

ROBERT F. (BOB) SMITH, OREGON,
 CHAIRMAN
 LARRY COMBEST, TEXAS,
 VICE CHAIRMAN
 BILL BARRETT, NEBRASKA
 JOHN A. BOEHNER, OHIO
 THOMAS W. EWING, ILLINOIS
 JOHN T. DOOLITTLE, CALIFORNIA
 BOB GOODLATTE, VIRGINIA
 RICHARD W. POMBO, CALIFORNIA
 CHARLES T. CANADY, FLORIDA
 NICK SMITH, MICHIGAN
 TERRY EVERETT, ALABAMA
 FRANK D. LUCAS, OKLAHOMA
 RON LEWIS, KENTUCKY
 HELEN CHENOWETH, IDAHO
 JOHN N. HOSTETTLER, INDIANA
 ED BRYANT, TENNESSEE
 MARK FOLEY, FLORIDA
 SAXBY CHAMBLISS, GEORGIA
 RAY LAHOOD, ILLINOIS
 JO ANN EMERSON, MISSOURI
 JERRY MORAN, KANSAS
 ROY BLUNT, MISSOURI
 CHARLES W. "CHIP" PICKERING, MISSISSIPPI
 BOB SCHAFER, COLORADO
 JOHN R. THUNE, SOUTH DAKOTA
 WILLIAM L. JENKINS, TENNESSEE
 JOHN COOKSEY, LOUISIANA

98-7
 (32)
U.S. House of Representatives
Committee on Agriculture
 Room 1301, Longworth House Office Building
 Washington, DC 20515-6001

COMMODITY FUTURES TRADING COMMISSION
 RECEIVED
 OFFICE OF THE SECRETARY
 JUN 3 2 26 PM '98
 CFTC
 CHARLES W. STENHOLM, TEXAS, RANKING MINORITY MEMBER
 GEORGE E. BROWN, JR., CALIFORNIA
 GARY A. CONDIT, CALIFORNIA
 COLLIN C. PETERSON, MINNESOTA
 CALVIN M. DOOLEY, CALIFORNIA
 EVA M. CLAYTON, NORTH CAROLINA
 DAVID MINGE, MINNESOTA
 DAVID MINGE, ALABAMA
 BOB POMBO, NORTH DAKOTA
 TIM HOLDEN, PENNSYLVANIA
 SCOTTY BAESLER, KENTUCKY
 SANFORD D. BISHOP, JR., GEORGIA
 BENNIE G. THOMPSON, MISSISSIPPI
 SAM FARR, CALIFORNIA
 JOHN ELIAS BALDACCI, MAINE
 MARION BERRY, ARKANSAS
 VIRGIL H. GOODE, JR., VIRGINIA
 MIKE MCINTYRE, NORTH CAROLINA
 DEBBIE STABENOW, MICHIGAN
 BOB ETHERIDGE, NORTH CAROLINA
 CHRISTOPHER JOHN, LOUISIANA
 JAY W. JOHNSON, WISCONSIN
 LEONARD L. BOSWELL, IOWA

May 25, 1998

COMMENT

PAUL UNGER,
 MAJORITY STAFF DIRECTOR
 JOHN E. HOGAN,
 CHIEF COUNSEL
 STEPHEN HATERIUS,
 MINORITY STAFF DIRECTOR
 VERNIE HUBERT,
 MINORITY COUNSEL

(202) 225-2171
 (202) 225-0917 FAX
 www.house.gov/agriculture/

The Honorable Brooksley Born
 Chairperson
 The Commodity Futures Trading Commission
 1155 21st Street, N.W.
 Washington, D.C. 20581

Dear Chairperson Born:

The Commodity Futures Trading Commission is now considering an application to approve a new futures exchange called the Cantor Financial Futures Exchange (CFFE). That application has been filed by various entities affiliated with Cantor Fitzgerald L.P. and the New York Cotton Exchange. We are writing to you because of the unique nature of this application and the possible legal and policy questions which are raised.

All futures exchanges today are membership organizations. CFFE would be the first proprietary exchange, an exchange owned or controlled by a single private firm, for futures trading. We question whether the kind of proprietary exchange CFFE proposes is compatible with the Commodity Exchange Act. For example, Cantor would control CFFE's board by appointing 8 of 13 directors, trade for its own account on CFFE, employ all Terminal Operators who execute trades on CFFE and control the dissemination of pricing data for CFFE transactions. That concentration of dominant market power in one firm raises possible anti-competitive and conflict of interest concerns that could undermine public confidence in CFFE or proprietary exchanges, in general.

Furthermore, proprietary exchanges, by definition, raise special fitness issues. If a firm controls an exchange's board, should that firm only be required to meet existing fitness standards for sitting on exchange boards or even a more exacting standard, since that single firm rather than a majority of members would decide policy for a proprietary exchange? Should the firm controlling the exchange or its affiliates be barred from trading on the exchange or in related cash markets, to the same extent as current exchange officials and personnel? What special market integrity problems do proprietary exchanges create?

JUN 3 5 23 PM '98
 COMMODITY FUTURES TRADING COMMISSION FOR RECORD PUBLIC RECORD

Page Two
May 25, 1998

There is also the question of public interest, a test required by the CEA for approval of any contract market designation. Price discovery and risk management may be compromised when a proprietary exchange, like CFFE, intends to trade futures that replicate already mature liquid markets offered on a traditional exchange. This concern was well framed in a recent comment letter to the Commission from the Chicago Mercantile Exchange, concluding that when a proprietary exchange applies to invoke trading practices not permitted on the principal exchange market, the test must be whether the principal market is adversely affected. Otherwise, Internet exchanges can easily be established for the sole purpose of passing rules to permit upstairs trading that will drain liquidity from the true competitive marketplace.

In most respects, the Commodity Exchange Act does not provide specific answers to these critical policy questions. This is an area Congress may want to consider, among others, in the context of reforming the statute to deal with the forces of financial modernization. We presume you would share our concern that the Commission not establish any precedents in this area that would complicate that reform process by offering a blueprint for others to follow in connection with futures trading in other commodities. We would be pleased to begin now, working with the Commission, to identify the areas that Congress should address in the next Congress to ensure the Commodity Exchange Act reflects current market conditions as well as probable developments.

In any event, the Commission's staff has found CFFE's application to be materially incomplete, due to significant substantive issues it presented, and suspended consideration of that application. We assume that, when and if the CFFE application is deemed to be complete and the suspension is lifted, the Commission will solicit public comments on that complete version of the application. Certainly public scrutiny of the completed application is appropriate, especially given the novel issues this application raises.

Sincerely,



The Honorable Robert F. Smith
Chairman



The Honorable Thomas W. Ewing
Chairman
Subcommittee on Risk Management
and Specialty Crops