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UNITED STATES OF AMERICA

COMMODITY FUTURES TRADING COMMISSION

ROUNDTABLE DISCUSSION

ON

PROPOSED RULES ON ACCESS TO

AUTOMATED BOARDS OF TRADE

Tuesday, April 20, 1999

1:05 p.m.

Hearing Room 1000
1155 21st Street, N.W.
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C O N T E N T S

P R O C E E D I N G S

CHAIRPERSON BORN: I'd like to welcome all of you to this roundtable discussion of the proposed rules of the Commodity Futures Trading Commission on access to automated boards of trade.

I am Brooksley Born, Chairperson of the Committee, and I welcome you on behalf of all the Commissioners.

These proposed rules were published in the Federal Register on March 24, 1999 and are open for public comment until April 23, 1999. The Commission has received a number of requests to extend that comment period for 60 days, which it has not yet acted upon.

The purpose of the roundtable is to allow the Commission to receive the views of various industry participants on the proposed rules during the public comment period. The proceedings of the roundtable will be transcribed and placed on the public record for consideration by the Commission in its deliberations on the proposed rulemaking.

Invited participants here today represent U.S. and foreign exchanges, U.S. and foreign brokers, foreign

regulators and technology experts. I would like to on behalf of the Commission thank you all very much for your time and your willingness to participate in this roundtable and to provide the Commission with your views and your expertise.

I would like to start by going around the table and asking each of the roundtable participants to introduce himself or herself by name and organization, and I will start with Jerry on my right. Let me just say before you speak that you should press the button so that the red light comes on on your microphone.

MR. TELLEFSEN: My name is Jerry Tellefsen, and I am a senior vice president with the Tellefsen Consulting Group located in New York City. Our firm provides management consulting counsel to the financial services industry, and as such, we have worked with every exchange in the United States except for the Kansas City Board of Trade.

MR. PRYDE: I am David Pryde, and I am a managing director at JP Morgan, and I am responsible for JP Morgan's futures and options brokerage business.

MR. JOHNSON: I am Phillip Johnson, Skadden, Arps, Slate, Meagher and Flom.

MR. DeWAAL: Gary DeWaal, executive vice president and general counsel of FIMAT USA, a member of the Societe Generale [ph.] Group.

MR. MELAMED: Leo Melamed, Chicago Mercantile Exchange.

COMMISSIONER HOLUM: Barbara Holum, a Commissioner.

MR. WILMOUTH: Bob Wilmouth, National Futures Association.

MR. THORPE: Phillip Thorpe, managing director of the Financial Services Authority of the United Kingdom.

MR. MUNRO: John Munro, senior vice president for regulatory and compliance issues with Rolfe & Nolan.

MR. RAPPAPORT: Dan Rappaport, with the New York Mercantile Exchange.

COMMISSIONER SPEARS: Dave Spears, Commissioner.

MR. POTTHOFF: Volker Potthoff, general counsel of Eurex, Frankfurt.

MR. DOWNEY: David Downey, Timber Hill.

MR. HAHN: Arthur Hahn, Katten, Muchin & Zavis, and I act as U.S. counsel for LIFFE, IPE, and the Italian Stock Exchange.

MR. GORDON: Scott Gordon, Chicago Mercantile Exchange.

COMMISSIONER NEWSOME: Jim Newsome, CFTC.

MS. BERGIN: Kyra Bergin. I am a managing director and the regional general counsel for Salomon Smith Barney based in London.

MR. CRAPPLE: George Crapple, co-CEO of Millburn Ridgefield, CTA and CPO, and I am chairman of the Managed Funds Association.

MR. HERSCH: Ron Hersch, Bear Stearn & Company.

MR. BRENNAN: David Brennan, Chicago Board of Trade.

CHAIRPERSON BORN: Thank you all again for your willingness to attend.

We would also like to welcome the members of the public who are attending the roundtable and would like to invite you to submit any written comments you may have on the proposed rules by April 23, 1999 or by such date to

which the Commission may determine to extend the comment period.

I should note that because the Commission is in the middle of a proposed rulemaking proceeding, the Commissioners and I may not indicate our views on the substance of the proposed rulemaking. We are here to elicit your views to listen to you and to ask you questions. We are not here to deliberate or to decide any matters or otherwise improperly to prejudge the issues posed by the proposed rules.

