articulated in terms of the  
7 standards of inspection, recordkeeping, reporting  
8 to the SDR, and open access. And so our comment  
9 would be very supportive of the initiative that  
10 you've outlined.

11 MS. DIETZ: Kim?

12 MS. TAYLOR: Thanks, Phyllis. I want to  
13 thank Chairman Wetjen and Commissioner O'Malia for  
14 holding this forum and letting us have an  
15 opportunity to participate today.

16 In answer to your question, I think --  
17 and speaking on behalf of the largest major  
18 exchange and clearinghouse that has to date  
19 primarily located its business in the U.S. regime  
20 gives me a certain perspective that I want to  
21 share.

22 I think CME broadly supports the idea of

1 mutual recognition with a level playing field. It  
2 needs to be thoughtfully considered though for all  
3 of its implications. It needs to be grounded in  
4 the PFMIs. I agree with several of the parties  
5 who have talked about that. And it needs to limit  
6 the exporting of what I would call PFMI gold  
7 plating across jurisdictions.

8           So now let me describe what I see in the  
9 current environment. In the current environment,  
10 with respect to futures, the CFTC has long granted  
11 and has persisted with basically complete relief  
12 from regulating foreign markets and foreign  
13 clearing of those products -- of foreign futures  
14 products by U.S. persons. That has been done with  
15 various types of exceptive relief and those have  
16 stayed in place over time and including in the  
17 post Dodd-Frank arena. Now, if I look at what's  
18 happening in Europe, I'm quite familiar with what  
19 I'll call the quest for European equivalence as a  
20 clearinghouse. And in some respects, the quest  
21 for European equivalence has many of the elements  
22 of what I would call a financial doomsday

1 thriller. The European authorities have taken  
2 hostage basically all of the exchanges and  
3 clearinghouses that do not operate on their soil,  
4 and said that as of a certain time those hostages  
5 will basically be shot. With respect to on  
6 December 15th if there's not an equivalence  
7 determination, the European parties will not be  
8 able to use markets or clearinghouses that exist  
9 outside of European soil unless equivalence has  
10 been determined. And the way that equivalence is  
11 being determined involves the exporting of a fair  
12 number of elements of European regulation. To  
13 take Bob's comment and turn it kind of on its  
14 side, it's almost as if the E.U. authorities are  
15 determining that there's European regulation and  
16 ineffective regulation. So the same comment could  
17 be used from either direction.

18           So what I would like to see is an  
19 opportunity for the global regulators to work  
20 together in a way that is not time limited by a  
21 big doomsday clock ticking off the time until  
22 December 15th, and come to an agreement on a

1 mutual recognition regime that allows for a level  
2 playing field across multiple jurisdictions.

3 MR. O'CONNOR: Thank you. I would  
4 preface my remarks by just picking up on something  
5 Kim said there, and I think we should stress the  
6 importance to have a global level playing field.  
7 So what I'm about to say I would say to Europe and  
8 Asia, also.

9 But turning to the opening this morning,  
10 I was encouraged to hear both -- at the outset,  
11 both commissioners refer to the importance of  
12 mutual recognition, and then further remarks by  
13 Commissioner Wetjen calling for the need for  
14 comity and competitiveness. And for me, as  
15 outlined by Commissioner O'Malia and echoed by Mr.  
16 Bailey, I think that that has to take the form of  
17 a full substituted compliance or equivalent route.  
18 So it's disappointing that the staff proposal  
19 refers to the exemption at an entity level rather  
20 than a jurisdictional level.

21 A second, and based on this initial take  
22 of the proposal, a second fundamental issue that

1 jumps out is that the proposal for exemption is  
2 limited to interbank clearing and not client  
3 clearing. And I'm not sure that provides any  
4 relief. We're very close to the entire interbank  
5 market being cleared already, particularly in  
6 rates and credit, and that market seems to be  
7 functioning pretty well within the existing  
8 frameworks and has done for a number of years  
9 ahead of any regulatory mandates. And I think  
10 client clearing is where the relief is needed, not  
11 interbank clearing. I think the approach, if  
12 adopted, will lead to increased or prolonged  
13 fragmentation and less choice for U.S. end-users.

14 MR. RAMASWAMI: Again, let me start by  
15 saying thank you for having us here. I work in  
16 the Singapore Exchange, and we are, I think the  
17 only Asian clearinghouse that has already started  
18 DCO. And so we've been through the hoops on  
19 registering. And while that was interesting, it  
20 didn't quite solve our problem. So let me kind of  
21 step back to say why.

22 I think that the object of the Singapore

1 Exchange trying to have our clearinghouse  
2 registered was to be able to continue to clear  
3 U.S. customer swaps which are done between U.S.  
4 entities and Asian counterparts. And in the  
5 context where we are a registered DCO, the issue  
6 just goes one level lower in the sense that you  
7 need to have FCMs as members. And today, in the  
8 context in which we operate, in most of our  
9 jurisdictions, the membership that we have are not  
10 the exact FCM entity of all the client  
11 organizations. So you have an equivalent  
12 affiliate which is a general clearing member  
13 generally subject to local regulations and is  
14 generally a part of the locally incorporated  
15 entities, and in the context where the GCMs are  
16 doing the clearing, it is still not possible for  
17 them to clear U.S. customer positions.

18 And again, speaking broadly, most of our  
19 members don't see the business rationale yet to  
20 have two memberships, one for, you know, clearing  
21 non-U.S. business and one for clearing U.S.  
22 business. And our hope, of course, is that there

1 would be a road through the affiliate model as in  
2 the futures markets to do the similar thing on  
3 swaps.

4 Now, again, if you step one further  
5 level into the detail, the core really seems to be  
6 about affording bankruptcy protection under U.S.  
7 regulation to the U.S. Customer base, and I think  
8 that that is something that one could work  
9 solutions for. But I think that it certainly  
10 doesn't stop at this level of debate. I think  
11 that we could easily agree to having recognized  
12 clearinghouses overseas, but if it doesn't extend  
13 down to being able to clear U.S. Client  
14 positions, then it doesn't quite solve the problem  
15 in its entirety. So I think it's important to  
16 bear that in mind as you deliberate the processes  
17 and as you go forward.

18 To me, the registrations are not, and  
19 being, you know, recognized, the difference is not  
20 great. In both cases you have to do all the data  
21 sharing. You do have equivalents in many, many  
22 contexts. And PFMI does provide a fairly good

1 basis, however, it doesn't address, as an example,  
2 the U.S. bankruptcy or different countries'  
3 bankruptcy laws. So it's in peeling the layers  
4 that I think you will need to kind of spend more  
5 time and attention.

6 CHAIRMAN WETJEN: Special thanks to you  
7 for being here today. You've come all the way  
8 from Singapore. We appreciate everyone attending,  
9 but you made a special effort given the distance  
10 you've traveled. And nice to have your unique  
11 perspective as a foreign-base registered DCO.

12 MR. RAMASWAMI: Thank you.

13 MS. DIETZ: Adam?

14 CHAIRMAN WETJEN: Can I just say one  
15 other thing, too? I couldn't agree more with Rama  
16 in a lot of ways. At the heart of this is a  
17 country's bankruptcy regime, and what we are  
18 regulators here at the CFTC have to say about that  
19 and what interests we have in terms of, if I can  
20 use the word "protecting" the U.S. customer in  
21 that way because I think we've all seen in recent  
22 times how the regimes work differently in our

1 space, in the derivative space, and referring  
2 obviously to the MF global situation. And for a  
3 variety of different reasons, the customers of the  
4 MF global FCM, they have commitments to have all  
5 their monies returned, and that has happened in a  
6 relatively quick amount of time. And I'm not sure  
7 where the proceeding is in London. I've lost  
8 track, but my understanding is it hasn't gone  
9 quite as quickly at least. And so that is  
10 something we're thinking a lot about. In fact,  
11 just this morning we had a rather lengthy  
12 discussion about it, Phyllis and I and some  
13 others, and it came up in the context of an  
14 earlier discussion we had with some of David's  
15 colleagues in Europe about both the equivalency  
16 determinations as well as related FCM seg  
17 bankruptcy issues. So that does seem to be, in a  
18 lot of ways, at the heart of this, but it's a very  
19 important consideration I think to make. And so I  
20 imagine that notwithstanding some of the  
21 complications it creates, I guess I would ask the  
22 group to appreciate with our interests as

1 regulators are in the sense of making sure U.S.  
2 customers trading in our regulated venues and  
3 through our regulated clearinghouses have the full  
4 benefit of appropriate bankruptcy protection.

5 MS. DIETZ: Go ahead, David.

6 MR. BAILEY: Acting Chairman Wetjen,  
7 just a comment on that point.

8 Coming from a European perspective, as  
9 we are going through the process of authorizing  
10 clearinghouses under EMIR to operate across  
11 Europe, we're having to deal with exactly the  
12 issue you've highlighted there of different  
13 insolvency and bankruptcy rules in different  
14 jurisdictions. And a critical element that we  
15 have found is ensuring the legal enforceability of  
16 the CCP's default rules in each of the  
17 jurisdictions that it operates. So a primary  
18 focus has been to ensure that if a clearinghouse  
19 is going to operate in more than one European  
20 jurisdiction, the CCP is able to give us a very  
21 clear comfort that its default rules are fully  
22 enforceable in those jurisdictions which will

1 facilitate its ability to handle the default and  
2 return client monies. So that's been the primary  
3 focus. I think that, to a large extent, if we  
4 have that in place as part of an exempt overseas  
5 regime, that will address a significant amount of  
6 the concerns that you've raised there.

7 MS. DIETZ: If I may just add for a  
8 moment and then we'll hear from Adam, just by way  
9 of background, this Commission has never issued an  
10 exemption that permits 4D segregated funds to be  
11 held in an account other than a 4D account. We  
12 came close to that with respect to Singapore. It  
13 was no action relief that permitted limited  
14 customer clearing for the period of time until  
15 they became registered. So I just wanted to point  
16 that out, that as a policy matter it would not be  
17 impossible to do, but it would be a major, major  
18 change in the policy of this Commission, and it  
19 would be given very careful consideration. Thank  
20 you.

21 Okay, Adam.

22 MR. COOPER: Thank you very much. And

1 Acting Chair and Commissioner O'Malia, and  
2 Designated Federal Officer Serafini, thank you.

3 I want to address a few things, but I  
4 think that last point you raised is critical,  
5 Phyllis. One of the key aspects -- you asked are  
6 the proposed eligibility requirements appropriate,  
7 and one of the key aspects of the PFMI is the  
8 requirement of fair and open access to the  
9 clearing infrastructure. Citadel believes the  
10 proper implementation of that principle is  
11 essential to the proper implementation of swap  
12 markets reforms. So we urge that the regulations  
13 be sensitive to the concept of fair and open  
14 access and provide or permit, if you will, as  
15 little daylight as possible between the CFTC's  
16 regulatory position on impartial access and the  
17 approach taken by the local regulator. But that  
18 fair and open access really is the crux of what  
19 we're talking about, and I comment David Bailey's  
20 point in his introduction that we should not  
21 separate the customer solution from the  
22 proprietary solution.

1                   So in thinking about whether an exempt  
2 DCO should be permitted to clear swaps for  
3 customers that are U.S. Persons, we have to  
4 recognize another critical component to swaps  
5 market reform is customer protection. Certainly,  
6 the discretionary authority granted to the CFTC  
7 shouldn't be exercised if the result would be a  
8 result that would place the U.S. customers at a  
9 disadvantage to the regime they would have here in  
10 the U.S. And so that's really the challenge here.

11                   I think there is a solution. I think  
12 we're pretty much in agreement that there's a path  
13 forward, and perhaps the way to navigate that path  
14 is that the Commission should establish a route  
15 whereby an exempt DCO would be permitted to clear  
16 swaps for customers that are U.S. persons. If  
17 there is some sort of fundamental demonstration  
18 that the outcome of its customer asset protection  
19 regime offers a level of protection that's at  
20 least as strong as in the U.S. And I think David  
21 a moment ago talked about the legal opinions or  
22 the assurances that can be given. That may be a

1 way to sort of navigate this path so we provide  
2 the fair and open access to customers and not just  
3 the proprietary solution, but assure that the U.S.  
4 participants are not disadvantaged.

5 CHAIRMAN WETJEN: So I think the  
6 follow-up question then is should that assessment  
7 of another regime's customer protection approach  
8 involve issues or rules or laws outside of our  
9 very particular responsibilities here. In other  
10 words, should it include an assessment of another  
11 country's bankruptcy approach which is not  
12 something that either we have a direct say in or  
13 even the FCA has a direct say in as I understand  
14 it in the U.K. Is that an appropriate thing for  
15 us as policymakers to consider?

16 MR. COOPER: To consider but not  
17 necessarily mandate. Right? I think it goes into  
18 the equation of the comparability assessment that  
19 needs to be made in the process of the exceptive  
20 relief exercise. So it's -- we're not seeking to  
21 legislate the foreign country's bankruptcy regime,  
22 but we have to make an assessment in light of the

1 requirements that exist here in the U.S. whether  
2 it's comparable and sufficient.

3 MS. DIETZ: So then just to clarify, the  
4 suggestion would be that an applicant for  
5 exemption, if they wanted to clear for customers,  
6 what we consider customers, they would have to  
7 make a demonstration, provide exhibits,  
8 documentation, legal opinions, whatever, analyzing  
9 a comparison of the U.S. and the home country  
10 bankruptcy laws and then it would be up to the  
11 Commission to make a judgment as to whether or not  
12 there was comparability. Because the PFMI's don't  
13 address bankruptcy.

14 MR. COOPER: Correct. Correct.

15 MS. DIETZ: I just want to make sure I  
16 understand.

17 MR. COOPER: Yes.

18 MS. DIETZ: Okay. Okay. Thank you.

19 Kim?

20 MS. TAYLOR: Just another type of issue  
21 that I think we need to make sure that is  
22 considered in looking at the bankruptcy

1       implications would be the implications of a large  
2       portion of the dollar-based swap business or the  
3       dollar-based FX business, clearing in a location  
4       that is outside the jurisdiction or oversight of  
5       the U.S. Authorities in a broad sense, not just  
6       in the narrow sense of the CFTC supervision of the  
7       exempt DCO. But in terms of the impact, the  
8       potential impact to the broader U.S. Financial  
9       industry or the economy at large of the  
10      liquidation or the crisis management impact of a  
11      large default situation that was done without U.S.  
12      oversight. I know that a lot of international  
13      regulators have also had that as a concern.

14                 MR. ALLEN: I just wanted to build upon  
15      those comments about the issue of the application  
16      of bankruptcy or insolvency rules more generally  
17      as it relates to client business. It strikes me  
18      that it fundamentally is the elephant in the room  
19      here because what we're talking about in terms of  
20      the clearing mandates is not really the entity of  
21      the market at all. The entity of the market has  
22      been substantially cleared now for a number of

1 years, a series of commitments made as early as  
2 2005 signaled the significant migration towards  
3 interdealer clearing of business. So when we're  
4 talking about clearing, whether under Title VII  
5 under AMIR, first and foremost we're really  
6 fundamentally talking about client business. That  
7 introduces the difficult topic of what does that  
8 mean in terms of risk allocation and the impact on  
9 customers in the event of a CCP default or member  
10 default. Inevitably, that's going to raise  
11 fundamental tricky questions which go beyond the  
12 conventional purview of the CFTC in terms of  
13 looking at considerations (inaudible). But I do  
14 think that that really is what this is all about.  
15 And the consequence of not going down that route  
16 and grasping that at all is that we get increased  
17 numbers of tangible examples of conflicts and  
18 potential for market fragmentation, early  
19 indications of which have already been suggested  
20 are not theoretical but area real. We've seen it  
21 in the context of trade reporting. We're seeing  
22 it now in the context of individual account

1 segregation requirements. And if we roll forward  
2 to the regulations that are still to come down the  
3 track, either here in the United States or in  
4 Europe, or quite frankly elsewhere, that potential  
5 for conflict in the absence of a genuine and  
6 concerted outcomes- based approach to the  
7 consideration of alternative regulation regimes is  
8 going to lead to increased instances of market  
9 fragmentation.

10 I think if that means that the focus of  
11 the CFTC has to encompass within its scope an  
12 allocation of risk in the circumstances of CCP  
13 failure -- I'm picking up on the point that David  
14 mentioned from the FCA -- then I think that's the  
15 route that has to be adopted. Otherwise, I  
16 appreciate it will be very difficult for the CFTC  
17 to get over the line in terms of satisfying itself  
18 that customers are not at risk. As I say, a focus  
19 of this effort exclusively around the interdealer  
20 business strikes me fundamentally misses the  
21 point.

22 MS. DIETZ: If I may I'd like to yield

1 the floor to an invited guest, Bob Wasserman, who  
2 is our bankruptcy guy. That's, I think, his  
3 title. So he's the chief counsel of the Division  
4 of Clearing and Risk.

5 MR. WASSERMAN: Thank you. And thank  
6 you all. Thank you to you all for letting me  
7 interrupt just for a few moments here.

8 With respect to the PFMI, I think we  
9 have a wonderful opportunity here because we have  
10 a standard that's been agreed to internationally  
11 among the regulators. There is a structure for  
12 evaluating and essentially assessing compliance  
13 with that standard that is going on even now among  
14 the various jurisdictions to see essentially are  
15 folks, in fact, observing those standards.

16 With respect to bankruptcy regimes,  
17 that's a much more difficult task. There is no  
18 agreed standard in terms of bankruptcy or customer  
19 protection. Some folks have mentioned, well,  
20 perhaps we could get opinions. I'll tell you that  
21 my experience in getting law firms to actually  
22 give opinions as opposed to memoranda with

1       respected to issues in general, and bankruptcy in  
2       particular, has been that it's like pulling teeth  
3       without anesthesia. To get them to give opinions  
4       that actually are -- essentially pin folks down as  
5       opposed to say, well, if this happens maybe, and  
6       if that happens maybe, I think would be a very  
7       heroic task. And so those are some of the  
8       difficulties I see. I would also note that when  
9       we're speaking of customer protection, it is not  
10      only at the level of what's at the CCP, and  
11      thankfully we've seen very few instances with CCP  
12      failure or loss of customer funds at that level,  
13      but rather, we are also concerned with potential  
14      loss of customer funds at the intermediary level.  
15      And so those are just some of the complications  
16      that would be involved if we were to start trying  
17      to assess bankruptcy regimes. Thank you.

18                   MS. DIETZ: And Bob would be the person  
19      who would have to assess them.

20                   Okay. Let's see.

21                   CHAIRMAN WETJEN: That was Commissioner  
22      O'Malia.

1                   COMMISSIONER O'MALIA: Thank you.  
2           David, so I'm clear, can you lay out where you  
3           said about the customer clearing regimes and  
4           requirements, how the U.S. is incomparable at this  
5           point and what would it take to be comparable?

6                   I'd also like to hear from Mr. Mizuguchi  
7           whether Japan is seeking customer client clearing  
8           in its application, and then maybe Phyllis can  
9           respond, or Bob can respond now how our LSOC  
10          proposal for swaps meets kind of response to  
11          whatever David is going to say.

