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secretary

From: Don Chance [dmc@vt.edu]
Sent: Monday, September 21, 1998 8:58 AM
To: secretary@cftc.gov
Subject: comments regarding regulation of OTC derivatives

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These comments are provided in regard to the CFTC's concept release on
regulation of OTC derivatives.

1998 SEP 22 A 7:40

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The OTC derivatives market has been an excellent example of the social
optimality of financial markets. Largely unfettered by government
regulation and stimulated by competition from exchanges in the U. S. and
around the world, the OTC market has developed into one of the most
economically successful phenomena in our markets. In fact they have been
so successful that the CFTC now seems to feel that it must regulate them,
in spite of the absence of evidence to suggest that such regulation is
necessary.

COMMENT

Two reasons seem to exist for such calls for increased regulation: (1) U.
S. futures exchanges want to see OTC regulation, arguing that the playing
field is not level without it, and (2) the huge size of the OTC market is a
threat, not only to the futures exchanges, but also to the CFTC, its
regulator. Neither reason is justified.

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Futures exchanges will indeed feel a competitive threat from OTC markets
and the CFTC worries that its base of power will erode. But the OTC
market, the futures exchanges and the regulators need each other.
Tampering with a system whose long-term viability so far appears only to be
a competitive threat to futures exchanges and erode the base of regulatory
power makes no sense whatsoever. Our markets have evolved to where they
are today, not because of government regulation, but perhaps even in spite
of it.

Leave well enough alone. When John Q. Public starts buying swaps at
Merrill Lynch some justification for public protection could be given. It
will be a long time, however, before Merrill Lynch would find it sensible
from a risk-return point of view to trade with Mr. Public. In the
meantime, we should let these markets continue to evolve and be a model for
the rest of the world.

Don