However, all Commissioners recognize the urgency of taking action on the important issues posed by this proposed rulemaking and wish to decide the matters as quickly as possible. After the close of the public comment period, we plan to work together to achieve a majority view on these issues as quickly as possible and then either to hold a public meeting or to act by seriatim on them.

The proposed rules are an important step by the Commission in addressing significant technological changes in the industry. With the advent of electronic exchanges, screen-based trading may occur anywhere in the world and

does in fact occur currently in many countries. The proposed rules are an attempt to address the issue of trading in the U.S. on electronic exchanges otherwise located abroad through the use of automated trading systems in the U.S.

This rulemaking tackles cutting-edge technological issues. It also addresses the difficult issue of how best to accomplish our important regulatory mandate of protecting U.S. customers in an increasingly global marketplace.

The Commission is proposing a new Rule 30.11 that would establish a procedure for an electronic exchange operating primarily outside the United States to petition the Commission for an order that would permit use of automated trading systems that provide access to the board of trade from within the U.S. without requiring the board of trade to be designated as a U.S. contract market.

If appropriate, in light of the information provide in the petition, the Commission would issue an order under Section 4(c) of the Commodity Exchange Act that would allow a member of the petitioner board of trade or an affiliate thereof to operate automated trading systems that

provide access to the board of trade in the U.S. subject to specified terms and conditions.

The Commission also is proposing a new Rule 1.71 which would apply to both domestic and foreign firms. New Rule 1.71 would clarify that U.S. customers and foreign futures and foreign options customers may trade on an automated trading system of a U.S. contract market or an exchange exempted under Proposed Rule 30.11 if such system meets minimum requirements and provides certain safeguards such as automated checks for customer trading or position limits and credit limits.

The history of Commission consideration of U.S. screen-based trading of otherwise foreign exchanges is relevant to today's roundtable discussion. In September 1992, the Commission approved a cross-exchange access program between the Chicago Mercantile Exchange and MATIF, a French futures exchange, which permitted entry of orders on MATIF through Globex terminals located in the U.S. by CME and MATIF members. This action by the Commission thus authorized U.S. screen-based trading on MATIF.

Thereafter, in February 1996, the Commission's Division of Trading & Markets issued a no-action letter stating that the Division would not recommend that the Commission commence an enforcement action against DTB, a German futures exchange, if it were to place its terminals in the U.S. offices of its members and if it abided by certain terms and conditions. DTB later became Eurex and currently has terminals in this country under that no-action.

Thereafter, the Sydney Futures Exchange and the New Zealand Futures and Options Exchange requested that T&Ms issue similar no-action relief to be effective when they adopt electronic trading.

In addition, inquiries about U.S. screen-based trading were received more recently by the staff from three other exchanges, although none of them has to date submitted a request for no-action relief. LIFFE, for example, came to the staff in June of last year to inquire about possible screen-based trading in light of its decision that month to consider the initiation of electronic trading during 1999.

As a result of this increased interest in U.S. screen-based trading by such exchanges, the Commission determined in July 1998 that it was appropriate to address through the Commission's rulemaking process the subject of the use in the U.S. of automated trading systems that provide access to boards of trade whose primary operations otherwise take place outside the U.S.

The Commission issued a concept release on this subject on July 17, 1998 and received public comment on the concept release through October 7, 1998.

The proposed rules being discussed today were issued by the Commission in March 1999 and reflect the Commission's consideration of the public comments received during the public comment period on the concept release. They also reflect comments received by the Commission during two meetings of the Commission's Global Markets Advisory Committee, the report of that advisory committee's Working Group on Electronic Terminals headed by Leo Melamed, and the comments received by the Commission during a meeting of the Commission's Financial Products Advisory Committee.

Thus, today's roundtable discussion is the fourth time that the Commission has met in the last few months to receive the views of interested industry participants on the issues before us today.