12                  MR. BAILEY: Sure. And just to one  
13          point Bob made out here about getting a legal  
14          opinion on bankruptcy laws, that kind of reaction  
15          is actually pretty much what I get whenever I try  
16          to get a legal opinion on anything, let alone  
17          bankruptcy.

18                  But Commissioner O'Malia, to your point,  
19          so from a European perspective, as we've been  
20          authorizing clearinghouses in EMIR -- and I'm  
21          talking specifically here to start with about  
22          European CCPs. We have -- clearly they're

1 operating in a number of -- or could be operating  
2 in a number of European jurisdictions, and  
3 therefore, what we've really focused on through  
4 the college arrangements that we have in place for  
5 that authorization is can the CCP effectively  
6 deploy its default rules? And as I'm sure you're  
7 aware, one of the structures available under EMIR  
8 is the individual segregated account, and under  
9 that account, one of the key benefits of that type  
10 of account is in the case of the insolvency of the  
11 clearing member as opposed to the CCP itself. The  
12 CCP can return the client's positions and the  
13 client collateral directly back to the client  
14 without going through the clearing member's  
15 estate. That provides, from our perspective, a  
16 really effective way of ensuring that that client  
17 can either transfer those positions to another  
18 clearing member or take whatever action they feel  
19 is relevant. And the important thing is their  
20 collateral and their positions are not tied up in  
21 the clearing member's account as it goes through  
22 administration. And that's the sort of maximum

1 level of protection afforded to a European client  
2 under AMIR, and they can elect to take on that  
3 protection.

4 CHAIRMAN WETJEN: So you have to assess  
5 all the individual European countries' bankruptcy  
6 regime as to whether or not that bankruptcy regime  
7 would permit what you just described?

8 MR. BAILEY: We are not -- so from a  
9 regulation perspective, the onus is on the  
10 clearinghouse to demonstrate that it can affect  
11 its default rules legally in each of the  
12 jurisdictions it wants to operate in. That's  
13 different from assessing each clearinghouse  
14 against all 28 countries because not every  
15 clearinghouse wants to operate in all 28  
16 countries. And that is primarily assessment from  
17 the CCP and the obligation is on the clearinghouse  
18 to demonstrate to us that it can affect its  
19 default rules.

20 Commissioner O'Malia's secondary point  
21 was on the comparability from a U.S. perspective  
22 and the U.S. Equivalents' assessment, and that is

1 a process -- just to be clear, that is a process  
2 that is being coordinated by EMIR and the European  
3 Commissioner, and I can't speak on their behalf as  
4 to the current status of that assessment, nor  
5 would it want to. But essentially, part of that  
6 process is assessing an overseas regime. Note is  
7 it identical to the absolute letter of every  
8 sentence of the law, but does it provide for  
9 broadly equivalent outcomes, i.e., is there a  
10 mechanism to get client funds returned to them in  
11 a timely manner and allow them to continue with  
12 that business? So again, I'll very much stress we  
13 are not assessing as regulators the bankruptcy.  
14 The insolvency legislation of the jurisdictions is  
15 for the clearinghouse to demonstrate to us that it  
16 can affect its default rules.

17 MR. MIZUGUCHI: You know, if I may just  
18 make a comment on this. The issue with, you know,  
19 a place where the customer has to make the choice  
20 of whether they go for this ultimately segregated  
21 account results in a lot of customers not making  
22 that choice up front. And therefore, you end up

1 with customers who have comingled margins, and  
2 therefore, the inability to unwind as quickly. So  
3 in some ways it's not, you know, inappropriate to  
4 think of a regime that would almost mandate  
5 customer funds to be in segregated accounts. And  
6 what that does in many cases then is levels the  
7 playing field everywhere and you do have, you  
8 know, house margins and customer margins, and  
9 customer margins are mandated to be individually  
10 segregated. And that's, again, something to think  
11 about because I think that's the issue, you know,  
12 if you go through the past occurrences in the  
13 European context, that's what made them, you know,  
14 they're all in omnibus accounts where they are not  
15 segregated by customer. While they're broadly  
16 segregated into customer and house, they're not  
17 individually segregated. And therefore, that is  
18 something that, you know, you could almost look at  
19 as a condition for equivalence or at least afford  
20 that to the U.S. customer base and then the rest  
21 can still have it optional if that's what they  
22 want to do.

1           Ultimately, you know, when it comes to  
2 margins, they are generally higher if you are  
3 individually segregated, and in most cases they  
4 say, oh, it's not worth the difference. You  
5 cannot be comingled, and then when the times are  
6 not good it looks bad. So I think that's really  
7 the fundamental assessment that has to be made  
8 about is it worthwhile to mandate that or not.

9           MS. PORTNEY: Just to add on that, and  
10 thank you very much, Acting Chairman and  
11 Commissioner O'Malia for a chance to weigh in on  
12 these big considerations. Just a follow-up to  
13 that point. I think though that still individual  
14 segregation, albeit might be a very, you know,  
15 good idea, still doesn't, to my knowledge, solve  
16 the bankruptcy issue that we have in the states  
17 which is ultimately that in the event of a  
18 bankruptcy that ultimately all customer assets  
19 would be pooled and distributed as per the  
20 administrator. And so, you know, ultimately,  
21 that's another way to perhaps further protection  
22 but doesn't actually get at the underlying

1 conflict of bankruptcy issues. So.

2 MS. TAYLOR: I think that a lot of this  
3 discussion is I think pointing to the fact that  
4 this is a very worthy goal, having a level playing  
5 field and a mutual recognition regime, but that it  
6 is -- it is a process that will have many impact  
7 points and needs to be thoughtfully considered for  
8 all of those impact points. And I think the  
9 global regulators need to work together to try and  
10 achieve it in a way that does not unnecessarily  
11 drive up the costs for everyone using the broader  
12 derivatives trading and clearing system. Although  
13 the idea about individual segregation as a mandate  
14 certainly has aspects to it that are tempting, I  
15 think that it is also an example of a situation  
16 where, as Emily points out, there might not be an  
17 ability in certain jurisdictions to actually  
18 achieve it, or it might be mandating a  
19 significantly higher cost on a vast majority of  
20 market participants who would not actually choose  
21 to "buy" that additional insurance.

22 So I think the discussion points to the

1 fact that it seems there's wide agreement that we  
2 need to pursue a mutual recognition regime that  
3 applies globally, but there is a lot of -- there  
4 are a lot of issues to be worked out and it's  
5 probably not something to be done without --  
6 hastily and without a lot of consideration of all  
7 those implications.

8 MS. DIETZ: If I can just make a couple  
9 quick points. Certainly, Kim, in response to your  
10 concluding remark there, one of the benefits of a  
11 meeting like this, and ultimately of a public  
12 comment period, is to take the discussion to the  
13 broader public with more specific details and be  
14 able to consider some of these very critical  
15 issues, some of which mark a dramatic change from  
16 the way business has been done in the past.

17 Also, just, I believe Commissioner  
18 O'Malia asked about customer clearing for our own  
19 clearinghouses, and JSCC has an application before  
20 us, and it includes customer clearing. And for  
21 all of our registered DCOs, we require that they  
22 have the ability to offer customer clearing. If

1       they don't have any customers or FCMS, so be it,  
2       but they have to have the capability to do that as  
3       full service.

4                   MR. MIZUGUCHI: Thank you. Just for the  
5       Japanese regimes, well, on the segregation  
6       (inaudible) requirements, basically, we are  
7       conforming to the PFMI principles. Some of the  
8       accounts, well, some of the CCP are taking some  
9       individual comments for some projects, like OTC  
10      derivatives projects, but we are basically  
11      conforming with the PFMI. Well, one of the  
12      difficulties we are facing here is that the  
13      Japanese CCPs are either being assessed by the  
14      European regime and also they're being assessed by  
15      the U.S. Regime. So what would happen? Well,  
16      unless you and the U.S. are conforming to each  
17      other, we are in a very difficult position because  
18      once we meet the criteria of one particular party,  
19      that may not guarantee that we are conforming to  
20      another party. So that's quite a dilemma we are  
21      facing now.

22                   CHAIRMAN WETJEN: Can I ask one

1 question? The bankruptcy point was made about how  
2 it squares with an individual segregation approach  
3 here in the United States or how it doesn't, but  
4 if someone representing a FCM were familiar with  
5 how they operate, isn't it, in fact, the case that  
6 it is possible to set up some kind of an  
7 individual segregated account? It would have to  
8 be funded by the FCM in some way as I understand  
9 it, but if someone would be willing to talk about  
10 that a little bit. In other words, I've heard  
11 from, I believe -- I know, at least one FCM that  
12 it is, in fact, a possibility. It might be a  
13 rather expensive one, but I wonder if someone from  
14 the FCM committee could speak to that.

15 MS. PORTNEY: I can talk to that if you  
16 like. We certainly can set up individual  
17 segregated accounts for our customers. And, you  
18 know, there could be a cost associated with that  
19 in terms of funding, as well as operational  
20 support. But I think the real issue when you get  
21 down to just pure customer protection is in the  
22 event of my FCM's bankruptcy, at the end of the

1 day those customer -- any assets held in any  
2 customer account, segregated or not, would be  
3 deemed a part of the overall customer pool of  
4 assets to be administered by the estate. So a  
5 customer having opted into individual seg has no  
6 real more protection in the event of my bankruptcy  
7 as a customer who was in my omnibus seg account.

8 CHAIRMAN WETJEN: But isn't there a way  
9 to work around that as well to make them -- give  
10 them some other status as a creditor in the case  
11 of a bankruptcy?

12 MS. PORTNEY: We have not -- we have not  
13 figured that out yet. From my understanding, it's  
14 really no. And even a third-party custodial  
15 account would be the exact same thing, which are  
16 not allowed in futures, could be allowed in swaps.  
17 But the same thing. It would be part of the  
18 pooled assets in the event of our bankruptcy.

19 MR. KLIEN: I'll second that from a FCM  
20 perspective.

21 I think, you know, the issue really is  
22 it's costly. You're likely going to want to pass

1 the cost on to the client, and the client is going  
2 to say, okay, this is very expensive, now I want  
3 your assurance that in an insolvency I'm actually  
4 getting better protection out of this and you just  
5 can't give them that assurance because at the end  
6 of the day the 4D pool and the 37 pool get  
7 administered as a pool and customers prorate in  
8 the loss.

9 MR. WASSERMAN: Yeah, the difficulty  
10 there is that the bankruptcy code has that  
11 provision, which provides for pro rata  
12 distribution. And so even though you're keeping a  
13 separate pool, so long as you are, in fact, a  
14 customer of the FCM, as opposed to a direct  
15 clearing member, you would be essentially pro  
16 rata-ed in the event of the insolvency of the FCM,  
17 which is why we developed LSOC basically as a way  
18 to harmonize a degree of individual customer  
19 protection, but on the other hand, dealing with  
20 bankruptcy code.

21 COMMISSIONER O'MALIA: Bob, building on  
22 that LSOC question, and it was part of the

1 question I asked David, since the swap rules  
2 mandate we offer LSOC, if we offered customer  
3 clearing as part of the exempt DCO proposal, would  
4 we have to insist that we, too, offer LSOC for  
5 that as well as therefore, European clearinghouses  
6 would kind of face the same challenges U.S.  
7 clearinghouses under European rules?

8 MR. WASSERMAN: Well, the difficulty is  
9 that in order to get the bankruptcy protection  
10 under the U.S. law, you have to be going through  
11 an FCM and to a registered DCO. And so that's why  
12 that would not be practical with an exempt DCO.  
13 With respect to the FCM issue, the approach we've  
14 taken to this point, including with actually LCH  
15 for many, many years, has been essentially they  
16 have a two-strand approach. And so in other  
17 words, they have FCM members -- that is to say  
18 registered with us who would clear for U.S.  
19 Customers who would then get the U.S. bankruptcy  
20 protection, as well as anyone else who wants to  
21 come into the FCM -- they have what I think they  
22 refer to SCM, swap clear members, and those are

1 direct members of LCH, Ltd., and they are not  
2 registered with us. They clear for non-U.S.  
3 Customers, and they would then be resolved or  
4 liquidated under the appropriate local law. So  
5 that's the approach we've taken to sort of  
6 harmonize those things.

7 I guess my concern, I would note one  
8 other point. I do realize that there is the  
9 requirement that the CCP -- as I understand it in  
10 Europe, the CCP then does an assessment that its  
11 rules, including the bankruptcy provisions, can be  
12 essentially -- are reliable under local law. The  
13 concern I guess I would have, while speaking from  
14 a personal perspective, it's great to have that  
15 work done elsewhere, that the difficulty in  
16 actually reliably getting that assurance, in other  
17 words, trying to get, for instance, the opinions  
18 that I think we're agreed are very difficult to  
19 get out of lawyers, would simply be passed down to  
20 the CCP and we would then be faced with, I think  
21 ultimately, either requiring the CCP to do that,  
22 which may not be able to be done, or essentially

1 accepting something that the CCP does that says,  
2 well, here's the best we can do in the way of  
3 legal assurance and having to accept that. And so  
4 that's where it really does get sort of  
5 complicated, I guess, from my perspective.

6 MR. KLIEN: Just a quick comment. Go  
7 ahead, sorry.

8 MR. BAILEY: So I just wanted to comment  
9 on that, that direct point. Just to note that  
10 from a European perspective, as we've been going  
11 through the EMIR reauthorization process for  
12 European CCPs, we have managed to get that level  
13 of reassurance. Obviously, we haven't looked at  
14 it from a U.S. perspective, but we have managed to  
15 get that reassurance from CCPs and their legal  
16 advisors that they are able to operate their  
17 default rules. Otherwise, we wouldn't be in a  
18 position to be reauthorizing European CCPs.

19 MR. KLIEN: I just wanted to make a  
20 comment and then ask a question of the staff if I  
21 can.

22 The comment is I'd like to echo what

1 others have said about how important it is to  
2 solve for client clearing, but I also think there  
3 is a benefit in solving for house clearing because  
4 we've actually seen instances where a U.S.  
5 Participant transacting outside the U.S. with a  
6 non-U.S. Counterparty had an available  
7 clearinghouse, wanted to clear the trade, and was  
8 unable to do so because the clearinghouse said  
9 we're not a registered DCO and we don't want to  
10 register. So there is an incremental benefit in  
11 doing that.

12 I guess the question I have for the  
13 staff is if you turn the pages of your own  
14 rulebook, there are actually two existing models  
15 for how to handle customer funds for customers  
16 clearing outside the U.S. under part 30. One  
17 model is that if a jurisdiction or a firm has a --  
18 I forget whether it's a 30.2 or 30.4 exemption --  
19 the client can deal directly with a foreign  
20 intermediary and place its money with the foreign  
21 intermediary for clearance outside the U.S. And  
22 as part of that comparability determination, I

1 think, in fact, the staff does look at the  
2 customer protection regime of the relevant  
3 authority. So that's one model. And the other  
4 model is under 30.7, if a customer chooses to  
5 clear through a FCM, the FCM will hold the funds  
6 under a 30.7 protection regime and then use a  
7 foreign intermediary to clear for its client  
8 account.

9           And I guess my question is, is the staff  
10 not looking at those precedents because you feel  
11 you're unable to because of the way Title VII is  
12 drafted? Or do you feel that as a policy matter  
13 they're just not good examples?

14           MS. DIETZ: Well, I think basically it's  
15 because those are dealing with futures. Part 30  
16 deals with foreign futures. And swaps are neither  
17 domestic nor foreign as they're defined under our  
18 regulation. So I think we've used swaps, or at  
19 least have up to this point viewed swaps  
20 differently from futures that are traded on  
21 another -- a foreign exchange.

22           Bob, do you have anything to add?

1                   MR. WASSERMAN: I think that's right.  
2                   And I think that essentially -- because  
3                   essentially, the foreign futures are just that,  
4                   foreign futures. And then when you're having a  
5                   swap involving a U.S. counterparty, it's, I think,  
6                   a bit more difficult to characterize that as  
7                   foreign in quite the same way.

8                   MR. TURBEVILLE: As mentioned earlier,  
9                   in commenting on my earlier remarks, implicit was  
10                  the belief that there was U.S. regulation and then  
11                  worse regulation everywhere else. And I certainly  
12                  believe there's U.S. Regulation and different  
13                  regulation everywhere else. And it can be better  
14                  or worse, but one thing that is apparent from this  
15                  conversation, which is very consistent with my  
16                  experience. I was honored to spend five years  
17                  with Goldman Sachs in London working with your  
18                  predecessors, and so I have a certain appreciation  
19                  for how things are done in Europe. And in  
20                  discussion -- my experience has been in talking  
21                  about -- for instance, just taking it for example,  
22                  the clarity issues, clarity in the area of

1 bankruptcy is often greater under U.S. law than if  
2 you have to deal with jurisdictions plus the E.U.  
3 on top of it with many different levels of  
4 E.U.-ish on top of that. And that's different.  
5 Is it a better way of going forward? I like  
6 France. I like Germany. But it's undoubtedly  
7 almost definitionally more complex and less  
8 transparent and clear in terms of outcomes of law  
9 and outcomes of regulation. So I would like to --  
10 could you comment on that? Forgetting what the  
11 outcomes are, is it or is it not generally clearer  
12 when you're dealing with outcomes as compared if  
13 you have to deal with a more complex situation?  
14 Take for instance the E.U. and the member  
15 countries.

16 MR. WASSERMAN: I would -- certainly the  
17 experience I've had in bankruptcies is that things  
18 tend to work a bit more cleanly the less complex  
19 they are. I will say that my nightmare has been  
20 waking up and basically having a judge say, when  
21 we're trying to get customers moved and trying to  
22 get money moved in that first day or two after a

1 bankruptcy and we've arranged for a transfer, and  
2 having the judge say, "Well, somebody has raised a  
3 very interesting and complex issue. Let's set up  
4 a briefing schedule." Because what we have seen  
5 under U.S. law has been, you know, even in a case  
6 like MF Global, where customers had definitely not  
7 gotten all that they were due when it was due to  
8 them, was the ability to transfer substantial  
9 amounts and do so very, very quickly and very,  
10 very efficiently. And I think while others have  
11 noted there are some very real concerns about the  
12 pro rata approach, the pro rata approach, and I  
13 think with the addition of LSOC, does make it very  
14 practicable to transfer on a bulk basis and do so  
15 very efficiently. And that's been the experience.  
16 And I'm not sure experience elsewhere has been  
17 quite as smooth.

18 MS. COHEN: So I agree with many of the  
19 comments that have been made about the importance  
20 of customer clearing being the key issue here, and  
21 I would just love to return for a couple of  
22 minutes to the point that was made a few minutes

1       ago which I thought was excellent about part 30  
2       and the futures model. And I guess for me I  
3       wouldn't be so quick to dismiss the relevance  
4       because they're swaps, not futures. I think the  
5       issue of customers seeking access in non-dollar  
6       markets is actually quite similar, and I think  
7       that these are such complex issues that the power  
8       of having certain models in place that have been  
9       tested and have worked in futures shouldn't be  
10      underestimated. And I think that looking to the  
11      part 30 model is, you know, would be a very, very  
12      good exercise.

13                   MS. PORTNEY: For what it's worth, that  
14      was actually the exact same point I was going to  
15      make. I think we're trying to solve for so many  
16      different things here, and right now what you have  
17      is that U.S. persons, you know, obviously cannot  
18      clear in a foreign market unless that market is  
19      registered as a DCO or there's this exemption  
20      process. So I think we all agree that having a  
21      framework around the exemption process is very  
22      important for the path forward, but secondarily,

1 as we're pointing out, that still wouldn't solve  
2 for the issue that every U.S. person must interact  
3 through or must transact through a U.S. FCM. The  
4 part 30, you know, process would allow -- would  
5 actually allow an intermediary, which again would  
6 be a much more efficient process and I think very  
7 futures-like. And I think there are a lot of  
8 benefits and the model is already there to allow  
9 that. So I would encourage the Commission to  
10 truly think about that.

11 And then as far as customer assets and  
12 segregation, again, taking even then a step  
13 further to think about the 30.7 account class and  
14 having some similar type of account model for  
15 swaps perhaps, but I think there is a roadmap  
16 that, yes, it absolutely pertains to futures right  
17 now but one that certainly could be informative as  
18 we look to solve very similar issues.

19 MS. DIETZ: And again, we have looked at  
20 that and considered that, but we're happy to, in  
21 light of the comments today, go back and revisit  
22 that.

1 Yes?

2 MS. TAYLOR: Is one of the  
3 considerations that would have to be part of that  
4 determination though to use 30.7 the fact that --  
5 I think the Commission has taken care to isolate  
6 the futures customers from the risks that come  
7 from the swaps trading. And so I would think that  
8 that would occur if you blended it into the 30.7  
9 unless you went with a similar parallel structure.

10 MS. DIETZ: It would have to be a  
11 parallel structure. And among the things that we  
12 have discussed internally is whether or not if you  
13 were going to go ahead with customer clearing, if  
14 you'd actually have to have a new account class.  
15 Because we've just done a rule-making that said in  
16 30.7 that's only for foreign futures and options.  
17 You know, we used to be able to put OTC  
18 transactions positions in there and that's no  
19 longer the case. So there is legal engineering  
20 that would have to take place, and we would have  
21 to kind of walk through that. And in a very  
22 detailed way if that's the path that we want to

1 take. Again, while none of these things is  
2 perhaps impossible, the fact is I would not  
3 dismiss the distinction between foreign futures  
4 and swaps. The legal construct that we're talking  
5 about here is that when you have the sufficient  
6 nexus with a U.S. person, we regulate the  
7 execution and clearing of that product. And there  
8 is no legal disagreement that we don't regulate  
9 foreign futures. So there is an additional legal  
10 hurdle, and again, maybe it's just a matter of  
11 engineering. But we're not dealing with exactly  
12 the same thing. So there is a level of complexity  
13 that, you know, we are aware of, and as a policy  
14 matter, if we go down that path, well, we'll just  
15 deal with the complexity.

16 Yes?

17 MS. VEDBRAT: So, you know, when we're  
18 looking at which DCO CCPs to join and which  
19 markets to invest in, we'll look at it across  
20 three different dimensions. One is like the  
21 liquidity pools that are available, customer asset  
22 protection, as well as, especially in the swaps

1 world, any type of new operational risk that may  
2 be introduced, and as we're having these  
3 discussions, the complexity of separating out U.S.  
4 person customers from certain DCOs versus others,  
5 it just adds a level of complexity that on the buy  
6 side is somewhat difficult to be able to execute  
7 again. So I'd just like to consider that.

8           The other thing is that there will be  
9 certain DCOs which may not be U.S.-based, may not  
10 want to register in the U.S. but have the maximum  
11 amount of liquidity, maybe in different time  
12 zones. So we may be disadvantaging U.S. Persons  
13 or U.S. customers by putting in a policy or a rule  
14 that does not allow customer clearing through  
15 those DCOs. So that's just, you know, if you  
16 could take that as a point of consideration. And  
17 then, you know, as we're talking about the  
18 segregation models, you know, if these DCOs were  
19 to offer full segregation, you know, maybe that  
20 could be taken as a point of consideration to be  
21 somewhat similar to LSOC.

22           David, I know that that doesn't address

1 your concern, you know, the other way around but,  
2 you know, as we're thinking about this exemption,  
3 if we could just take that as a consideration  
4 around the customer clearing element.

5 CHAIRMAN WETJEN: Supurna, you mentioned  
6 that you look at this in three dimensions, one of  
7 them being the customer protection afforded in a  
8 particular jurisdiction or trading venue. So I  
9 presume that has to involve some assessment of the  
10 bankruptcy protections, but to what degree does  
11 your analysis include that? And how does it  
12 relate to assessments about costs around  
13 individual seg? So help me understand that a  
14 little bit better.

15 MS. VEDBRAT: I mean, so when we look  
16 at, you know, customer protection there could be,  
17 you know, elements that are within our investment  
18 management agreements that may not allow any type  
19 of cross-border. So that would just, you know,  
20 for a U.S. person I think we've shared that for  
21 certain CCPs. You know, we can only use them if  
22 they are U.S. registered DCOs.

1                   From a bankruptcy regime perspective, if  
2                   you had individual seg, for certain types of our  
3                   investment vehicles, you know, it would be the  
4                   pension plans or what have you, regardless of  
5                   cost, you know, that may be the preferred choice.  
6                   And then, you know, for the rest of, you know, the  
7                   segregated models, we worked very closely with Bob  
8                   Wasserman on LSCO, and we felt relatively  
9                   comfortable that the amount of protection, as well  
10                  as, you know, the oversight that both the  
11                  Commission as well as BlackRock would have from an  
12                  oversight perspective, we felt pretty comfortable  
13                  looking at that as an alternative on providing,  
14                  you know, the right level of asset protection, as  
15                  well as operational efficiency.

16                  In Europe, we don't have that available  
17                  and, you know, to some extent, you know, that's a  
18                  little bit of a road block for us to move forward  
19                  because you have LSOC, you have individual seg,  
20                  and you have Omni, but it's not clear that the  
21                  individual seg is being offered in an efficient  
22                  manner.

1                   CHAIRMAN WETJEN: So it's the  
2 operational challenges that you're running into  
3 when you're looking at whether or not to avail  
4 yourselves of individual seg in jurisdictions like  
5 Europe?

6                   MS. VEDBRAT: Yes. You know, and I  
7 mean, obviously, you know, we don't have the  
8 mandate, you know, in play right now, so we are  
9 taking our time to make sure that we are  
10 considering the three elements that I mentioned.

11                   And ours would be -- it's not only the  
12 CCP level because, you know, as a customer and  
13 user, you know, we obviously access the CCP  
14 through an FCM or an SCM, so we have to look at  
15 it, you know, through both sets of flow.

16                   CHAIRMAN WETJEN: Because I think this  
17 operational challenge issue is something that  
18 probably informs one of the other considerations  
19 we have to make in deciding what to do here. And  
20 that, again, is considerations about  
21 competitiveness. And so we need to think through  
22 what kind of an effect would making an exemption

1 or providing relief there will that have in terms  
2 of how one clearinghouse competes with the other.  
3 And it sounds like this operational challenge is a  
4 significant one that people need to think about,  
5 at least on the buy side.

6 MS. VEDBRAT: But also the liquidity  
7 component is important because if you eliminate or  
8 you restrict U.S. Person customer from being able  
9 to clear, you know, in these DCOs, I think that  
10 that could be a disadvantage or at least to the  
11 U.S. customer. And in the event also, you know,  
12 where you may have a majority of available  
13 liquidity in one of these foreign DCOs that choose  
14 not to register.

15 MS. DIETZ: I think these last remarks  
16 are a nice segue into one final topic as we -- I  
17 see the clock ticking, and this circles back to  
18 something that the acting chairman mentioned at  
19 the very beginning, and that is concerns about  
20 competition. And the impact that the proposal, as  
21 I have outlined for you today, has on competition  
22 as between really any market participants --

1 between clearinghouses, registered clearinghouses,  
2 exempt clearinghouses, duly registered  
3 clearinghouses, you know, clients, customers. And  
4 if anyone has any -- you know, I've heard -- taken  
5 some notes on particular disadvantages here and  
6 there, but if anyone has any particular remarks  
7 they'd like to share about competition of any type  
8 as a result of the proposal as it stands now.

9 Kim?

10 MS. TAYLOR: My competition concern is  
11 not so much directly related to any specific  
12 element of the proposal. My competition concern  
13 is related to the fact that in listening to the  
14 discussion about such a proposal or the broader  
15 discussion about mutual recognition across  
16 jurisdictions and perhaps even globally so that  
17 customers and intermediaries and clearinghouses --  
18 clearinghouses and intermediaries can serve  
19 customers in various ways, which I think is a good  
20 goal, that to me is feeling like it is not  
21 something that is going to be definitively solved  
22 in the very short term. And the serious

1 competitive issue that is in place right now and  
2 live and active right now for all exchanges and  
3 clearinghouses that are not located on European  
4 soil is the fact that on December 15th, European  
5 persons will no longer be able to trade or clear  
6 futures outside of European soil without having  
7 them treated like bilateral swaps and the  
8 regulatory capital requirements just explode.  
9 That is a serious competitive issue and it is  
10 something -- the certainly -- the lack of  
11 certainty around that is already starting to have  
12 an effect on end customers decision-making around  
13 where they might want to trade, where they might  
14 want to clear, and my concern is that there's been  
15 kind of no discussion about trying to solve for  
16 that part of the problem on a faster path than  
17 solving the broad global mutual recognition  
18 regime. And particularly, I would like to  
19 reiterate the case for the fact that the CFTC,  
20 with all of the various types of part 30  
21 exemptions, has a very hands-off approach to the  
22 trading of futures and clearing of futures by U.S.

1 customers in foreign jurisdictions, and there's no  
2 move to have a corresponding acknowledgement of  
3 that coming the other way from Europe in a  
4 timeframe that is not going to be harmful to not  
5 only -- this is an issue that affects not only  
6 U.S. exchanges and clearinghouses; it affects  
7 exchanges and clearinghouses in every jurisdiction  
8 that is not in the E.U.

9 MR. RAMASWAMI: You know, I would echo  
10 Kim's comments that the uncertainty around this  
11 can create more harm because it's been a series  
12 of, I guess, the deadline being extended every  
13 time you get close to the deadline. Right? So  
14 now the people assume that it will always keep  
15 getting extended, and if it doesn't get extended  
16 for whatever reason, you'll have, you know, a  
17 calamitous few days in terms of people adjusting  
18 to the fact that it didn't get extended. So  
19 that's one worry.

20 And the second worry about this is, of  
21 course, you know, by making it extremely complex  
22 for U.S. persons to access overseas creating

1 capabilities, what happens over time is that you  
2 will have unnatural concentrations of risk in one  
3 or two clearinghouses in time zones that are far  
4 away from where the risk needs to be managed in  
5 the case of an event. So you would have, you  
6 know, not market operating times during which  
7 you're going to have to deal with issues that are,  
8 you know, again, you have pretty large positions  
9 that will build up over time. I think the  
10 relative sizes of the capital markets between the  
11 U.S. and Europe and let's say Asia, it's pretty  
12 clear that if segregation were to happen as, you  
13 know, it can in a worse case, you would have  
14 concentrations of Asian exposures lying in Europe  
15 and in the U.S., which will not be able to react  
16 because of the time zone differences, and that in  
17 itself will have outcomes which are not quite  
18 desirable.

19 So those are the two issues that one  
20 worries about in complexity. And I think, again,  
21 the point that Emily and you made earlier about  
22 looking for parallels which have worked has a lot

1 of appeal and is something that people will be  
2 able to adjust to and work with easier than, you  
3 know, any other kind of solution.

4 COMMISSIONER O'MALIA: I would -- to  
5 Rama's point and to Kim's point, you'd be  
6 interested to know it's 142 days from today that  
7 the European clearing mandate or the determination  
8 of December 15th and European clearing  
9 determination of U.S. CCPs is required. Whether  
10 we have an exempt DCO with customer clearing or  
11 not customer clearing, we've simply run out of  
12 time. We need to proceed kind of in an  
13 expeditious fashion to harmonize our rules at this  
14 point and figure out what it's going to take to  
15 make sure that we can get the recognition for not  
16 only the U.S. but whether it's going to be  
17 Singapore or Japan or the other entities that are  
18 seeking recognition that have met the PFMI's. I  
19 think it's time and we need to set some dates  
20 between our governments to sit down and hammer out  
21 these issues because the proposals and getting  
22 comment and redrafting and considering, we don't

1       have enough time to address this and to get the  
2       outcomes that we're hoping to achieve or that  
3       we've all considered. And I think if the staff  
4       recommendation is a member clearing only, you  
5       know, there are a lot of concerns about that, I  
6       think we need to refocus our efforts on  
7       harmonizing our rules.

8                     And David, that's pointed at us and  
9       pointed at you, if you could take that message  
10      back, that it's name the time and the place and  
11      we'll be there.

12                    MR. BAILEY: Just on that, Commissioner  
13      O'Malia, I would agree. And I don't think we  
14      should leave the committee members around the  
15      table underestimating the amount of discussions  
16      that are taking place between the regulators to  
17      get to a harmonized and sensible position. There  
18      has been more collaboration over the last 24 to 36  
19      months on these markets than I've ever seen  
20      before. I think that's positive, and that gives  
21      me comfort that we can get to a sensible place in  
22      the timeframe that we need to.

1                   CHAIRMAN WETJEN: Let me just add, you  
2 know, based on the discussion this morning, I  
3 think there's willingness to resolve this  
4 certainly before December 15th. That's my  
5 impression. Whether we get there remains to be  
6 seen, but I think that's certainly a shared goal.

7                   With that, we should probably -- well,  
8 I'll turn it over to Ted to tell us to tell us to  
9 break for lunch.

10                  MR. SERAFINI: Well, we can break for  
11 lunch now but there are two more comments, if you  
12 guys want to make.

13                  Stephen?

14                  MR. O'CONNOR: Yeah. Sorry, I'll be  
15 very quick. So just one response on the  
16 competition question. Two barriers the proposal  
17 seems to erect I think are the fact that foreign  
18 DCOs will continue to find it hard to access U.S.  
19 clients. Maybe that's the intent, but I don't  
20 think that's consistent with G20 and FSB goals to  
21 avoid fragmentation. And the second barrier is  
22 that U.S. Clients will find it potentially hard

1 to transact with the U.S. with foreign DCOs. So  
2 both sides of that coin.

3 But then a sort of technical question.  
4 Going back to what I said earlier, the entity  
5 versus jurisdiction approach. I'd be quite  
6 interested to hear, Phyllis, why you went down  
7 that road, and I'm thinking partly because the  
8 statute provides the exemption route in the CEA.

9 And then a question for Acting Chairman  
10 Wetjen, you mentioned competitiveness being in the  
11 statute also. Does that give you some wiggle room  
12 to go more towards a jurisdictional than an entity  
13 approach?

14 MS. DIETZ: In response to your  
15 comments, first of all, while I think we are aware  
16 of the competitive issues related to -- and we  
17 have, you know, grappled with the customer  
18 clearing, no customer clearing issue -- there is  
19 always an alternative, and that is for a  
20 foreign-based ECO to register. And then the whole  
21 customer-clearing issue goes away.

22 We do have Singapore Exchange, LHC - two

1 LHCs. We have ICE Clear Europe, and even the  
2 Natural Gas Exchange in Canada -- though some  
3 people don't think that's foreign, but it is.

4           So, the U.S. is a jurisdiction that  
5 permits clearinghouses that are not organized in  
6 the United States to register and be fully  
7 registered. So, I also don't want to lose the  
8 perspective of that. But, you know, we're all for  
9 efficiency in the markets. You know, I don't need  
10 duplicative regulation. I got enough regulation.  
11 I, you know, work long enough hours.

12           So, I think we all have the same goals,  
13 but let's not lose sight of it's not a matter of  
14 either I get customer business -- from the  
15 clearinghouse's perspective. Either I have  
16 customer business, or I don't. Well, if you  
17 register, you can have it.

18           The other thing -- in terms of the --  
19 looking at the individual clearinghouse, versus  
20 just the structure -- while the statute is written  
21 in terms of the regulatory framework, we do think  
22 it's important to look at the individual

1 clearinghouse to get these certifications from the  
2 home country regulator, to look at their  
3 assessment, to make sure that, indeed, it's not  
4 just the framework, but it's actually the  
5 clearinghouse that -- and this is an eligibility  
6 requirement -- that is actually complying.

7           And so that's the only reason, you know,  
8 we've done it that way -- because we see it as  
9 twofold. And as an analog to our registration  
10 process, let's look at the individual entity.

11           But I would say in terms of the, you  
12 know, application process, which would be  
13 individualized, it's basically the disclosure  
14 framework. So, it's not that -- in itself, it's  
15 not a heavy lift.

16           MR. O'CONNOR: But on the theme of  
17 avoiding double regulation, David's already done  
18 all that homework. So, for you to go in again and  
19 do similar stuff -- isn't that a double burden?

20           MS. DIETZ: Well, we're not actually  
21 doing the same thing. The disclosure framework's  
22 already been developed. There's already a

1 regulatory scheme. And, to a great extent, we are  
2 relying on the home country regulator's oversight  
3 and their certification.

4 So, I think that the continuing -- like  
5 the reporting obligations -- those are the kinds  
6 of things that we feel we need to discharge our  
7 responsibility for our own market oversight.

8 So, it's not so much that daily  
9 reporting of margin on deposit is not supervisory  
10 in nature; it's to help us look at the clearing  
11 member. They also operate in the U.S. markets --  
12 and to help us understand the risk profile of  
13 entities that we may regulate and that have a  
14 significant impact on, you know, our markets.

15 So, we're not the supervisor --

16 MR. SERAFINI: Can I ask a -- do we send  
17 people out to -- for exempt DCOs, or those that  
18 are operating under no-action relief -- will we  
19 send CFTC staff to inspect books and records, or  
20 are we just simply relying on reports?

21 MS. DIETZ: Yes and no. We want to have  
22 authority to do that, if it is necessary. But it

1 is the staff expectation -- and I'll say "staff"  
2 very carefully -- it's the staff expectation that  
3 we will not make routine on-site visits, and --

4 MR. SERAFINI: Routine or house calls?

5 MS. DIETZ: Well, on-site visits at all.  
6 I mean, we have a full plate making --

7 MR. SERAFINI: More than a full plate.

8 MS. DIETZ: More than a full plate  
9 visiting and overseeing the clearinghouses that  
10 are fully registered with us. So, I think the --  
11 while we want to have the ability to do it, I  
12 don't envision that, because I don't know whose  
13 staff is going to do it.

14 So, I think the answer to your question,  
15 as a practical matter, is no.

16 MR. SERAFINI: Well, I mean -- but if  
17 we're -- to Stephen's point and to David's point  
18 -- if they're doing the job, when do we not --  
19 when do we give up the job, and rely on their  
20 regulatory -- I mean, we haven't been that brave  
21 in terms of substituted compliance thus far,  
22 however -- and maybe if Gary Barnett is here --

1 will we be sending people to inspect swap dealers  
2 overseas currently? These are the same entities  
3 we've given substituted compliance.