The proposed rules seek to avoid imposing undue or duplicative regulatory requirements on exchanges by deferring where appropriate to the foreign regulator of the exchange seeking access to the U.S. market. The procedures set forth in the proposed rules are intended to provide an exemption from the contract market designation requirement and related requirements under the Commodity Exchange Act and Commission regulations to boards of trade established in a foreign country which wish to make their products accessible from within the U.S. via trading screens, the internet or other automated trading systems, provided they are subject to generally comparable regulation in their home countries.

Such exemption would avoid duplicative regulation, encourage other countries to allow access to the automated trading systems of U.S. exchanges and stimulate global competition and open markets in the futures industry.

Parenthetically, it should be noted that foreign boards of trade are currently eligible to provide for contract market designation under the Commodity Exchange Act and could do so as an alternative to applying for an exemption under the proposed rules.

The New York Board of Trade conducts floor-based trading in Dublin, Ireland on designated contract markets under U.S. law. Moreover, the Commission has approved a number of linkage arrangements between U.S. exchanges and foreign boards of trade relating to open outcry trading as well as the CME/MATIF linkage as to Globex trading. For example, the Commission approved a linkage between the Chicago Board of Trade and LIFFE during the last 2 or 3 years.

This roundtable will approach the proposed rules systematically, provision by provision, and elicit reactions and discussions from the participants on each subpart of the proposed rules. You should all have an agenda in the packet in front of you.

We will begin with discussion of the Standards for Exemption, then move to discuss the information to be

provided to the Commission by the petitioning board of trade, and then address the terms and conditions to be applicable to an exempted board of trade. Thereafter, we will address the standards to be applied to qualified Automated Order Routing Systems, or AORSs, which permit customer access to electronic trading.

The first topic for discussion on the agenda is the proposed Standards for Exemption. The exemption approach recognizes that screen-based trading in the U.S. in effect constitutes the operation of an electronic exchange in the U.S. under the CEA. This position is the same as that taken by the SEC with respect to screen-based securities trading. In its recent Tradepoint Order, the SEC exempted a low-volume electronic UK exchange from having to register as a national securities exchange under the U.S. securities laws in order to allow screen-based trading in the U.S. subject to various terms and conditions. I think you have all received a copy of the Tradepoint decision.

This approach to screen-based trading is currently also being followed by the UK, Australia and Japan. However, I understand that Australia may also require a

linkage between a foreign exchange and the Sydney Futures Exchange similar to the CME/MATIF link, as does Singapore.

The Commission staff is presently participating in a project of IOSCO on screen-based trading that involves a survey of foreign countries, and preliminary results indicate that France, Italy, and the Netherlands take a similar approach.

The exemptive approach provides legal certainty for petitioning boards of trade and those trading on them. The Commission has clear statutory authority to exempt transactions from the contract designation requirements under Section 4(c) of the Act. Absent such an express exemption, private parties could challenge boards of trade with automated trading systems in the U.S. as illegal under Section 4(a), requiring designation as a contract market and related provisions. This would create legal uncertainty for the board of trade and its U.S. members, for example, where a U.S. trader suffered a significant loss and challenged the legality of the trading.

I propose that we first focus on each of the standards for exemption and receive comments on them. They

are based on the assumption that the Commission may defer to a foreign regulatory scheme which is generally comparable to that of the U.S. This is similar to the UK standard applied to screen-based trading on non-UK exchanges, that UK investors must be afforded protection by the home country regulatory scheme equivalent to that provided by the UK.

Similarly, the focus of the proposed rules is on protection of the U.S. participants in the market.

We have some slides, and I am going to ask that the first slide, which shows the standards for exemption, be shown.

[Slide.]

I think you each have a copy of what is up there in case any of you cannot see it. It seemed to me we should go item-by-item. These are provisions that are included in Section 30.11(b)(1), which specifies the Standards for Exemption.

The first standard is that "the board of trade is an established board of trade otherwise primarily located in a foreign jurisdiction."

This standard is designed to ensure that an electronic board of trade has not been created offshore solely to evade U.S. law and regulation. It is also intended to ensure that the board of trade has a track record of having operated subject to the regulation of its home regulator.

I would like to throw the floor open for discussion of this standard for exemption.

Are there any comments?

[No response.]

CHAIRPERSON BORN: Does everybody think this is a reasonable standard?