4 I'm just a little concerned about how  
5 thin we're going to be stretched if we insist on  
6 double-checking the regulators we've given  
7 substituted compliance to.

8 MS. DIETZ: Mm-hmm. Well, I would make  
9 a fine legal distinction between substituted  
10 compliance and an exemption. Substituted  
11 compliance, meaning you're required to comply with  
12 our laws and rules, but we're going to allow  
13 compliance with this other regime to substitute  
14 for that.

15 That's not what this exemption is about.  
16 The exemption is, you would be subject to our  
17 regime, but we're giving you a pass with these  
18 certain conditions. And we are largely relying on  
19 the other regulator. I mean, that's one of the  
20 fundamental premises. Somebody else is doing this  
21 job. We're going to allow them to do it.

22 But we do not, as envisioned by the

1 staff, give up 100 percent responsibility for  
2 everything. But as a practical matter, we're not  
3 going to go visit them. We would sooner terminate  
4 the exemption.

5 If we think that -- and this is the  
6 staff's vision -- if this clearinghouse is in  
7 trouble, and we talk to the regulator under our  
8 MOU or similar arrangements, and they say, yeah,  
9 they are in trouble, we can terminate the  
10 exemption, and we're done. We're not going to  
11 work with them. We're not going to examine them.  
12 We're not going to issue an examination report.  
13 We don't review their rules when they're filed,  
14 you know.

15 They're not really on our bus, but they  
16 sort of are. And we have a continuing interest in  
17 a way that is very, very minimal, compared to what  
18 we would do for registered DCO.

19 MR. O'CONNOR: Sorry. And I guess I  
20 didn't phrase -- my question I was trying to raise  
21 before -- entity versus jurisdiction -- probably  
22 was better phrased, why exemption, rather than

1 full substituted compliance?

2 MS. DIETZ: And I think it's basically  
3 because that's how we read the statute. And to  
4 the extent that U.S. Persons trading swaps are  
5 within our jurisdiction, we would exempt them from  
6 the requirements that would otherwise be imposed.  
7 So, the statutory language is exemption, so that's  
8 why we have stuck to it, in terms of the legal  
9 construct.

10 I think, though, as a practical matter,  
11 I'm not sure that, at the end of the day, there's  
12 any real difference, because it's really the home  
13 country regulator that is going to be supervising  
14 this entity. And the fact that we get  
15 information, or a certification once a year, or  
16 they tell us if there's been a clearing member  
17 default -- of a U.S. clearing member doing swaps  
18 business -- that doesn't make us the supervisor.

19 And my own view is, I don't consider the  
20 CFTC to be the supervisor -- or even secondary  
21 supervisor -- of an exempt DCO. They're exempt  
22 from our requirements, except for certain

1 conditions that we're going to impose, which are  
2 permitted under a statute.

3 So, I think that's how we're reading the  
4 law.

5 MS. ADRIANCE: And, Stephen, just to  
6 give you -- if what you're concerned about is kind  
7 of a fairness issue -- why the CFTC is imposing it  
8 on a clearinghouse and somebody else might not be  
9 -- I can give you our experience with the European  
10 jurisdiction.

11 It's a two-step process. There is an  
12 equivalence determination that's made at the  
13 European level, and then there is an individual  
14 clearinghouse process of review that is -- I mean,  
15 our submission to ESMA for this review amounted to  
16 thousands of pages of documentation. So, it  
17 certainly is not a situation where going one way,  
18 it's a free pass, and going the other way, it is,  
19 you know -- you have to submit your PFMI  
20 compliance report.

21 The regime in Europe is a two-step --  
22 and, actually, the second step -- the

1 clearinghouse-specific step -- is much more  
2 onerous than the process that Phyllis is  
3 describing.

4 MR. SERAFINI: Mark, did you want to say  
5 anything?

6 CHAIRMAN WETJEN: Stephen, I'd love to  
7 answer your question, but we're overdue for lunch.

8 MR. SERAFINI: Chris, the crowd looks a  
9 little eager to get out of here, but would you  
10 like to close us out with any remaining comment?

11 MR. ALLEN: Okay, I shall be very brief  
12 then. I'm just going to make two very brief  
13 points.

14 The first is, I think, in relation to  
15 the contemplation of any client-related business,  
16 are there not possibly limits, quite  
17 fundamentally, going forward? The capacity for  
18 dual registration to be the solution -- because I  
19 think those fundamental conflicts associated with  
20 account segregation, whether it's Article 39  
21 (inaudible) and the interaction with the various  
22 elements of the U.S. Bankruptcy Code -- I mean, I

1 think the prospects for client activity relying on  
2 dual registration is a short-lived solution.

3           The second point, which is just to pick  
4 up another point that Kim made, relating to the  
5 European perspective for the recognition of  
6 non-E.U. CCPs -- I would just like to reiterate  
7 that, to the extent that there is any obstacle in  
8 terms of the satisfactory resolution of that  
9 dialogue between the CFTC and the European  
10 Commission -- which may have its origin in any  
11 kind of miscommunication regarding what the  
12 Europeans are looking to see from the CFTC -- I  
13 would very much encourage that that now be removed  
14 as soon as possible -- because whilst we have just  
15 seen the deadline pushed back to December, in  
16 terms of, fundamentally, what it's going to be,  
17 the regulatory capital consequence of that  
18 determination landing fully.

19           It was originally set for this June, and  
20 the period between now and December, of course, is  
21 quite short. More fundamentally, the deadline is  
22 not really December, because firms and

1 institutions need to know the direction of travel  
2 well ahead of December 15.

3 The consequences, from a regulatory  
4 capital perspective, as Kim alluded to, are not  
5 trivial. They're absolutely devastating in terms  
6 of the impact on the market if that dialogue is  
7 not resolved successfully.

8 Thanks.

9 MR. SERAFINI: With that, thank you,  
10 Phyllis, for presenting. Thank you, Bob  
11 Wasserman, for also joining the conversation.

12 We'll break for lunch and reconvene at  
13 1:30. There's lunch available for the GMAC  
14 members upstairs, also.

15 (Recess)

16 MR. SERAFINI: Good afternoon,  
17 everybody. I'd like to call the GMAC meeting back  
18 to order. We have a second panel today, to talk  
19 about the regulation of foreign- based SEFs.

20 We have, joining us, some CFTC staff.  
21 We have Vince McGonagle, the Director from the  
22 Division of Market Oversight, David van Wagner,

1 the Chief Counsel from DMO, and Riva Spear, the  
2 Senior Special Counsel from DMO, as well.

3 So, with that, Mark, do you have any  
4 comments you want to make at the beginning here,  
5 before we turn it over to the panel?

6 CHAIRMAN WETJEN: Just one real quick  
7 comment -- I alluded to it earlier -- this  
8 morning, at the beginning of the meeting. We have  
9 in place an interim solution for these trading  
10 venues overseas -- and London, in particular. But  
11 we've always viewed it as an interim solution.

12 I see on the screen here there's a  
13 recitation of the statutory provision that gives  
14 us the authority to provide this status for  
15 offshore trading venues. And so it's been the  
16 plan for a number of months now that we would  
17 follow up the interim solution with a more  
18 permanent solution, if you will.

19 Staff has been working very hard on  
20 that. We've discussed a preliminary terms sheet  
21 on what this kind of regime might look like.  
22 David, and Vince, and Riva will get into more

1 detail there about what the current thinking is on  
2 the part of the staff.

3 But we're, as with the morning session,  
4 looking forward to input from this group, to  
5 further clarify our thinking on how we might  
6 approach this.

7 The other quick comment I'll make is  
8 that we have a couple of people around the table  
9 here who have very, very unique perspectives, I  
10 think, on this -- and so looking forward to  
11 hearing some comments from them. By that, I mean  
12 the platform operators who sort of wrestle with  
13 this and our rules, and have tried to sort out  
14 market solutions that are legal ones in both  
15 jurisdictions where they operate.

16 So, looking forward to the session, and  
17 thanks.

18 MR. SERAFINI: And, again, this  
19 afternoon, we also have Jun Mizuguchi and David  
20 Bailey joining us for the second panel, too.

21 But with that, I'll turn it over to the  
22 CFTC staff, to give their opening remarks.

1                   MR. VAN WAGNER: Thanks very much. I'm  
2 David van Wagner, from the Division of Market  
3 Oversight.

4                   Shortly after the Commission adopted its  
5 swap execution facility rules, CFTC Chairman Gary  
6 Gensler and Michel Barnier --

7                   CHAIRMAN WETJEN: David, move the mic  
8 up, please.

9                   MR. VAN WAGNER: Oh, really? Okay. Is  
10 it better? Okay. Shortly after the SEF rules  
11 were adopted in May 2013, CFTC Chairman Gary  
12 Gensler and Michel Barnier, from the European --  
13 the European Commissioner for Internal Markets and  
14 services announced a path-forward statement,  
15 reflecting their joint understanding of how to  
16 approach cross-border regulation of derivatives.

17                   This path-forward statement provided  
18 that if the CFTC's trade execution mandate -- the  
19 mandate by which swaps that are subject to our  
20 clearing mandate and have been made available for  
21 trading on a SEF or a DCM -- if it became  
22 effective before March 15 of 2014, the CFTC would

1 write no- action letters to provide relief to  
2 certain European- regulated multilateral trading  
3 facilities -- or MTFs, and provided that those  
4 platforms were subject to a sufficient of pre- and  
5 post-trade price transparency requirements,  
6 comparable provisions providing for  
7 nondiscriminatory access by market participants,  
8 and an appropriate level of governmental  
9 oversight.

10           The CFTC's trade execution mandate  
11 indeed became effective on February 15, 2014, with  
12 respect to certain interest rate and credit  
13 default swap contracts that were determined to be  
14 made available in trade.

15           So, in fulfillment of the Commission's  
16 path- forward commitments, the Division of Market  
17 Oversight and the Division of Swap Dealer and  
18 Intermediary Oversight issued, on February 12th, a  
19 no-action letter offering conditional relief for  
20 qualifying MTFs, from the SEF registration  
21 requirements, and, also, for parties that were  
22 executing swap transactions on these qualifying

1 MTFs, they would be relieved from the trade  
2 execution mandate to the extent that they trade  
3 execution mandate swap.

4 The conditions for relief that were  
5 imposed on the MTFs generally track the purposes  
6 underlying the path- forward statement. And so  
7 they included things such as to promote pre-trade  
8 price transparency, the qualifying MTF would have  
9 to use an order book or an order book plus an RFQ  
10 trading system for execution of swaps subject to  
11 the trade execution mandate.

12 To promote post-trade price  
13 transparency, the qualifying MTF would have to  
14 report all the swaps executed on the platform to a  
15 CFTC-regulated swap repository or a  
16 provisionally-registered SDR.

17 The MTF would also have to provide  
18 nondiscriminatory access to its platform in a  
19 manner that was comparable to the CFTC's impartial  
20 access requirements.

21 In addition, the MTF would have to have  
22 an appropriate level of trade practice oversight.

1 And I should stress that each of these conditions  
2 -- the substantive MTF requirements -- would have  
3 to be grounded or based on home country  
4 regulations or requirements versus the MTF self-  
5 imposing the requirements on themselves.

6 On April 9th, the Division of Market  
7 Oversight and the Division of -- DSIO -- revised  
8 the MTF relief letter to adjust certain other  
9 requirements, but the original February 12th  
10 letter -- and they were tweaked in a fairly small  
11 regard, I guess. To date, we haven't granted any  
12 relief to any MTFs under this letter.

13 So, an important note to add -- and that  
14 is that the MTF no-action letter was intended to  
15 provide transitional relief until the Commission  
16 adopted a formal SEF exemptive category for  
17 foreign-based platforms, as was anticipated in the  
18 Commodity Exchange Act.

19 Accordingly, relief under the MTF  
20 no-action letter would expire with the adoption of  
21 the SEF exemptive category rulemaking, which Riva  
22 Adriance will discuss and pose questions around.

1           I've spoken here only about the  
2 path-forward and only about MTFs. But in addition  
3 to that, staff has also reached out to a number of  
4 other foreign regulators who would be potentially  
5 interested in the same basic framework of the MTF  
6 no-action letter that we issued. We're still  
7 having discussions around the possibility of using  
8 that template elsewhere. So, there might be more  
9 to follow.

10           But that's really it on the MTF  
11 no-action letter, segueing to the exempt SEF  
12 rulemaking.

13           MS. ADRIANCE: Thank you. Thank you,  
14 David. I don't know if this is close enough --  
15 try and do this without pulling it out of the plug  
16 -- okay.

17           All right. As was mentioned, there is  
18 the act- provided authority for going forward with  
19 more than just a no-action letter -- but something  
20 more permanent. Maybe this will help.

21           And it's on here. I'm trying to figure  
22 out how I can get this up. We do have the

1 statutory language, if we can somehow get it up  
2 there. I don't know if anyone can read this, but  
3 the reason I wanted to actually have it posted up  
4 here is because -- thank you -- because the  
5 language is -- many times, people will mention  
6 that there's this authority for the Commission to  
7 exempt swap execution facilities under certain  
8 conditions and under certain circumstances.

9           But, very often, the details of that  
10 authority are not necessarily understood. And so  
11 I want to just -- you know, this is something that  
12 was discussed this morning by -- Phyllis discussed  
13 the statutory authority for exempting derivatives  
14 clearing organizations.

15           And this -- if you look at this statute  
16 -- the statutory language up here -- you'll see  
17 that, similar to the Commission's exemptive  
18 authority discussed this morning, Section 5H(g) of  
19 the Commodity Exchange Act provides the Commission  
20 with authority to exempt, conditionally or  
21 unconditionally, a swap execution facility from  
22 registration, if certain conditions are met.

1           In order to grant an exemption to a  
2 foreign-based swap execution facility, this  
3 statutory authority requires the Commission to  
4 make a finding -- to find that the foreign-based  
5 swap execution facility is subject to comparable  
6 comprehensive supervision and regulation on a  
7 consolidated basis by the appropriate governmental  
8 authorities in the home country of the facility.

9           So, the Commission has to -- has a  
10 certain standard that is required that the  
11 Commission set out here. And I want to point out  
12 that this exemptive authority, as I said, closely  
13 mirrors the Commission's exemptive authority to  
14 exempt from registration under certain conditions  
15 some foreign derivatives clearing organizations.  
16 And both provisions provide that the CFTC may do  
17 so conditionally or unconditionally.

18           In addition, both provisions contain a  
19 substantially similar requirement that, in order  
20 to provide this exemption, the CFTC must make a  
21 finding. And so, therefore, that limits under  
22 what conditions we can provide that exemption.

1           To repeat a point that Phyllis made this  
2 morning, the finding required of the Commission  
3 focuses on the regulator and the regulatory  
4 requirements imposed by that regulator, rather  
5 than focused on the foreign-based swap execution  
6 facility. So, the basic standard goes to the  
7 regulator and the regulatory scheme.

8           Due to the fact that this is a parallel  
9 statutory authority to that of the authority  
10 provided to the Commission in connection with  
11 clearing organizations, the exempt staff  
12 rulemaking team -- and we do have a team, and we  
13 have a team from across the Commission -- this  
14 team expects that the proposal it eventually  
15 provides to the Commission for consideration  
16 would, in many ways, track any exempt DCO  
17 rulemaking that the Commission would approve for  
18 publication.

19           So, for example, similar to an  
20 eligibility requirement mentioned by Phyllis  
21 earlier -- and was also kind of mentioned by some  
22 others -- the rulemaking team expects to propose

1 an eligibility requirement that a memorandum of  
2 understanding or other similar arrangement was in  
3 effect between the Commission and the home country  
4 regulator.

5 As was mentioned this morning, there  
6 needs to be a mechanism for good communication  
7 coordination. So, in a similar way, we would  
8 expect a number of those kind of basic,  
9 structural, administrative kind of proposals would  
10 be very similar.

11 However, the Commission faces an  
12 important difference in the application and in the  
13 staff context, in terms of making this finding  
14 that this home country regulator has comparable,  
15 comprehensive supervision and regulation. So,  
16 this standard is under the direct proposal  
17 discussed this morning.

18 When Phyllis was discussing the standard  
19 to be used in clearing organizations, she was able  
20 to turn to a standard that regards -- the  
21 regulatory framework that was consistent with the  
22 principles for financial markets infrastructure --

1 the PFMI, which, as you all know and was  
2 mentioned, was something that would establish the  
3 joint international efforts. The Commission was a  
4 key contributor to those efforts, and it currently  
5 serves as a member of the -- okay, this is less my  
6 familiarity -- the CPSS-IOSCO taskforce that  
7 monitors implementation of the PFMIs.

8 Okay, and in terms of that -- so the  
9 Commission has -- since the adoption of the PFMIs,  
10 the Commission's amended its regulations to  
11 establish regulatory standards that are fully  
12 consistent with the PFMIs. And so in this way,  
13 the Commission has been treating, you know, my  
14 language as another division. So, this is  
15 (inaudible) but my language is that this is being  
16 viewed as the PFMIs are comparable to the  
17 supervisory and regulatory framework established  
18 by the (inaudible) regulations -- and, therefore,  
19 comprehensive, consistent with the requirements of  
20 Section 5B(h) of the Act -- or similar to what we  
21 require for derivatives clearing organizations.

22 So, there was a standard that the

1 Commission could adopt and use as a standard for  
2 making that determination as to whether the  
3 particular foreign clearing organization was  
4 supervised by an appropriate regulator that met  
5 the standard required under the Act.

6 Okay, so that's a great tool that they  
7 had. Unfortunately, the regulatory framework  
8 applicable to swap execution facilities under the  
9 Act -- which was implemented by part 37 of our  
10 regulations -- has no comparable standardized  
11 international principles that have been  
12 established concerning appropriate oversight and  
13 supervision of swap trading platforms.

14 Consequently, while we have part 37 to  
15 use as a baseline regarding supervision and  
16 regulation, we cannot turn to any joint  
17 international standards to rely on when  
18 considering whether a foreign-based swap execution  
19 facility is subject to comparable, comprehensive  
20 supervision and regulation on a consolidated basis  
21 by an appropriate governmental authority in its  
22 home country, as compared to what we have.

1           So, we have part 37, but we do not have  
2           an international standard that we can compare this  
3           to. So, therefore, the exempt staff rulemaking  
4           team is now in the process of considering what  
5           standard would meet the statutory requirement.

6           And we're doing so without prejudice.  
7           We're trying to understand, what does this  
8           statutory standard require of the Commission? And  
9           the team, therefore, has quite a number of  
10          questions on this topic, and we would like to pose  
11          a number of the questions today, to help us, to  
12          help the team formulate this regulatory standard  
13          that we have to try and draft so that we could  
14          provide a proposal to the Commission.

15          So, therefore, I'm coming today from a  
16          different position from what was earlier, where  
17          the team that had worked on that rulemaking had  
18          gone through and considered a lot of different  
19          issues, and made some conclusions that they were  
20          going to provide to the Commission shortly. We  
21          are starting out at the beginning, and, therefore,  
22          we are guessing that you all have a lot of

1 opinions on this, and we would like to get those  
2 opinions as we consider this.

3 MR. SERAFINI: Terrific. Before we open  
4 it up for a full discussion, David, would you like  
5 to make a few comments?

6 MR. BAILEY: Yes. Thank you, Chairman.  
7 I have a number of thoughts on this, but much of  
8 what I said this morning with respect to the need  
9 for and the process to implement an exempt DCA  
10 regime applied to the trading venue space and a  
11 potential exempt SEF regime, as David and Riva  
12 have been outlining.

13 So, I'm not going to repeat my comments  
14 from this morning, but the broad construction  
15 applies.

16 I'd also note that this is an area of  
17 trading where we've already seen real  
18 fragmentation in the markets between the U.S. and  
19 other jurisdictions -- and specifically between  
20 U.S. person liquidity and non-U.S. person  
21 liquidity, as we've seen reported extensively  
22 within, for example, the -- but not exclusively --

1 the statistics.

2 And I think we should just bear in mind  
3 that that fragmentation has the potential to have  
4 a really negative impact on the outcomes that end  
5 users achieve in markets and on overall market  
6 resilience in times of stress.

7 So, from our perspective, having an  
8 exempt SEF regime and having something comparable  
9 in other jurisdictions, including the E.U., is  
10 absolutely essential.

11 In terms of -- I'd like to highlight two  
12 issues for this discussion. Firstly, that we have  
13 precedents in terms of cross-border regimes for  
14 trading venues that I think we can usefully look  
15 to, to see what's worked well and what hasn't.

16 And secondly, I think it's fair to say  
17 that the pace of regulation in the trading venues  
18 space between different jurisdictions is  
19 especially stark, in the case of trading venues,  
20 as compared with post-trade issues. And I just  
21 want to highlight a couple of consequences of  
22 that.

1           So, on the first point, I'd just like to  
2 highlight that a good example of a cross-border  
3 regime is the way that, for example, the FCA or  
4 the FSA, as we once were, and the CFTC have  
5 collaborated with respect to derivative exchanges.

6           From a U.K. perspective, we have what's  
7 known as the recognized overseas investment  
8 exchange regime. And from the CFTC's perspective,  
9 you have the Foreign Board of Trade regime. And  
10 those are now overseas exchanges, to operate in  
11 our respective jurisdictions, and remain  
12 supervised by the home supervisor on a day-to-day  
13 basis.

14           We've got great collaboration with  
15 colleagues here at the CFTC in making that happen.  
16 We had a delegation across discussing the regime  
17 only last week. And their success was recognized  
18 in the path-forward, and I think they are a really  
19 good example of how a cross-border regime can and  
20 should work.

21           We've also, as David's outlined, we have  
22 got the example of the interim qualifying MTF

1 regime, which was announced the day that this  
2 committee last met, back in February.

3 Here's an example of something that  
4 hasn't worked as effectively as we had intended.  
5 But there's a number of reasons for that, and, to  
6 a large extent, that comes down to the fact that  
7 Europe, at the time that that was put in place,  
8 was still developing its rules for trading venues,  
9 for OTC derivatives.

10 But I would like to highlight a couple  
11 of points that we have learnt from the experience  
12 of putting together the interim QMTF regime. The  
13 first is, if there are a significant number of  
14 top-out requirements -- or additional conditions  
15 placed on the regime -- it makes it very difficult  
16 for market participants to amend the way they do  
17 business, to meet those additional top-out  
18 requirements.

19 And the second point I'd like to  
20 highlight is that the qualifying MTF regime  
21 contained a footnote. And we've a lot of  
22 experience of making sure we always read the

1       footnotes in CFTC releases -- noted that in the  
2       case of significant participation from U.S. market  
3       participants, then the CFTC reserved the rights to  
4       amend or remove the exemption.

5               And that has caused a significant amount  
6       of comment, and I think that's a concern amongst  
7       European participants around -- actually, and  
8       European venues around how that would operate in  
9       practice. So, a lesson from that is clarity on  
10      such requirements, and, if possible, not having  
11      those requirements would make a regime work more  
12      effectively.

13             So, there's a couple of points there  
14      that we've learned from the qualifying MTF regime  
15      so far that I think we need to take forward. And  
16      in my view, it serves as something we can work  
17      with as an interim measure, but it's not a  
18      template on which to base a long-term exempt SEF  
19      regime.

20             My second point aligns with that, which  
21      is, European trading requirements for derivatives  
22      are only just being finalized. The (inaudible)

1       legislation has only been agreed back in April,  
2       and it's shortly to be published in the European  
3       Union's official journal.

4                 But it does mean that we now have  
5       confirmed regulations, and we'll see imminently  
6       from ESMA a consultation on the rulemakings  
7       underneath those requirements. These now give us  
8       the basis for a workable cross-border, long-term  
9       regime with respect to OTC derivatives.

10                And in terms of what that should look  
11       like -- well, I think that can follow the same  
12       basis that I described this morning. It can  
13       follow an outcomes-based jurisdiction-level  
14       assessment of equivalence.

15                To Riva's recent points, I think we do  
16       have a basis, we do have an international set of  
17       agreed principles in which trading venues for OTC  
18       derivatives can be based. And that is the  
19       February 2011 IOSCO report on trading of OTC  
20       derivatives, which contains a number of principles  
21       which have been enshrined in the way that Europe  
22       has developed its regime. And I think they are a

1 starting point for the assessment of equivalence.  
2 And they were jointly developed by authorities,  
3 including the U.K. FSA, and the CFTC, and the U.S.  
4 SEC, in terms of leading the development of those  
5 principles. So, I think that does give us a  
6 basis.

7 But a second point -- we'd also need  
8 excellent cooperation between regulators. But as  
9 we've talked about already this morning, I think  
10 that is actually already in place.

11 So, the building blocks are there in  
12 Dodd-Frank and in what we're developing  
13 (inaudible) and in other jurisdictions. I think  
14 we can leverage on the lessons we've learned from  
15 the Foreign Board of Trade regime and from the  
16 qualifying MTF regime on what's worked and what  
17 has not. I'm confident we can put in place  
18 sensible regimes, both from a U.S. perspective and  
19 the European perspective.

20 I'm looking forward to some more direct  
21 questioning from the committee later.

22 Thanks.

1                   CHAIRMAN WETJEN: David, if I could just  
2                   add something very, very quickly -- I agree with  
3                   your two points.

4                   On the first point, to me, it's another  
5                   highlight of the importance of the other  
6                   countries' part of the G20 adopting standards in  
7                   their own legislation that are as comparable as  
8                   possible to what the U.S. has already had in  
9                   place.

10                  It sounds like exporting our standards  
11                  -- and I don't intend it to sound that way, but  
12                  I'm only making the point from a practical  
13                  perspective, because the closer they are, the  
14                  fewer top-ups, if you will, theoretically would be  
15                  necessary.

16                  So, I appreciate you making those  
17                  points.

18                  MR. BAILEY: And just, very quickly, to  
19                  come back on that, Chairman -- I think I agree  
20                  with that, and I think that's why it's important  
21                  that we base our regimes on those international  
22                  standards. And I know that the SEF regime

1 implements the IOSCO principles I described  
2 earlier, as does the European regime. And I think  
3 that's a really good basis on which to work from.

4 MR. SERAFINI: Thank you, David. Jun,  
5 did you want to make some remarks?

6 MR. MIZUGUCHI: Well, thank you,  
7 Chairman. Well, I just wanted to make some  
8 general comments -- just a few special comments.  
9 I'm just trying to do touch-up on some kind of  
10 Asia-Pacific flavor, if possible.

11 Well, this (inaudible) it basically  
12 started from the Pittsburgh summit in 2009. Then  
13 (inaudible) derivative contracts should be traded  
14 where appropriate, to improve on transparency,  
15 mitigate (inaudible) market protection.

16 Then it followed, as David mentioned,  
17 that the (inaudible) they issued two reports --  
18 2011 and 2012 -- on the organized training  
19 platforms, to try to emphasize the kind of  
20 flexible approach to defining an organized  
21 training platform for the purpose of G20 purposes,  
22 with certain characteristics (inaudible) and to

1 try to maximize the number of the standard  
2 products that can be traded on that platform, so  
3 that the initiative on the (inaudible)  
4 transparency will be increased.

5 But here, not a kind of particular form  
6 of platform is prescribed at the IOSCO report.  
7 And a number of the countries since then have  
8 tried to introduce kind of a sort of authorization  
9 system for the OTPs.

10 Then while here, we are talking about  
11 the exemption (inaudible) the OTC with the regular  
12 group, discussing about various approaches -- how  
13 to make it (inaudible) a regime such as  
14 substituted compliance, or a grievance, or  
15 exemption, or permission forever.

16 So, that's a work that's going on. This  
17 is my general comment.

18 And some specific comments -- while  
19 recently, IOSCO Asia-Pacific Regional Committee  
20 sent a letter to the CFTC -- recently, issues have  
21 emerged with respect to the potential for the  
22 liquidity fragmentation, along with jurisdiction

1 rights.

2           While this issue seems to be arising  
3 from a so-called (inaudible) it appears that the  
4 liquidity has been fragmented between the U.S.  
5 person and non-U.S. person, as David pointed out.

6           Of course, I think it's this issue of  
7 market confusion. It's partly related to the  
8 issue of possible lack of maybe credibility or  
9 predictability of the framework of the regulation  
10 for the (inaudible) and market stakeholders.

11           I think the CFTC already took some  
12 action to address this issue, but enhancing the  
13 credibility or predictability of the (inaudible)  
14 the regulation -- I think it should be very much  
15 helpful to reduce the regulatory uncertainty and  
16 to avoid any consequences and unnecessary burden  
17 for the market participants.

18           And then in this (inaudible) it's also  
19 important to have an appropriate (inaudible) or a  
20 reasonable transition period, especially for the  
21 40 entities to introduce kind of a new  
22 requirement. That's my first comment.

1                   And second comment is that the exemption  
2                   about the U.S. SEF issue -- we've talked about the  
3                   (inaudible) comprehensiveness.

4                   Then, as I mentioned in morning  
5                   (inaudible) there are two issues -- how to assess  
6                   the compatibility and the comprehensiveness of the  
7                   foreign regimes. Of course, they're not really  
8                   such a granular principle, but, as David said, the  
9                   IOSCO has two reports that have a really good  
10                  basis for how to lay out some principles or the  
11                  characteristics.

12                  But, of course, the granularity of the  
13                  (inaudible) principles might not be as great as  
14                  the PFMI -- and also conditions, which might be  
15                  (inaudible) on the exemption, are not yet clear.

16                  I'm aware that the CFTC (inaudible) for  
17                  the European MTF -- in favor of (inaudible). But  
18                  I think it's - - going through all this, I think  
19                  it's very important that, more in general, the due  
20                  recognition should be given to the differences in  
21                  legal and regulatory frameworks, or open- market  
22                  practices and characteristics, because Europe,

1 U.S., Japan, and possibly Asia or other markets --  
2 and, also, in terms of the market debts or  
3 liquidity -- are different.

4 So, this may have significant  
5 (inaudible) in local markets. In that regard, I  
6 would like to emphasize that a one-size-fits-all  
7 approach would not be appropriate in this kind of  
8 assessment.

9 Then the last issue, which is a similar  
10 issue -- which I mentioned in the morning -- well,  
11 actually, the trading venue issues is closely  
12 related to the trading obligation -- trading  
13 mandate issue.

14 Well, I just think one -- and, also,  
15 (inaudible) timing of how the trading mandate will  
16 be implemented. Well, just one example -- suppose  
17 that, well, the (inaudible) is not subject to the  
18 U.S. trading mandate. But in Japan, we are  
19 basically -- they are implementing the trading  
20 mandate, at the latest, by next year. In that  
21 case, suppose that the U.S. and Japan implementing  
22 IRS -- well, as for the trading mandate.

1                   And then -- well, (inaudible) and if  
2                   there is -- well, in this case, the issue being  
3                   OTP, which is eligible in both countries for use  
4                   through, for example, some registration exemption.  
5                   When trading obligation in both countries are  
6                   implemented -- well, otherwise, both U.S. and the  
7                   Japanese counterparties basically would refrain  
8                   from trading, or they are not able to do so in  
9                   fear of breaching the rules of each country.

10                   Well, in that regard, I think flexible  
11                   and/or (inaudible) coordinated approach among  
12                   regulators -- it would be quite important to avoid  
13                   unnecessary burden (inaudible) for the market  
14                   participants. I will stop here.

15                   MR. SERAFINI: With that, I'll turn it  
16                   back to CFTC staff, if they want to, you know,  
17                   maybe pose a question to the group.

18                   MS. ADRIANCE: Okay, thank you all. We  
19                   put together a number of questions. Actually, I  
20                   think our first list was probably starting with,  
21                   like, 30 questions or something. But rather than  
22                   scare everybody, we got it down to a smaller

1       number, which I believe was circulated to the  
2       members of the GMAC committee.

3               So, I'm going to begin with going  
4       through this. And, certainly, you know, I know  
5       this morning, Phyllis started with actually kind  
6       of taking a step back and asking about the overall  
7       -- whether this was a good thing to do, in terms  
8       of the exempt DCO rulemaking.

9               And I don't know if anyone wanted to  
10       address it in the context of an exempt SEF  
11       rulemaking before we go onto the more specific  
12       questions.

13               MR. TAKAYAMA: I wanted to make quite a  
14       general comment. And given the (inaudible) of the  
15       liquidity and the fragmented market which are in  
16       place, we should be reminded of the basic, you  
17       know, concept of the mutual recognition -- or the  
18       regulators have to be mindful of the appropriate  
19       deference to each other (inaudible) the  
20       international principles.

21       And based upon that notion, I think that any  
22       conditions to be given by the U.S. authorities should

1 be limited to the U.S. person's trades -- and, plus,  
2 thinking about the cost-benefit analysis, we have to  
3 be also reminded of the primary intended benefit of  
4 the SEF.

5 I understand that is the (inaudible) trade  
6 transparency. I think that other types of benefits --  
7 credit risk concerns are supposed to be met by the  
8 mandatory clearing. And (inaudible) trade and  
9 transparency could be met by the reporting by the  
10 bureaus.

11 So, again, given the fragmentation of the market and  
12 the liquidity split, we have to be focusing up on the  
13 primary benefit of the SEF under any condition to be  
14 put upon. It is limited to the trades between a U.S.  
15 person and trades made by U.S. persons, and under any  
16 of those conditions, should be those enhancing the  
17 (inaudible) trade transparency.

18 Thank you.

19 MS. ADRIANCE: Thank you. Was there  
20 anyone else that --

21 MR. COOPER: Thank you. This morning in  
22 the panel, I expressed Citadel support for the

1       exemptive process in the context of DCOs, and I  
2       concur with David's view that, in the process,  
3       you couldn't separate the customer solution from  
4       the proprietary solution.

5       And the basis on which we felt so strongly about that  
6       was this notion of fair and open access, which I think  
7       is core to the success of swap market reforms. I'm  
8       going to come back to that concept and phrase it a  
9       little bit differently as open and impartial access to  
10      being a cornerstone to the success of swap-market  
11      reforms -- and add to that straight through  
12      processing.

13      Those two concepts, we think, are absolutely critical.  
14      So, Citadel supports very much the notion of exemptive  
15      authority and relief applied in the context of foreign  
16      SEFs, provided that this process ensures the exemption  
17      is only granted in those cases where we've made a  
18      determination -- or the Commission's made a  
19      determination -- that impartial, and open access, and  
20      straight through processing exists.

21      As I mentioned this morning, in the DCO context, we  
22      don't think there can be any opportunity for daylight

1 to exist between the CFTC's very strong and clear  
2 regulatory and policy positions on these matters --  
3 that is, open access and straight through processing  
4 -- and the rules that are applicable to the exempt  
5 SEFs.

6 A memorandum of understanding or other, similar  
7 vehicles are, we think, very important to ensuring  
8 continued sort of viability and inclusion of those  
9 attributes in the markets where the exempt SEFs exist.

10 If I may just finally mention -- we were very  
11 encouraged to see that in the recently-adopted  
12 (inaudible) legislation in Europe, they included  
13 provisions on STP that very closely parallel the  
14 Commission's STP rules. And we think that's very,  
15 very important and very encouraging.

16 CHAIRMAN WETJEN: If I can just follow  
17 up very quickly on what Adam said -- again, it  
18 highlights, for me, the importance of some of  
19 these standards -- and not every standard is of  
20 equal weight. Adam identified a couple that are  
21 two of the true hallmarks of our SEF regime. And  
22 I think the other critical one, of course, would

1 be the controls around the types of execution  
2 methodologies permitted on a SEF for mandated  
3 swaps.

4 Those are the three key component parts  
5 of our SEF regime. Those are part of the  
6 conditions of our MTF, along with some others.  
7 And so I think, going forward, we're really going  
8 to have to work through this, and think carefully  
9 about it, and I guess I'd stop there, but ask the  
10 panelists the question -- David made the good  
11 point that there is a set of principles that has  
12 been adopted, but I don't know if anyone's in a  
13 position among the staff across the room here to  
14 identify some of the key principles that were laid  
15 out by IOSCO, and to what degree they touch upon  
16 two of the issues that Adam addressed.

17 MR. BAILEY: So, I can take that,  
18 Chairman. I have them in front of me, in fact.  
19 If I look back at the authors, I see a certain  
20 David van Wagner is one of the key authors. So,  
21 we won't test him right now.

22 CHAIRMAN WETJEN: This is short-term

1 (inaudible).

2 MR. BAILEY: So, the characteristics  
3 that IOSCO laid out -- just at a high level --  
4 included things like registration of the platform  
5 with a competent regulatory authority, including  
6 requirements related to financial resources and  
7 operational capability, access for participants  
8 based on objective and fair criteria that are  
9 applied in an impartial, nondiscriminatory manner,  
10 pre- and post-trade transparency arrangements,  
11 operational efficiency and resilience, including  
12 linkages to post-trade infrastructure. And I'm  
13 paraphrasing here, not to go into the detail --  
14 active markets (inaudible) capabilities,  
15 transparent rules, and nondiscriminatory -- or  
16 rules that do not permit a platform operated to  
17 discriminate. And they also included having been  
18 multilateral of nature.

19 So, I think they capture the key  
20 elements that would underpin a sensible regime for  
21 this kind of trading -- and, certainly, capturing  
22 the key attributes of the European regime that

1 we're developing -- and my understanding of the  
2 U.S. regime, as well.

3 MR. SERAFINI: John?

4 MR. NIXON: I'm happy to just make a  
5 couple comments.

6 First of all, I think that if the CFTC  
7 and the Commission knew in 2010 what they know now  
8 about SEF trading and execution in the OTC  
9 markets, we might have had a slightly different  
10 outcome on some of the rules, because it's  
11 certainly been something that's had to morph over  
12 a period of time.