Volker--and let me ask that each of the participants specify their name as they start to speak so that our transcript will have full identification.

MR. POTTHOFF: Volker Potthoff of Eurex.

First of all, I plead guilty, because we are probably the ones who brought up the whole mess with the DTB.

It is also hard for me as a non-U.S. lawyer to elaborate on something which I think U.S. lawyers should

elaborate on, that is, the question of the structure of the rule proposal. As I understand it, the foreign exchange is treated from the perspective of the Commodities Exchange Act as located in the U.S., and this gives a certain kind of jurisdiction over the foreign board of trade. I think as a principle matter, this is where our concern starts, because the principle that we see and the principle that is prevailing in Europe, and maybe our UK friends may also elaborate on their recognized overseas investment exchange procedure, but it is that we respect the jurisdiction of another regulator, of the home country regulator of a foreign exchange.

We feel that by presenting issues like, for example, the relationship--I see that we will come to that later, but I should mention it here--if you require information on manipulation rules, on recordkeeping, reporting of the board of trade, fitness standards for intermediaries and things like that, you are in big trouble, and that is our opinion, because you have to evaluate jurisdiction by jurisdiction whether this is really in

accordance with--and we come to that point as well--comparability standards.

I just wanted to raise this major concern at the beginning. We may discuss it later on, but this is my opening remark on that.

CHAIRPERSON BORN: Yes. I think the next standard is the comparability standard.

Are there any other comments on the first standard?

[No response.]

CHAIRPERSON BORN: Why don't we then go on to the comparability standard, which is the second of the Standards for Exemption, that is, that "the board of trade is subject to a regulatory structure generally comparable to that in the U.S. with respect to the protection of customers and market integrity."

This standard would permit the Commission to defer to the home regulator, as Volker has suggested, and to be assured that the U.S. investors will receive appropriate protections.

This standard is quite similar to the Commission's current standard in Rule 30.10, a comparability requirement there, under which the Commission has already exempted futures brokers in six countries and permitted them to represent U.S. customers without registration as an FCM in this country. The countries that already have had their regulatory systems recognized as comparable include the UK, France, Canada, Singapore, Australia and Japan.

The proposed standard in these rules is intended to be somewhat looser than the 30.10 standard in that it uses the term "generally comparable" rather than "comparable," and the Commission staff anticipates that those countries which have already been approved under 30.10 would be readily and quickly approved under this standard because their regulatory schemes have already been analyzed on most relevant points.

Also, T&M made a similar analysis for Germany when it approved the DTB no-action letter, so they assume that that country should have relative ease in compliance with the proposed rule.

No replication of the U.S. regulatory scheme is required or contemplated by this proposed standard. The Commission would instead look to whether the regulatory scheme overall protects investors and market integrity to a comparable degree.

The standard is designed to protect U.S. investors by assuring general comparability of regulatory protection. It would allow the Commission to distinguish between foreign countries based on the risks posed by their regulatory schemes to our investors. Without this standard, exchanges in the UK, Germany, Malaysia, the People's Republic of China and India would likely have to be treated equally despite differing risks posed.

I would invite comments on the comparability standard.

Danny Rappaport?

MR. RAPPAPORT: Thank you.

Speaking from the exchange perspective, I think we are relatively comfortable with the comparability standard in one sense but very uncomfortable in another. It may be fairer and appropriate in terms of protections for the

public, the general U.S. public trading in these foreign markets, but to the extent that those foreign markets trade products that are traded by U.S. exchanges, the comparability standard is very discriminatory against U.S. exchanges in that what we are really looking for is regulatory parity. So whereas a regulatory regime may be comparable in terms of the CFTC having confidence in deferring to it, it still may result in discriminatory competitive issues for the exchanges.

So I think that the comparability of a regulatory regime needs to be looked at from a number of different perspectives, the investor perspective and the domestic exchange perspective.

CHAIRPERSON BORN: Phil Thorpe wanted recognition, and then Gary DeWaal.

MR. THORPE: Thank you, Chairperson.

I feel my comments must be more altruistic than I had intended. As you have indicated, the United Kingdom has a comparable system, so I can now speak without concern about our comparability.