13 I think we've also found out that the  
14 futures markets -- which the regulators were very  
15 used to regulating -- is very, very different than  
16 the nature of the OTC markets and the cross-border  
17 block sizes that are traded in some of the OTC  
18 markets.

19 But one of the things -- when I talk  
20 about the exempt SEFs -- and, I think, David, you  
21 touched on the IOSCO rules. If I look at the SEFs  
22 and what Adam is saying, to me, a lot of the

1 futures markets have been based on principles that  
2 the CFTC has set. And I think as we go forward,  
3 if you're going to have exempt SEFs, you're going  
4 to have to do them on principles and not on rules.

5 I think that you've laid out -- or IOSCO  
6 has laid out -- some very important principles  
7 that they feel that all OTC execution venues  
8 should offer into the marketplace, such as  
9 impartial access, open-access rulebooks -- all of  
10 the ones that you've just mentioned.

11 And I think that if you're going to have  
12 a global regime that allows for exempt SEFs or  
13 exempt trading facilities, they need to be based  
14 around certain principles that the regulators  
15 agree, as opposed to specific rules.

16 MR. SERAFINI: Kim?

17 MS. ADRIANCE: Thank you. I just want  
18 to make a couple of comments.

19 First of all, I think, again, we support  
20 the concept of mutual recognition -- that is,  
21 creating a level playing field between the  
22 different jurisdictions.

1           We do think that, in some ways, for  
2 trading venues, there are -- it lacks some of the  
3 complications of clearing; doesn't have bankruptcy  
4 complications. But in another respect, it's  
5 perhaps more complicated than getting a mutual  
6 recognition regime for clearinghouses because of  
7 the timing differences. The rules for trading in  
8 Europe don't go into effect for some time, and  
9 it's uncertain whether there will even be trading  
10 mandates in many other jurisdictions.

11           So, there's not kind of at least  
12 uniformity of mandate -- or, you know, closer  
13 uniformity of mandate status. So, those are  
14 complications.

15           Another complication that we have seen  
16 is, again, the fact that a European regime is  
17 holding futures in OTC in the same timeframe. And  
18 so, again, the U.S. -- actually, it's not just  
19 U.S.-based exchanges; it's any futures exchange  
20 that is not located on European soil -- is in a  
21 position where it is already not recognized as a  
22 futures contract for trading purposes for parties

1 who are counting their OTC trading as part of  
2 their determination of what is called NFC plus  
3 status, but it's similar to a major swap  
4 participant in the U.S. It's a status that many  
5 people would prefer to avoid if they can.

6 And futures that are traded on  
7 European-located exchanges count as futures, and  
8 don't count against this status. And futures that  
9 are traded on non-E.U. platforms do count as OTC,  
10 and count against this status.

11 So, in this case, going back to my  
12 opening analogy from the morning, we're in a  
13 position where the hostages aren't all going to be  
14 shot on December 15th. The hostages are being  
15 shot now. So, we are already feeling the impact  
16 of, for certain market participants, the  
17 sensitivity to this NFC plus.

18 And, again, the CFTC does not put any  
19 restrictions on the ability of U.S. persons to  
20 freely trade on E.U.-based trading platforms  
21 foreign futures.

22 So, I think we would ask for there to be

1 an acknowledgement of that, and perhaps a  
2 separation of the decision-making process on  
3 futures versus OTC.

4           Then I also wanted to just mention -- I  
5 was interested in a couple of specific comments  
6 that David made, one being that if there are a  
7 number of conditions or top-up requirements in a  
8 kind of neutral recognition or exemption regime,  
9 that is problematic. It's difficult for parties  
10 to adjust their business, and it was problematic  
11 that the CFTC and the QMTF reserved the right to  
12 expire or withdraw the exemption.

13           And I would like to point out that on  
14 the clearing front, those corresponding things are  
15 exactly the same things that are being opposed by  
16 the E.U. regime on the recognition of equivalence  
17 for clearinghouses. There are top-up conditions  
18 being imposed on the PFMI requirements, and there  
19 is -- and, again, I'm at a bit of a disadvantage  
20 because we haven't seen anything in writing, but  
21 from what we've been able to glean, there are  
22 top-up conditions and the two-year review.

1           So, the equivalent status only exists on  
2           a two- year cycle. And so I would need to agree  
3           with you that those types of practices are  
4           somewhat problematic, but I would suggest that  
5           they're problematic whichever side of the pond  
6           they start on and emanate to.

7           CHAIRMAN WETJEN: Just real quick --  
8           what is the rationale for the two-year time limit  
9           on the equivalency determination? David or Kim,  
10          I'm just curious.

11          MR. BAILEY: So, if I may come in on  
12          both those points -- and just before I answer that  
13          question -- just in response to Kim's points, I  
14          think the -- my comments with respect to the  
15          qualifying MTF regime very much reflected that  
16          it's an interim regime in a place where you have  
17          two regimes -- where one has implemented new  
18          standards; the other is still catching up.

19          And so my comments about topping-up  
20          requirements were a significant number of them --  
21          and the fact that the status could be, in fact,  
22          pulled at any point in time on very short notice,

1 with no sort of transitional -- but, Chairman  
2 Wetjen, with respect to your comments -- from a  
3 personal perspective -- and, again, I'm not the  
4 European Commission -- I don't recognize the  
5 two-year window.

6 My understanding was, if given the  
7 equivalence, that applied, full-stop, as opposed  
8 to being on a two-year cycle. So, that's another  
9 factor I recognize. But I appreciate -- if it was  
10 there, that would be something that we need to  
11 discuss.

12 MS. ADRIANCE: And we're in a position  
13 where we haven't seen anything in writing, because  
14 this is legislation that has to be formulated.  
15 But we have had discussions where we have been  
16 told that there would be a two-year review  
17 process. So, the equivalence would be reevaluated  
18 on a two-year cycle.

19 CHAIRMAN WETJEN: Wally?

20 MR. TURBEVILLE: Thanks. Out of concern  
21 for hostages -- and maybe less sympathy for people  
22 who have to work through topping-up -- but more

1 out of a concern for just trying to understand --  
2 make sure we're all clear on what's going on right  
3 now, what's the state of play right now -- I just  
4 have a question that you can help clarify.

5 One of the things that's been going on  
6 -- at least in terms of what's been reported -- is  
7 the issue of so-called the guaranteeing, where  
8 U.S. affiliates are no longer being guaranteed --  
9 at least the swap obligations of subsidiaries are  
10 no longer being guaranteed in some way. I have a  
11 couple of questions.

12 Do we know what's really going on there?  
13 Because there's different levels of assurance that  
14 a parent can give a subsidiary.

15 And is it a question of true guarantee  
16 being dropped -- some kinds of guarantees being  
17 dropped? And how, if any, does that fit into,  
18 what's the state of play in this discussion right  
19 now?

20 MR. MCGONAGLE: So, I certainly  
21 appreciate the question. And maybe the members of  
22 the GMAC can sort of talk about what they

1 understand on the D guaranteeing, but we're not in  
2 a position here -- this staff -- to offer an  
3 opinion about what we've seen.

4           You know, there's been certain questions  
5 that have been posed to us, that we're evaluating  
6 -- us being commissioned staff, but DMO staff in  
7 particular -- we're not in a position to sort of  
8 address that -- certainly in connection with what  
9 we're thinking about here on this exempt stuff.

10           But I appreciate the comment; certainly  
11 appreciate the interest. I don't know if the  
12 Chairman or Commissioner O'Malia want to speak to  
13 that.

14           CHAIRMAN WETJEN: I'll say something  
15 real quickly. When we adopted the guidance, we  
16 made a set of policy judgments based on what the  
17 statute provided, and it also, obviously,  
18 reflected a number of policy judgments. And if  
19 the basic construct of our cross-border policy --  
20 or at least the swaps -- is a risk-based analysis,  
21 the focus -- which it was -- the focus,  
22 consequently, then was on, okay, how, in the

1 marketplace today, could risk be imported back to  
2 the United States?

3           So, we looked at a variety of different  
4 ways that could happen. We settled on certain  
5 legal structures -- the form branch structure.  
6 That was a pretty clear example. A little less  
7 clear but, nonetheless, I think, pretty compelling  
8 was a trade that was backed by U.S. parent, with a  
9 guarantee. Clearly, as a legal matter, put the  
10 parent on the hook -- so that suggests a pretty  
11 good indication of the potential of risk  
12 transference.

13           And we stopped there. There are other  
14 terms of a contract that perhaps could indicate  
15 risk transference back to the United States. And  
16 some of those were considered at the time, but,  
17 again, we had a statute we had to interpret.  
18 There were some limits to the statute. And we're  
19 also making a judgment based on facts as we  
20 understood them at the time.

21           And so whether or not they're new  
22 contractual terms that are part of swap agreements

1 -- that's what staff has been looking into, as of  
2 late. New contractual terms -- in other words, it  
3 would be the functional equivalent of a guarantee.  
4 That's what we have to look at, I think, and  
5 that's the process that's currently underway.

6 MR. SERAFINI: Supurna?

7 MS. VEDBRAT: You know, so my point is a  
8 little bit -- just a point of discussion, and  
9 maybe somebody on the panel can help clarify.

10 You know, if we end up with an exemption  
11 for, you know, certain, you know, OTFs or foreign  
12 steps -- you know, one concern I would have is  
13 that, you know, would half my trade flow be under  
14 one jurisdiction, rather than other half?

15 Like say for example, if we were to  
16 trade, you know, something via one of the  
17 platforms in London, and it happened to be a U.S.  
18 CME swap -- so the clearing end of it would be  
19 under U.S., and then, you know, the frontend,  
20 where we're exchanging market risk, would be under  
21 another jurisdiction.

22 So, how would we manage that type of

1 risk? Because it's the same trade.

2 MR. BAILEY: So, I think you've probably  
3 highlighted a very clear reason why we need an  
4 exempt SEF and an exempt DCO regime to work  
5 together.

6 MS. VEDBRAT: Exactly. I mean, they are  
7 somewhat interlinked, and, you know, to some  
8 extent, you know, you want to have certainty of  
9 what's going to happen through a single trade.  
10 And it just (inaudible) actually trying to ride it  
11 out. The permutation and combinations become  
12 very, very complex.

13 MS. ADRIANCE: Can I just ask -- I mean,  
14 when -- I understand there is a complexity there.  
15 In terms of that, since there was obviously the  
16 need to be some kind of coordination -- or some  
17 kind of recognition on the side of both the  
18 clearing and the trading -- do you -- I mean, did  
19 you have, along with that, a recommendation as to  
20 what we should be taking into account, or how we  
21 should consider that? Or are you just basically  
22 raising the issue and saying --

1 MS. VEDBRAT: I'm raising the issue  
2 right now. I think we need, you know, to see,  
3 like, the final method, you know, rules. There is  
4 a lot in our conversations; you have some idea.  
5 I'm not quite sure how we can translate, you know,  
6 what we know so far into a principle-based  
7 approach.

8 I mean, I think some of the issues were  
9 raised, like straight through processing and  
10 things like that, but, you know, a couple of  
11 others -- you know, what type of documentation  
12 would you need? Today, if I trade on a U.S. SEF,  
13 essentially, I need very little EB documentation.  
14 Like, how would that pertain? And a lot of those,  
15 you know, documentations for the SEF are also  
16 intertwined with the CCP requirements.

17 And then I don't know if we can  
18 schedule, like, (inaudible) to be part of straight  
19 through processing, but that would be another  
20 concern.

21 And, you know, what are the rules around  
22 RFQ? Like, if it's a principle-based approach,

1 some of the fundamental rules which are going to  
2 drive how you trade would need to be explained a  
3 little bit more. Otherwise, you're going to end  
4 up trading on the facility, you know, that  
5 essentially matches, you know, what your desired  
6 outcome is, and where there's liquidity.

7 MR. VAN WAGNER: Right. I mean, so the  
8 point is -- it's certainly on trading  
9 methodologies, and we associate pre-trade price  
10 transparency with those requirements. I mean, I  
11 do think we are -- we will be looking at a  
12 principles-based regime. Of course, we've got to  
13 balance that with what our Congress told us,  
14 insofar as being comparable and comprehensive,  
15 compared to our own.

16 And I do think that an outcomes-based  
17 approach is what we've followed in the FBOT regime  
18 -- the FBOT regime being the regime that's  
19 comparable to contra-markets for futures.

20 So, we're thinking through those issues.

21 COMMISSIONER O'MALIA: David, can I ask  
22 a question? If FBOT is principles-based, what is

1 QMTF?

2 MR. VAN WAGNER: QMTF is transitional.  
3 We knew that, as we sat at this table a year or so  
4 ago, and we scanned the horizon, and we realized  
5 that there was really not a regulatory regime out  
6 there at all that was comparable to ours -- or,  
7 really, anything that had been built out or mature  
8 yet.

9 So, the only point of reference that we  
10 had was our own, for the time being.

11 COMMISSIONER O'MALIA: Right. So, 16,  
12 18 months' difference between U.S. rules now --  
13 Dodd-Frank, SEF rules, and what's going to be the  
14 MTF MIFID rules. Do we have time to implement an  
15 exempt SEF regime, or should we develop something  
16 that works to recognize MTFs and solve for this --  
17 at most -- 24-month solution?

18 I mean, this is now about timeframe.

19 MR. VAN WAGNER: Right. No, understood.  
20 And we're obviously not. There's parallel tracks,  
21 so the MTF no-action letter is out there now.

22 I would think that, in parallel with the

1 exempt SEF rulemaking being issued -- or at least  
2 the proposed being issued -- they might start to  
3 look back at the template that is now the MTF and  
4 no-action letter, and possibly have to refine it.

5 And it would be refined not only for  
6 Europe and MTFs, but possibly other jurisdictions.  
7 We would try to be as standardized as possible,  
8 but yeah. I think it'll be informed as we go  
9 through the exempt SEF process, as well.

10 We didn't want to get out in front of  
11 the Commission on the exempt SEF process, so the  
12 only thing the Commission had told us to-date are  
13 the SEF rules.

14 MR. MCGONAGLE: And I think -- just to  
15 touch bases a little on context, and focus on what  
16 statutory requirements we have, and looking at,  
17 too, why the direct effect back to the U.S. --  
18 but, also, made available to trade swaps -- could  
19 only be traded on a DCM, a SEF, or an exempt SEF.  
20 But we also have an obligation to consider,  
21 effectively, you know, how do we interact with  
22 other trading outside of the U.S. and looking at

1 the path forward?

2 And so that's where the QMTF discussions  
3 came about, to sort of recognize what we have  
4 already in statute that we need to be focused on  
5 to ensure we have price transparency within the  
6 U.S., and recognizing that there are other  
7 facilities coming up to speed, and aren't close  
8 enough yet to where we're at, and how do we  
9 bridge?

10 COMMISSIONER O'MALIA: But shouldn't we  
11 take a look at where trading is occurring right  
12 now? We've got U.S. dollars trades on SEF. We  
13 have nine U.S. persons, nine U.S. dollar trades  
14 off SEF. And I don't see how the market changes  
15 as a result of another transitional platform that  
16 isn't being utilized like the QMTF.

17 So, in light of the data that we're  
18 seeing today, the real-life trading experience,  
19 what is the right answer? And I throw that open  
20 to everybody, frankly -- and not just our staff.  
21 But, I mean, why would we -- let's look at the  
22 data, and figure out what it's telling us, and

1 about the way people are trading, and figure out  
2 what the best solution is, going forward.

3 MR. BAILEY: So, maybe I can come in on  
4 that. So, on that point, Commissioner O'Malia,  
5 the fragmentation you've highlighted is real, and  
6 it's here now.

7 Certainly, from our perspective,  
8 ideally, we would have an exempt SEF and a  
9 matching European regime in place now. We can't  
10 do that, because -- to a large extent -- Europe  
11 hasn't developed its rules to the same pace as the  
12 U.S. We recognize that.

13 And so the right answer is to have those  
14 regimes in place at the point that we can do. And  
15 that's not right now, but, as you said, it's  
16 somewhere between now and two days' time -- the  
17 sooner the better, from our perspective.

18 I think the interim regime -- whilst  
19 another template for a longer-term regime -- still  
20 has the potential to be useful, and one we  
21 continue to discuss.

22 MR. NIXON: Let me just try and see if I

1 can take a stab at Scott's comments, and pick up a  
2 little bit on what David said.

3 I mean, the QMTF obviously hasn't  
4 worked. We haven't got an -- I don't think  
5 there's been one application for a QMTF. If there  
6 is, I haven't, you know, read about it.

7 As Scott said, U.S. trading is basically  
8 all being done on SEF. Non-U.S. trading is all  
9 being done off SEF. That's the way it's working.  
10 And if a U.S. person wants to trade off of a SEF  
11 with a non-U.S. person on an MTF, they are trading  
12 in a nonguaranteed subsidiary. So, right now, you  
13 basically have fragmented trading between two  
14 platforms.

15 And ICAP, as all of you know, had  
16 applied recently and was granted temporary  
17 registration by both the FCA and the CFTC for its  
18 new SEF, called IGDL -- which basically was put in  
19 place because we were not sure at the time we  
20 decided to make this application whether or not  
21 the QMTF was going to be something that would come  
22 into place and stay for a short period of time, or

1       come into place and stay for a long period of  
2       time.

3                   And we decided that this was probably  
4       the most logical way to go forward -- was to have  
5       an entity that was dually registered by the CFTC  
6       and the FCA. And I will tell you that that entity  
7       is basically trading U.S. dollar swaps. That is  
8       where it is. All of the European swaps are being  
9       traded off SEF, onto a different, you know, MTF.

10                   So, we have in place an entity that is  
11       dually regulated, and which all U.S. and non-U.S.  
12       persons are prepared to trade on. But they do  
13       trade it on one product at this stage, and one  
14       product only.

15                   CHAIRMAN WETJEN: Just one quick point  
16       to follow up on John's comments -- and back to the  
17       overall discussion about conditions -- and  
18       following something as broad as principles gets us  
19       to where we need to be in every instance.

20                   The question I have -- and this is not a  
21       rhetorical one -- but there's some folks around  
22       the table that might be willing to speak to this.

1 If we had no conditions on our MTF letter, would  
2 there be any SEF trading?

3 MR. NIXON: Well, when you said no  
4 conditions, if your conditions were (inaudible) --

5 CHAIRMAN WETJEN: Yeah, so we recognize  
6 the platform in London, and we say, we don't care  
7 about your open --

8 MR. NIXON: If you're saying that a U.S.  
9 person domiciled in the U.S. -- or a U.S. person  
10 domiciled anywhere -- could trade on an MTF, and  
11 does not have to trade on a SEF, my guess is most  
12 of the trading right now will be done on an MTF.

13 CHAIRMAN WETJEN: Yeah, and so back to  
14 the point I made at the very outset of the meeting  
15 -- this statute requires us to consider  
16 competitiveness issues as it relates to our  
17 policymaking. And so we have to be mindful of  
18 what impact our actions will have on our SEF  
19 regime.

20 I don't want to sound like I'm overly  
21 defense of the QMTF letter, but I just want the  
22 group and the public to have the benefit of our

1 thinking. That's why the conditions are there, in  
2 addition to trying to remain faithful to the  
3 statutory requirements we have. That's why the  
4 MTF letter was constructed as it was.

5 I don't like the fact, either, that it  
6 hasn't had the practical impact that we intended.  
7 David and I spoke about that over the lunch hour.  
8 We might have some more work to do there. But  
9 that's, again, just giving the group the benefit  
10 of the thinking behind the conditions of the MTF.

11 But we would like it to be useful. I  
12 mean, that's the whole idea.

13 MR. NIXON: One thing to add, though,  
14 Mark -- that while being, you know, cautious of  
15 the competitiveness of the SEF regime, we also  
16 have to be cautious of the competitiveness of the  
17 U.S. banks, who have to deal in the SEF regime,  
18 versus the foreign banks that are dealing in the  
19 MTF regime.

20 So, competitiveness goes -- you know,  
21 cuts both ways.

22 CHAIRMAN WETJEN: Wallace?

1                   MR. TURBEVILLE: Yeah, thanks. All this  
2                   having been said, from the public's perspective,  
3                   there are some dynamics going on here that are  
4                   quite instructive, and quite revealing, and quite  
5                   informative. Whether whatever's being done in  
6                   terms of the guaranteeing is avoidance or evasion  
7                   is an issue, but if it's just avoidance, if it's  
8                   all by the rules, it would be awfully important  
9                   to, as we think about how all this is going to  
10                  play out over time, to have a pretty clear  
11                  understanding, as broadly as possible.

12                  And I'm just urging that to see what's  
13                  really going on here, because I think there's some  
14                  important information being generated that we  
15                  would like to understand. And from the public's  
16                  perspective, this is being discussed, but being  
17                  discussed (inaudible) less than full understanding  
18                  of what's going on. And how much of this is  
19                  interdealer or how much of this is customer?

20                  So, anyway, there's information being  
21                  generated by actual market activities that I, for  
22                  one, would love to understand more about. And I

1 think there are many others that are observers,  
2 but want to understand what's going on.

3 CHAIRMAN WETJEN: Bob?

4 MR. KLIEN: Yeah, I'd like to go back to  
5 John's comments about what would happen if you  
6 actually sort of allowed free choice of where to  
7 trade, and the observation that non-U.S.  
8 participants would not trade on SEFs.

9 I think that's a pretty profound  
10 statement, and it's consistent with our  
11 observations, as well, and I'd like to draw a  
12 historical analogy. I mean, people have often --  
13 going back for decades -- complained about the  
14 regulation of the U.S. equity markets and how  
15 strong it was -- and I think the answer to that,  
16 from a policy perspective, is, yes, but non-U.S.  
17 participants flock to trade in those markets, so  
18 we must be doing something right.

19 Here, we have a regulatory regime that  
20 is very tough. And non-U.S. participants are  
21 doing everything they can not to trade under that  
22 regime. So, I think it poses the question of

1       whether the regulatory regime got it right or not.  
2       And I think that's something, you know, that we  
3       all ought to be talking about.

4                   To some extent, the agency is bound by  
5       what Congress put in the statute, but I think  
6       there's a lot in the SEF rules that are not  
7       strictly dictated by what's in Title VII. And I  
8       think stepping back to base principles and  
9       figuring out what it is that we want to get out of  
10      the SEF trading mandate from a public policy  
11      perspective might be a very useful thing to do --  
12      both for its own value and, also, in comparing how  
13      we're going to do a comparability analysis -- how  
14      you're going to look at the regulatory regimes in  
15      other countries, and which regulatory regimes  
16      really fit the public policy goals that you're  
17      trying to advance.

18                   CHAIRMAN WETJEN: Supurna and then John  
19      Parsons?

20                   MS. VEDBRAT: Yeah. You know, I just  
21      wanted to comment on the non-U.S. person trading  
22      on a SEF. I mean, there are, like, you know, some

1 structural components that, you know, may make for  
2 a non-U.S. person to trade on a SEF not optimal.  
3 I mean, there are only limited number of hours  
4 when you have a SEF and a CCP open.

5 So, if you're a non-U.S. person, and you  
6 have the choice of, you know, trading on a SEF and  
7 then waiting for CCP to open, and then, you know,  
8 potentially having, like, your trade go through,  
9 like, (inaudible) versus bilaterally trading it,  
10 you may opt to -- even if it's a cleared swap.  
11 So, that's somewhat -- you know, when we move out  
12 of the U.S. time zone, you are seeing, you know,  
13 some of the structural components, you know, come  
14 into play.

15 And then the other thing is that for a  
16 non-U.S. Person, it is voluntary -- just as  
17 clearing is voluntary. And clearing, you know, to  
18 some extent, you can justify it as helping with  
19 counterparty risk.

20 The SEF framework is still, you know, in  
21 its initial stages, so it is a little bit, you  
22 know, delicate. So, you can't confidently say

1 that if you're trading on a SEF, you will  
2 definitely be able to execute the risk and have  
3 certainty of clearing.

4 So, you know, I don't want to put that  
5 in avoidance category; it's just, like,  
6 preliminary stages and a reality.

7 COMMISSIONER O'MALIA: You are  
8 front-running the TAC meeting next week, by the  
9 way. So, stop it.

10 MS. VEDBRAT: Well, I mean, there was --

11 CHAIRMAN WETJEN: Supurna, you  
12 mentioned, too, hours of operation as it relates  
13 to time zones, and then you said (inaudible).

14 MS. VEDBRAT: Yes. So, if you trade on  
15 a SEF -- if the SEF is, you know, open for  
16 trading, but, like, you know, the CCP is not open  
17 for clearing, your trade can sit in a pending  
18 status, so you don't know.

19 Once the clearinghouse were to open, if,  
20 you know, it is truly going to go through, there  
21 is, you know, a probability that the trade gets  
22 voided out.

1                   So, I mean, you know, as an asset  
2                   manager, you know, you want to make sure that  
3                   you're getting the best price and best execution,  
4                   you know, for your underlying funds. So, taking  
5                   that type of risk when there is an option or a  
6                   choice of trading bilaterally -- you know, whether  
7                   it's cleared, or whether it's, you know, bilateral  
8                   -- you know, you opt to do that.

9                   CHAIRMAN WETJEN: I'm glad I asked you,  
10                  because I thought you were suggesting that there  
11                  wasn't a similar policy (inaudible) European laws.  
12                  I don't know whether that's the case or not, but  
13                  it's --

14                  MS. VEDBRAT: We don't know that yet.  
15                  So, it's more just, you know, on the trading of,  
16                  you know, the SEFs -- a piece of it.

17                  CHAIRMAN WETJEN: John, did you want to  
18                  -- David Bailey?

19                  MR. BAILEY: Thank you. And just on  
20                  Supurna and Chairman Wetjen's comment there, I  
21                  suspect Europe would end up in the same place as  
22                  the U.S. on that point. I can't see how it would

1 end up anywhere else, but, as Supurna says, we  
2 need to see the final MIFID rule makings.

3 I just wanted to come back to some  
4 points that John made and Robert made about  
5 disparities between the U.S. And the European  
6 regimes, and what would happen if there were no  
7 conditions applied, for example, in the QMTF  
8 regime.

9 Whatever that would imply in terms of  
10 trading, we just need to remember that is an  
11 interim situation where you've got a finalized set  
12 of requirements, versus in Europe, a  
13 still-to-be-finalized set of requirements.

14 I think when we've got the European  
15 regime finalized, the regime, from a regulatory  
16 standpoint, would be extremely comparable -- and,  
17 therefore, regulation will not be a driver of  
18 where business is done, and there will be other  
19 factors that will influence where business is  
20 done, but it will not be regulation.

21 And therefore, at that stage, we won't  
22 need things like top-up requirements.

1                   MR. NIXON: David, I don't disagree with  
2 your comment at all, other than I would suggest  
3 that many cases around the world, it's the  
4 regulator that you know, it's the regulator that  
5 you're most comfortable in dealing with. And  
6 having somebody in a foreign county -- or in Asia  
7 -- having regulatory oversight by the CFTC is  
8 somewhat difficult for them to actually understand  
9 and comprehend, versus their local regulator.

10                   And I think that would probably still  
11 apply in Europe, although I do agree with you that  
12 the rules will look very similar.

13                   MR. SERAFINI: Commissioner O'Malia  
14 (inaudible).

15                   COMMISSIONER O'MALIA: I guess I'd like  
16 to get the GMAC's opinion -- the member panel's --  
17 their opinion on the path forward for the next 18  
18 to 24 months is -- we've kind of defined where we  
19 have our differences. Should we try to breathe  
20 life into the QMFT? Should we pass an exempt SEF?  
21 Should we get on some sort of comparability regime  
22 now to recognize MTFs?

1                   And I would also ask that you opine on  
2                   what the recognition regime for Europe might be.  
3                   You know, should they recognize SEFs? Is there a  
4                   comparable -- you know, Kim raised the issue of  
5                   DCMs, et cetera, and SEFs. Where do we stand on  
6                   that? What do we do for the next 18 months? Do  
7                   we throw up another idea that we have little to no  
8                   understanding will it work or not -- or what's the  
9                   best and most efficient path forward to really  
10                  bring trading onscreen?

11                  CHAIRMAN WETJEN: Let me just say real  
12                  quick in response to Scott's question -- I don't  
13                  think the solution would be an exempt SEF  
14                  rulemaking, although we'll have to continue  
15                  working on that. And I say that because there  
16                  wouldn't be anything to compare it to until MIFID  
17                  is implemented. So, we'd have to have an interim  
18                  solution in place, up until the time MIFID is  
19                  fully implemented.

20                  Disagree with that, Vince, or Scott, or  
21                  David -- sorry.

22                  MR. VAN WAGNER: I think that's right.

1 David Bailey can probably speak to the  
2 circumstances or the authorities that FCAA has  
3 that are unique. But when we had discussions  
4 prior to drafting the MTF letter with European  
5 regulators, it was quite clear that they really  
6 did not have anything that they were going to be  
7 able to offer us that would come anywhere close to  
8 what the conditions that we put into the letter.

9 We were more encouraged, frankly,  
10 because there are mechanisms that the FCA has to  
11 close that gap, and to have less topping-up, I  
12 guess, as David would describe it.

13 But, I mean, fundamentally, when there  
14 is such a gulf, it is very hard to do anything  
15 other than for this Commission to, say, not impose  
16 any sort of SEF requirements at all, because it's  
17 really a very distinct discrepancy, as far as  
18 swap-dedicated platform regulations go.

19 I mean, David maybe can talk about the  
20 mechanisms that they can at least bridge that gap  
21 to a large extent, but --

22 MR. MCGONAGLE: And as I hear it, I

1 think the one focus we have is this very strong  
2 need to be proactive, as Commissioner O'Malia and  
3 Chairman have touched on -- sort of, how do we get  
4 to the future state, recognizing that where CFTC  
5 facilities are, and how, you know, the mandatory  
6 trading is only three months old.

7           And we're working, still, on  
8 implementation of trading, on the SEF facilities,  
9 while, at the same time, sort of recognizing the  
10 significant question about fragmentation and  
11 attraction, frankly. You know, we want people to  
12 trade on SEF. We want it to be competitive. We  
13 want these markets to do what they're intended to  
14 do, which is, you know, handle this price  
15 discovery process and these risk-related issues.

16           And so we can't wait. We can't wait 18  
17 months. And so, you know, we have been working in  
18 these communications, and, you know, something  
19 will come out of it. The expectation might not be  
20 -- you know, if QMTF isn't a viable option, then  
21 an entity will go that way. And if it's not a  
22 viable option, you know, the SEF alternative might

1       come up.

2                       So, I guess this is my way of saying  
3       that, you know, we continue to work on this issue.  
4       And, frankly, that's one of the reasons why we're  
5       here -- is to get the feedback about, what are the  
6       areas that we should be focused on? And the items  
7       that we talked about earlier, you know, on this --  
8       on the pre-trade transparency in particular, sort  
9       of, where do we crystalize around so we have a  
10      sense that we're going in the right direction?  
11      And I think that's very helpful.

12                      MR. SERAFINI: Chris, did you give up?

13                      MR. ALLEN: No, I was just going to make  
14      a point that this question of who is using and  
15      who's prepared to use SEF -- I mean, typically,  
16      for many of the overseas institutions -- the  
17      non-U.S. institutions that are already swap  
18      dealers -- they're perfectly happy to use SEFs --  
19      and, in fact, are contributing prices into SEFs at  
20      the moment, to the extent that we're essentially  
21      talking about IFQ markets.

22                      Many of us, as dealers, are, quite

1 frankly, agnostic as to whether they're streaming  
2 those prices into SEFs, MTFs, or other types of  
3 execution venue, and that's what's happening now.

4 But the reluctance does derive, in part,  
5 from parts of the customer and client base, who  
6 are not so keen about being brought into the scope  
7 of U.S. regulatory oversights in circumstances  
8 where, were it not for the execution of business  
9 through a given platform, they otherwise would not  
10 have been caught.

11 So, I think it's worth bearing in mind  
12 that the discussion that people are having around  
13 the incentives or disincentives -- and the  
14 motivation factors behind who's using the  
15 platforms -- is not really a question of sort of  
16 foreign swap dealers (inaudible) that sort --  
17 they're perfectly happy to use these platforms.  
18 It's the underlying end users who are not  
19 registered swap dealers or MSPs.

20 CHAIRMAN WETJEN: Wally?

21 MR. TURBEVILLE: In going forward, one  
22 thing I want to make very clear -- a different

1 point than was put forward. It was put forward  
2 that the equity markets were used, despite  
3 regulation, and we got it right somewhere. The  
4 regulation of derivatives is for a completely  
5 different set of purposes. So, if people aren't  
6 using them, that could be a very good indication  
7 that we got it right.

8 So, in whichever way forward we decide  
9 to go, let's assume that the right analysis is, we  
10 actually got it right. The purpose should be to  
11 get people to use it through incentives, both and  
12 negative -- whichever incentives -- but to do it  
13 in a way that's perhaps better.

14 MR. SERAFINI: Kim Taylor?

15 MS. ADRIANCE: I had been thinking about  
16 Bob's point about the equity market, too. And  
17 here's what I think is the difference: There's  
18 not really a good alternative way to get exposure  
19 to U.S. equities other than to trade in that  
20 regime. And there is a perfectly good way to get  
21 exposure to derivatives without touching the  
22 CFTC's regime because you happen to go first.

1           And I think it's perhaps clear that some  
2 elements of the regime are less attractive than  
3 not having any kind of restrictions. If you can  
4 trade bilaterally in Europe, and you're not  
5 subject to CFTC regulation, or you're not subject  
6 to pre-trade transparency, or you're not subject  
7 to anything of a trading nature -- because those  
8 rules aren't ready yet -- then it's a pretty easy  
9 choice to make, to be voluntarily subject to extra  
10 regulation or not.

11           And I'm not sure you'll be able to make  
12 an evaluation, unfortunately, about which regime  
13 is the better one that people actually prefer  
14 until there's more than one regime in place.

15           MR. SERAFINI: Emily, did you want say  
16 something?

17           MS. PORTNEY: I was just going to, I  
18 guess, kind of add, perhaps, on both these points  
19 -- but, Chris, your point about the end user, you  
20 know, is -- I mean, I think we just can't lose  
21 sight of the fact that, ultimately, U.S. Persons,  
22 the end user, is locked out of major pools of

1 liquidity -- of basically non-dollar liquidity.  
2 And that is not good for the U.S. and for end  
3 users.

4 And I think it might very well be that  
5 there is an interim solution, where, you know,  
6 some forms of principles- based solution that, you  
7 know, MTFs, et cetera, you know, for a period of  
8 time are recognized -- and at least it goes  
9 towards the promotion of screen-based trading and  
10 more transparency, until the regimes are fully,  
11 you know, completed.

12 But at the moment, you're stuck in a  
13 situation where it's truly, I think, detrimental  
14 to both, you know, U.S. broker-dealers, as well as  
15 the end user.

16 CHAIRMAN WETJEN: Raj?

17 MR. MAHAJAN: Yeah, I just want to make  
18 two comments.

19 One, since Bob's not in the room, it's a  
20 little easier to make this comment. But, I mean,  
21 equity markets didn't start out perfectly in the  
22 '90s. I mean, we had a duopoly. We had scandals

1 of collusion. It wasn't always great. And now,  
2 arguably, because the SEC stepped in, we have a  
3 far too complicated market structure today.

4 So, I think that using that as a paragon  
5 of virtue is not necessarily appropriate.

6 The second thing I would say is, in and  
7 around -- I feel the conversation is really  
8 limiting us to two choices -- around SEFs and  
9 foreign SEFs. I mean, there is a third way, which  
10 is, you know, exchange-traded instruments,  
11 deliverable swap futures.

12 And in particular, you address, really,  
13 four aspects of that -- four aspects of the  
14 problem. So, you get price transparency. It's  
15 vertically integrated with the central  
16 counterparty. Some of the most liquid markets in  
17 the world are traded there.

18 And, increasingly, as a large  
19 participant in those markets, we're seeing your  
20 customers -- and this is really directed to the  
21 banks -- start to participate directly in those  
22 markets, especially with respect to interest

1 rates.

2           So, I wonder if we're really creating a  
3 false choice here between two different options,  
4 when there is a third way. But I suspect I'm  
5 going to get a lot of resistance to that, because  
6 that would -- in effect, you would (inaudible)  
7 banks.

8           MS. PORTNEY: Just for the record,  
9 actually, I think all of these things will exist  
10 over time. I don't think any of them are mutually  
11 exclusive. You will absolutely -- and we've  
12 already seen a growth in swap futures. You know,  
13 certainly, I think you'll get to do more exchange  
14 trading of swap-like contracts or products.

15           But, I mean, I think you'll continue to  
16 also still have a -- you know, a bilateral market  
17 will probably still exist to some degree. I mean,  
18 I think all of these things will coexist, but I  
19 think it's just a matter of timing.

20           And I still come back to the point that  
21 at this point in time, you are putting -- and we  
22 can't, for that much longer -- put the U.S. person

1 at a disadvantage, in terms of trying to be able  
2 to kind of hedge the risk, et cetera. And we do  
3 need to think of a solution.

4 In the interim, I think you're right.  
5 This whole marketplace will evolve, and we will  
6 see all of those things happen.

7 CHAIRMAN WETJEN: Raj, do you see any  
8 points of resistance, though, to market  
9 participants, particularly on the buy side,  
10 embracing those markets? Like, what, if anything,  
11 does the CFTC need to thinking about there?

12 If they have a need, a hedging purpose,  
13 an investment purpose --

14 MR. MAHAJAN: Well, I mean, I don't want  
15 to steal Kim's thunder here, but, I mean, the CME  
16 is actively targeting the buy side to come and  
17 trade futures, block futures, and deliverable swap  
18 futures. They're speaking to the sort of  
19 household names on the buy side around this.

20 Now, you know, 12 to 18 months ago, I  
21 would've said that there was more reluctance. But  
22 as a direct market participant in those products,

1 we're seeing an extraordinary amount of  
2 participation, as evidenced by order sizes coming  
3 through those markets to suggest that we are  
4 seeing more adoption of those products.