There are some basic principles which we have concerns about when looking at the issue of comparability. I take comfort from what you are saying. We are very concerned that comparability should not be reduced to like comparison.

There are a number of ways that the same sorts of standards that are espoused by the CFTC may be met by other jurisdictions. These may be alien in some sense, but they may nevertheless meet the national characteristics of the market where they arise; they may be justified in terms of the legal structure and the market structure of the countries in which they arise. And it is important in determining comparability that that flexibility to recognize that there are different ways of skinning the cat--that that must be recognized.

We have seen in the past, and I regret to say it does come up under the 30.10 exercise--may of us bear scars from that from the past--that the devil does lie in the detail, that finding an achievable way forward to utilize 30.10 was a difficult experience, difficult to get to the

point of agreeing with the Commission on what were comparable standards.

If progress has been made on that front, that would be very much welcome.

CHAIRPERSON BORN: Thank you, Phillip.

Gary DeWaal?

MR. DeWAAL: Thank you. What strikes me as odd--and again, I probably have no real vested interest in the topic of general comparability--but what strikes me as odd as a matter of philosophy and intellectual analysis and starts back with a review of Tradepoint--when you are discussing the Tradepoint Exchange, you are discussing a very different animal. You are discussing an overseas exchange that offers securities that are not registered under the U.S. securities laws and are not generally available to U.S. customers.

When you are discussing the products being offered on these electronic exchanges, you are talking about products that are otherwise, in most cases, other than certain stock index futures contracts and contracts based on

sovereign debt, you are talking about instruments that are generally available to U.S. clients.

So that, for example, when I go through the specific information requested about home country rules, I think these are sort of interesting, and maybe they give rise to a discussion of whether rules are comparable or not comparable, but at the end of the day, the only thing that is relevant is the fact that these products are being offered through internet access or electronic access. And it is not the product that we should be interested in, because the product is a product that if it were done in an open outcry market abroad, we would not really be here having this discussion. The rules already would allow U.S. clients access. It is simply because of the fact that there is this electronic internet access.

Therefore, I wonder how relevant the comparability rules are. To a certain extent, people slid over the first comment, which is "the board of trade is an established board of trade otherwise primarily located in a foreign jurisdiction," but to me, that is among the most important issues. If it is out there, if it is subject to a host

country regulator, and it is not otherwise prohibited by the Commodity Exchange Act or the CFTC rules, it seems to me that that is it--the general comparability. I personally do not understand, frankly, the relevance.

CHAIRPERSON BORN: I see David Pryde asking for recognition, and then Ron Hersch.

MR. PRYDE: From a practical matter, speaking as an FCM, I think this comparability issue is really something that could turn out to be a nightmare for FCMs and really unworkable, and I am talking about order routing systems right now.

Let's say we give a client an order routing system that has access to a number of exchanges, some of which pass the comparability test, and others do not. And somehow, whether by design or by accident, this client executes an order on a noncomparable exchange. Then, I think the legal certainty of that transaction and therefore our liability is increased dramatically, and I really question whether we can reasonably provide oversight that would avoid that type of situation.

I think lack of comparability does not mean that a foreign exchange is not a bona fide foreign exchange. I think that that should not be the only qualification.

CHAIRPERSON BORN: What kind of standards do you think would relate to a bona fide board of trade?

MR. HERSCH: Well, that wasn't exactly what I was going to take a stab at, but I think it just got thrown in my lap. If I could backtrack for just one moment, first of all, with respect to the whole issue of comparability, I am sort of concerned that what we are looking at here is applying a word, "comparability," which can be very subjectively interpreted depending upon who is making the judgment, rather than looking at, really, what the regulatory goal is of a home country's rules and regulations. I am troubled by using the word "comparability." I think that what is more appropriate is to look at what the goals are of the structure that exists and to really look at what the end results should be, rather than trying to say that the U.S. regulatory structure, which we all think is great, is the template and the exact thing

that needs to be applied to every exchange that wants to do business from the U.S.

In terms of the second question which just got thrown in my lap--if I recall, it was what the standards should be--one of the things that we have been discussing since this very lengthy proposal was put out a few weeks ago is looking at the home country's jurisdiction, making certain to the best of our ability that there is a system in place in that home country that monitors the trading that takes place on their exchange, and really more or less looking at what the end results is of the standards that they put in place in that home country on a case-by-case basis rather than trying to fit everything into a specific template.

CHAIRPERSON BORN: I think I had said Volker Potthoff was next, although I am not sure; then, Scott Gordon and Leo Melamed.

MR. POTTHOFF: Thank you.

It goes back to a philosophical question here, because what we appreciate is your concern in terms of

investor protection. I think that is the ultimate goal that the agency should be concerned about.

When we look at a test like the 13.10 test, that is something that you apply to the intermediaries, and the intermediaries are the ones that you have control of. And if, within the comparability tests, you look at the system and how intermediaries act in different locations or under different regulatory systems, I think you are hitting the wrong point, because an electronic exchange is not dealing with the ultimate customer. It is the FCM, so to say, that is supervised by the agency and that has to treat the customer in accordance with certain standards applied in the U.S. That is fine.

If it is, for example, a UK entity that has customers or a German entity, they have to comply with their standards, and I think the agency puts a lot of burden on itself in going jurisdiction by jurisdiction and looking at intermediaries and under what regulatory scheme they act.

We would rather refer to something like principles on electronic trading, such as the IOSCO principles, which we will probably come to later on. That is the treatment of

the members that you should also be concerned about. But from then on, if you look at the change, you are regulating the FCMs. Plus, if all other regulators in the world, around the globe, would apply the same standards that you do here, we would have the strictest standards applied around the globe, and that would probably cause some kind of hassle and even distraction on the regulators' side abroad.

Thanks.

CHAIRPERSON BORN: Scott Gordon?

MR. GORDON: Scott Gordon, Chicago Mercantile Exchange.

I just want to pick up on something that Danny mentioned with respect to regulatory parity. That is, from the standpoint of a U.S. exchange, we are certainly in favor of open access for foreign boards of trade, and I think what becomes critical is that there is a comparable regulatory structure so that many of the trade practices and other issues are equal between the U.S. exchanges and the foreign exchanges, and to the extent that the foreign exchange has a lesser standard, whether it is in terms of applications or guaranteed execution or payment for order flow or--I could

go on with other issues--we are certainly not asking for them to be held to a higher standard, but to the extent that we are held to a higher standard, I think it becomes problematic. So I would like to reserve some comment for later in the program, but I just want to be able to echo what Danny said.

CHAIRPERSON BORN: Thank you, Scott.

Leo Melamed?

MR. MELAMED: I guess this I guess this point touches on the nub of the problem for American exchanges. We find ourselves, I think, in what exactly Volker said--the strictest regulatory regime probably in the world. And we are in favor of anything that will reduce that strict regulatory regime. Indeed, we want that regulatory bar reduced to a level that is commensurate with today's world and not one that depended on when the CFTC was created, and the amendments that were created onto it over the years. That stricture has very little applicability in today's world. So we entirely agree that the regulatory environment and thicket within which American exchanges live is wrong,

too strict, does not serve the purposes intended and is in the worst interests of American exchanges.

Nevertheless, that's reality. We live within that stricture. And until the CFTC changes that, we have to abide by it.

Now, if we are placed in a competitive position whereby regulatory jurisdictions with much lesser strictures are allowed to come into these shores, which we welcome--indeed, we want full competition with foreign terminals and foreign boards of trade within these shores--but we implore that in such case, one of two things must happen. Our preference is that our regulatory burdens be lessened, and if not, there be regulatory parity one way or another achieved so that American exchanges can compete on a level playing field. That is our main concern is the availability of our competitive stance. We welcome the ability to compete with electronic boards of trade from any land, but we think it highly unfair if we must live within a stricture that is totally impossible for us to compete against.

That is our message, Madam Chairman.

CHAIRPERSON BORN: Thank you very much, Leo--"Madam Chairperson," please.

I see Art Hahn wants recognition, and George Crapple after Art Hahn.

MR. HAHN: Thank you.

I think the issue is joined. I think the question is what is comparability, and that becomes a battleground between people who would like easy access and people who are concerned, as Leo is, about a level playing field.