5 And you solve a lot of the problems I've  
6 been listening to here by adopting those products  
7 around price transparency, a point that Adam  
8 brought up. The regulatory burden that John and  
9 Robert brought up, the CCP problem that Supurna  
10 brought up -- I mean, they're all addressed with  
11 skipping that step and going directly to  
12 (inaudible).

13 CHAIRMAN WETJEN: Jun, you've been very  
14 patient. Did you want to say anything?

15 MR. MIZUGUCHI: Well, thank you.  
16 Commissioner O'Malia raised the issue of  
17 (inaudible) 16-month gap, until the (inaudible)  
18 implemented sometime later. Well, after a similar  
19 issue we have in Japan, as well -- because, as I  
20 said (inaudible) by September 2015, which might be  
21 earlier than the MIFID case.

22 Well, in that case, we are putting some

1 requirements of the Japanese (inaudible) and,  
2 also, the trading obligation by that time. In  
3 that case, well, I don't know when this draft  
4 exemption (inaudible) rules will come out, but I  
5 think we may need to have a similar arrangement  
6 with our European colleagues, like in terms of  
7 arrangement so that if (inaudible).

8 So, I think then you have bilateral  
9 (inaudible) so as not to have any market  
10 disruptions.

11 CHAIRMAN WETJEN: John, did you want to  
12 weigh in?

13 MR. PARSONS: I just have a question  
14 that's mostly, actually, for Emily -- because you  
15 used this language as if U.S. persons don't have  
16 access to certain liquidity pools and certain  
17 currencies, as if they're blocked. But Raj was  
18 talking about one avenue. John had described  
19 another avenue. It's not currently used, but I  
20 don't see why it's not feasible -- and I'm happy  
21 to hear about, why is it not feasible to provide  
22 that same avenue to customers for other

1 currencies?

2 MS. PORTNEY: Yeah, I guess just to  
3 clarify -- so I think, certainly, swap futures are  
4 a way that, you know, U.S. participants can hedge  
5 risk. But they are relatively new products. You  
6 know, there are relatively, you know, few of them.  
7 They're not widespread. I mean, at some point,  
8 there will be many more, and that's great, and  
9 could potentially be used in much more scale.

10 But at the moment, it's just going to  
11 take time for that to even be thought of as a full  
12 alternative to the rest of the swaps market.

13 MR. PARSONS: But the (inaudible) market  
14 is the most liquid market in the world -- futures.

15 MS. PORTNEY: And the other thing I was  
16 going to just say is, just from a -- you know, if  
17 an MTF registered as a SEF, a U.S. person could  
18 access it, but, as we know, no one has done that  
19 yet. No MTF has done that.

20 So, to the extent there are liquidity  
21 pools that are centered in certain jurisdictions,  
22 where the SEF is not registered, then it is -- for

1 all intents and purposes, a U.S. person cannot  
2 access that liquidity pool, because they have to  
3 trade on a SEF.

4 MR. MAHAJAN: Well, John mentioned  
5 having it; it's just that only dollars were being  
6 used. But it's feasible in other currencies,  
7 right?

8 MR. PARSONS: Yes, one of the reasons  
9 that we have a dually registered SEF and MTF is so  
10 that European clients can be comfortable dealing  
11 under both regulatory regimes.

12 Quite honestly, we thought that that was  
13 what was going to give some regulatory certainty  
14 to clients on a cross-border basis.

15 And just for a second, on what Raj said  
16 -- I think that, you know, Emily's right; these  
17 things evolve, and they take a period of time.  
18 And you're right; the euro-dollar market is an  
19 extremely liquid market. So is the foreign  
20 exchange market. So is the U.S. Treasury market,  
21 and so is the interest rate swap market. And they  
22 are all traded off exchange.

1                   And it's going to be a long time before  
2 we can get a \$500 trillion market to just trade on  
3 an exchange. I'm sure Kim would be very excited  
4 about that, but it's going to obviously take a  
5 little while before we get anywhere close to that.

6                   And so, consequently, you are going to  
7 have to manage change in an evolution, not in a  
8 revolution over the course of the next number of  
9 years, quite frankly.

10                   MS. ADRIANCE: If I could raise the  
11 issue of, you know, there's been definitely a lot  
12 of issues raised regarding what's necessary, that  
13 there's an interim period. Certainly, aside from,  
14 you know, the fact that they're -- obviously, over  
15 time, the C staff will look at what might be done  
16 in the interim period, we are still trying to move  
17 forward with a rulemaking.

18                   And, you know, I know that there was  
19 questions sent out -- and just to point out that  
20 those questions, besides following regulatory  
21 approaches -- which I think we've covered to some  
22 degree -- we had questions about reporting,

1 financial resources, financial integrity of  
2 transactions, effects on swap market liquidity,  
3 monitoring of trading and trade processing, system  
4 safeguard and compliance -- does anyone have  
5 anything more specific on one of those issues that  
6 they want to pass onto us, so that staff actually  
7 can, you know, take into account your views on  
8 those issues?

9 It would be really helpful to them.

10 MR. MCGONAGLE: So, I think, you know,  
11 what you're hearing is, we're evaluating what our  
12 obligations are, what was, you know, the current  
13 registration that we face for SEF, and if there is  
14 going to be an exempt category. And we don't have  
15 standards like they do for the exempt DCO, but we  
16 do know that, you know, the correlation between  
17 the exempt DCO and an exemption category for a  
18 foreign swap execution facility would be  
19 important.

20 So, we might need to, say, catch up in  
21 some respects to what the exempt DCOs rulemaking  
22 team is already doing. Phyllis touched on the

1 fact that, you know, they have words on paper --  
2 pretty concrete. We're not there yet -- and in  
3 part because we're trying to get crystalized  
4 around some of these concepts.

5           And so talking about what Riva has just  
6 touched on -- reporting obligations -- I know  
7 Commissioner O'Malia had a comment at the  
8 beginning of the day today -- but if we can center  
9 on some of those items in the remaining time that  
10 we have here -- if there is any feedback that you  
11 think that we should take away on reporting  
12 obligations for this exempt category, system  
13 safeguards -- sort of, where do we draw the line  
14 between principles and prescriptive approach, and  
15 making a determination of, what is a comparable  
16 and comprehensive framework so we can think about  
17 applying it?

18           So, we sort of put that out there in one  
19 massive Q&A. And Riva can go through some of the  
20 topics again slowly, and we see whether, you know,  
21 in the time we have, whether there's some comments  
22 that make sense to throw out there and have a

1 discussion on.

2 MR. SERAFINI: Rama, did you have any --

3 MR. RAMASWAMI: You know, in the list of  
4 topics that we have, I think one of the things  
5 that it drives towards is to make all the SEFs  
6 look more and more like exchanges. And I think  
7 that the difference between a commoditized,  
8 high-volume, lower-value activity and a less  
9 voluminous but more high-value transactions is  
10 significant.

11 And I think that pushing everything into  
12 a commoditized, you know, set of rules as an  
13 exchange, I think, is not, you know, always the  
14 best road. I think the key here is to ensure a  
15 large number of such entities, or SEFs, or  
16 whatever platforms, as you would have a large  
17 number of brokers or a large number of banks  
18 (inaudible) kind of have very highly concentrated  
19 -- one or two execution facilities that just  
20 commoditized these instruments over time.

21 And I think that commoditization versus  
22 specialization option is really a choice that the

1 end customer makes, and should not be driven  
2 beyond the point by regulation. I think that's  
3 something that, if you go on each of those topics  
4 by principles -- you know, should SEF fail? No,  
5 the answer's no; it should never break down,  
6 right? Should it report within a second price?  
7 Yes.

8 So, you'll end up very much defining  
9 what is a commoditized exchange platform  
10 definition today. So, I think that's something to  
11 worry about when you go through each of these  
12 topics.

13 MS. ADRIANCE: If I can ask just a  
14 further question on that -- obviously, Commission  
15 has, in the past, had regulations, guidance --  
16 whatever they call it -- anywhere from very  
17 specific requirements to principles.

18 And I understand your point. What we're  
19 trying to understand is -- for instance, just  
20 reporting. When it comes to reporting, is there  
21 something on this foreign-based swap execution  
22 facility? Should it be appropriate that a foreign

1 home country regulator have a reporting  
2 requirement that they place on that facility?  
3 Should there be any requirements that we should  
4 have, or should it be there should be no reporting  
5 requirements?

6 Is it appropriate that that foreign home  
7 country regulator required a foreign swap facility  
8 to provide reports of post-trade transparency to  
9 the marketplace, to provide pre-trade  
10 transparency? It was mentioned that that's  
11 something that SEFs can offer.

12 Is there something in between the two  
13 extremes that is appropriate that we should be,  
14 you know, considering? We have this requirement;  
15 do we make this finding? Is there something  
16 that's between these two extremes that is  
17 appropriate to place in terms of differences in  
18 reporting -- some standard that we should find is  
19 necessary for us to find that that foreign  
20 regulator has the appropriate regulatory oversight  
21 and supervision?

22 MR. RAMASWAMI: Yeah, I guess it's fair.

1 And the principles there are pre-trade price  
2 transparency and post- trade exposure reporting.  
3 And I think that's what we've got to push for.  
4 Every platform should have, somewhere or the  
5 other, the post-trade exposure requirements  
6 (inaudible). And, similarly, the pre-trade price  
7 transparency (inaudible). But whether it needs to  
8 be specifically here or not, I think needs to  
9 evolve.

10 MR. NIXON: Riva, can I also just say  
11 that in that -- just in regards to that one  
12 question -- or your point -- it's hard to find --  
13 you can't just leave it as let the Wild West  
14 decide. There needs to be something between here  
15 and there -- between the principle and some sort  
16 of specific rules.

17 But, also, I think you should take into  
18 consideration, what are the rules that can be  
19 implemented by the provider that is actually going  
20 to make his service more competitive to somebody  
21 else's service? Because, to a certain extent, you  
22 know, service providers often lead with

1 innovation. And if they can provide services that  
2 they believe are better -- they're more compliant,  
3 they're more robust, they report better -- those  
4 are the services that you're going to find  
5 institutions are probably going to turn to.  
6 They're going to drive to that highest common  
7 denominator.

8           So, I just think that needs to be  
9 considered as you make your determinations of what  
10 needs to be very specific, versus what needs to be  
11 more of a principle.

12           CHAIRMAN WETJEN: Supurna?

13           MS. VEDBRAT: Yeah. To, you know, your  
14 question on reporting -- you know, here in the  
15 States, we have the SEFs do the reporting, and,  
16 you know, whether we're talking about SEF trading  
17 or clearing, reporting is, like, one- sided. The  
18 buy side actually is not really reporting, unless,  
19 you know, buy side to buy side trades. And, you  
20 know, that hasn't begun yet.

21           You know, if something like that could  
22 be maintained, you know, that would be a preferred

1 route for the end user, because in certain  
2 instances overseas, there's dual-sided reporting.  
3 And, you know -- but, first of all, it has yet to  
4 be, you know, commoditized and, you know, made to  
5 work efficiently.

6 But, also, you know, just for the  
7 broader end user, it is a completely new  
8 requirement, and it is, you know, to some extent,  
9 very cumbersome.

10 So, we'd like to see our current  
11 reporting structure somehow persist, you know, in  
12 the exemptive order. I don't know how you would  
13 do that, because it may be less than what's done  
14 international.

15 CHAIRMAN WETJEN: There's nothing magic  
16 about 3:30. So, unless -- I didn't mean to  
17 interrupt -- Riva, if you had more questions --  
18 no? Okay.

19 MS. ADRIANCE: We have a number of  
20 questions if people are willing to sit here and  
21 answer our questions. We still -- I can keep on  
22 going with questions.

1                   MR. MCGONAGLE: But I do think -- I  
2                   mean, there's some of the feedback that we've  
3                   gotten this afternoon -- we're sort of able to  
4                   pull this in and come back out to participants,  
5                   and have more focused discussions around some of  
6                   these elements, certainly. But we wanted to get  
7                   the high level -- sort of where the reaction is --  
8                   and we've heard that, I think, throughout the  
9                   course of the last two hours -- you know, where,  
10                  structurally, the market should go, and how, in an  
11                  exempt SEF, how we might facilitate that  
12                  relationship. So --

13                  MS. ADRIANCE: I would just want to make  
14                  one kind of ending comment from our perspective.

15                  I think you would want to be careful in  
16                  examining temporary exempt SEF -- or temporary SEF  
17                  relief -- MTF relief regime -- that you consider  
18                  the implications of the exemptions that you're  
19                  allowing on the ability for the truly registered  
20                  SEFs to be viable -- because if they have to  
21                  operate in a very unlevel playing field, that is  
22                  going to be a recipe for difficulty in the SEF

1 regime-building and attraction, I would think.

2 MS. VEDBRAT: I just want to add one  
3 more thing. Will the exempt SEF have the ability  
4 to put in the request or made available to trade?

5 I think that would be a little bit of --  
6 yeah, I mean, that would be a concern.

7 MR. MCGONAGLE: To submit a product for  
8 (inaudible). Oh, I don't think so. I think it's  
9 limited only to the -- I think (inaudible) only  
10 limited to a registered SEF.

11 MS. VEDBRAT: Yeah.

12 MR. VAN WAGNER: Right. I wouldn't  
13 anticipate -- but I would think market forces are  
14 such that you're going to find, typically -- if  
15 something is mature enough to be made available  
16 for trading, you're going to have a SEF who's  
17 probably going to list that product and do just  
18 that.

19 So, yes, we're not envisioning that an  
20 exempt SEF could trigger it. But, I mean, you  
21 could speak from your perspective of watching an  
22 exempt SEF with a good product. What would you

1 do?

2 MS. VEDBRAT: Well, I mean, if we are,  
3 you know, looking at this, you know, for the next  
4 12 months, in order to be able to give the U.S.  
5 person access to some of the non-dollar traded  
6 swaps that may not be offered by, you know, the  
7 registered SEFs, then how do we solve for that?

8 I mean, I'm not suggesting that we allow  
9 them to. That would not be a good idea. You  
10 know, but, you know, what I'm hearing is that our  
11 interim solution -- are we giving access to the  
12 U.S. person, or, you know, maybe alongside that,  
13 we also want to encourage the non-U.S. Person to  
14 start trading electronically.

15 MR. MCGONAGLE: Yes, on a duly  
16 registered SEF.

17 MS. ADRIANCE: Just to raise another  
18 question -- since I think there was a pause there  
19 -- just to pick another subject, which is  
20 monitoring of trading and trade processing, in  
21 terms of -- you know, in the past, you've had the  
22 U.S. system, which was -- you know, in the futures

1 markets, there's large-trader reporting that comes  
2 to us. The Commission is very involved in the  
3 oversight, plus you separately have each of the  
4 exchanges, who do their own monitoring of trading.

5           So, there's kind of a dual system going  
6 on. There's a lot of oversight and a lot of  
7 attention to the markets that either on realtime  
8 or are on very soon thereafter -- T+1 -- that goes  
9 to what is happening in the marketplace. And,  
10 certainly, as we look at our system, we see  
11 changes around the world. There is beginning to  
12 be some changes that are in -- you know, we're  
13 beginning to see, for instance, in Europe, there  
14 is now going to be requirements for position  
15 limits. There's going to be other requirements.

16           But we still have to make a decision --  
17 again, back to our standard that we have to make  
18 this finding. And one thing we're trying to sort  
19 out is, here, we have this requirement, in a  
20 sense, on ourselves, as well as on the  
21 marketplace.

22           Is that appropriate, or is it -- where

1 we're looking to foreign entities, is there  
2 certain requirements that you'd want to see just  
3 on the marketplace that they carry out? Is it  
4 appropriate that we would expect, also, that a  
5 regulator itself carry out some kind of oversight  
6 when it comes to monitoring of markets? And that  
7 is monitoring and surveillance of markets.

8 CHAIRMAN WETJEN: So, left with us -- no  
9 worries.

10 MR. SERAFINI: Well, maybe this is a  
11 good place to wrap it up. I just want to know if  
12 Chairman Wetjen or Commissioner O'Malia -- do you  
13 guys have any closing remarks you'd like to make?

14 COMMISSIONER O'MALIA: Well, first of  
15 all, let me thank our witnesses and our staff that  
16 have contributed to this debate -- and, certainly,  
17 our panelists, who have traveled and spent a lot  
18 of time here.

19 The first panel was very interesting,  
20 and has really made me think about a lot of things  
21 that the Chairman and I have been chatting up here  
22 about, and thinking about, and turning around and

1 thinking, "How do we do this differently?" as is  
2 the debate around the second panel, too.

3 And I think we really need to look at  
4 the data -- figure out how the market is moving,  
5 what changes are in place, and how we set  
6 ourselves up working with our colleagues  
7 internationally, to make sure that we close the  
8 differences as quickly as possible.

9 And I've had an opportunity to talk to  
10 David -- and appreciate his candor and  
11 thoughtfulness on these issues -- and, certainly,  
12 his contribution to come here -- and Jun, as well.  
13 Thank you for your contribution to come this  
14 distance, representing both your governments --  
15 and others, frankly.

16 So, thank you, everyone, for  
17 contributing.

18 CHAIRMAN WETJEN: Thanks, Commissioner  
19 O'Malia. I have to say -- I have to make, I  
20 think, some similar comments.

21 I think that today's meeting has perhaps  
22 raised more issues than it has closed out, and I

1 think that's true, probably, of potentially both  
2 panels. And so in that respect, it's been very,  
3 very valuable. In other respects, perhaps a  
4 little disappointing -- but I think all of it is  
5 in the public's interests, and in the interests of  
6 the markets that those around this table care very  
7 much about and are heavily involved in.

8           So, very, very useful, productive  
9 session today, and I thank everyone for coming --  
10 especially our friends from Asia -- and our  
11 panelists, Jun and David -- really appreciate your  
12 valuable input today. It was very helpful to the  
13 conversation.

14           Thank you very much.

15           MR. SERAFINI: Thank you everybody for  
16 being here. I also want to thank the CFTC staff  
17 -- (inaudible) and her team -- for all the work  
18 they did to set this up logistically.

19           So, with that, as the GMAC DFO and  
20 temporary Chair of the Committee, I adjourn this  
21 meeting.

22           Thanks.

1 (Whereupon, at 3:20 p.m., the  
2 PROCEEDINGS were adjourned.)

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CERTIFICATE OF NOTARY PUBLIC

DISTRICT OF COLUMBIA

I, Stephen K. Garland, notary public in  
and for the District of Columbia, do hereby certify  
that the forgoing PROCEEDING was duly recorded and  
thereafter reduced to print under my direction;  
that the witnesses were sworn to tell the truth  
under penalty of perjury; that said transcript is a  
true record of the testimony given by witnesses;  
that I am neither counsel for, related to, nor  
employed by any of the parties to the action in  
which this proceeding was called; and, furthermore,  
that I am not a relative or employee of any  
attorney or counsel employed by the parties hereto,  
nor financially or otherwise interested in the  
outcome of this action.

(Signature and Seal on File)

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Notary Public, in and for the District of Columbia

My Commission Expires: May 31, 2018