My own view is that both have very legitimate positions and that they are not simple. I am certainly sympathetic with the position of the Chicago exchanges that some of the strictures on their conduct be loosened. I think that that is appropriate, and I think it is overdue.

This is, though, the concern of the LIFFE Exchange, and that is that this is a very serious set of rules that are going to have to be put in place. There are legitimate points being made about them. But while that debate takes place, the current circumstance where Eurex has its terminals in, where Globex is doing business, and where

there is not a mechanism for the LIFFE Exchange to enter this market is intolerable.

The moratorium on no-action positions has blocked the same channel that Eurex took; Globex is in, and we have to wait for a rule or some other action by the Commission. And the legitimate concerns that you have heard around the table I think are going to take some time to sort out. They are serious concerns. I do not mean to diminish certainly the level playing field issues that Leo raises. But we can't wait, and the point that I would make is that if there cannot come to be consensus around balancing these various legitimate concerns, I would seriously ask the Commission to entertain some kind of interim relief, whether it is an interim order, as the FIA has proposed, whether it is a no-action position as a number of the Commissioners have proposed, but that the current circumstance of artificially keeping out foreign exchanges cannot abide while these very serious issues are debated.

I would make another comment on the comparability. Scott Gordon and Leo have talked about trade practice issues. I think I need to underline the fact that this

Commission as I understand it is prohibited by the Congress from legislating on foreign trade practices. You are not supposed to do that. I think that that is what the Congress has mandated you. I think the right approach there is to deal with trade practices on U.S. exchanges, and to the extent that they need to be amended and modified, I think that that ought to happen promptly. But I would remind people that there isn't freedom to go and have this Commission legislate trade practices on foreign exchanges, and I would further say that we should not have a circumstance where, under the guise of comparability, we get into the United States Commodity Futures Trading Commission regulating foreign exchanges.

CHAIRPERSON BORN: I had already recognized George Crapple to come next; I see Scott Gordon, Ron Hersch, Danny Rappaport and Gary DeWaal after George.

George?

MR. CRAPPLE: I have a narrow point that really follows on Gary DeWaal's comment. The futures contracts in question have all been approved for trading by U.S. citizens, so as a CTA, we can pick up the telephone and

trade any of these contracts, and the Commission has presumably made a judgment that the regulatory universe that these contracts exist in is okay for American investors. I think that should be the end of the comparability analysis.

The very word "comparability" sounds like it could be an endless inquiry.

CHAIRPERSON BORN: Well, of course, it is the inquiry that has already been undertaken with respect to all these countries, and the Commission has already made a positive finding that these countries are comparable.

Scott Gordon?

MR. GORDON: I just want to respond to something that Leo said. I did not mean to imply that the Commission regulate foreign trade practices of the foreign boards of trade. My point was that on a comparability level that it be considered, and to the extent that the foreign board of trade has a lesser standard, what I would suggest is that we lower the standard for the U.S. exchange, thereby having the comparability. Obviously, it is on a case-by-case basis, but that would certainly be one way to do it.

MR. MELAMED: I would endorse that. I think the approach that the reverse of keeping out terminals until that is the case is unacceptable.

CHAIRPERSON BORN: Ron Hersch?

MR. HERSCH: Madam Chairperson, if I may, I appreciate the Chairperson's desire to take the proposals which have been published and go through them point by point and certainly respect your decision to do so. But I think my comment at this point is appropriate since it does go to the heart of the Standards for Exemption as it does for so many of the other points that are made in the proposed rules.

This is not the first time or occasion where most if not all the people on this roundtable have been able to go through this proposal. Everyone has seen it and gone over it page by page, some of us collectively and some of us separately. And if I may say so, it is my opinion, and I believe it is the opinion of many of those on this roundtable that these rules are overreaching and burdensome and in fact inappropriate for the global marketplace and for the U.S. futures markets as well.

These principles underlying the proposed rules reflect a theme of the CFTC in adopting rules and regulations to regulate to the lowest common denominator. Specifically, each rulemaking, including this part of the rule, reflects the latest aberrant crisis event or imposes requirements that apply to all firms even though the concerns addressed by the regulations are localized to only a few firms.

I would urge the CFTC in addressing important issues such as technology and global markets to set requirements that are appropriate to the circumstances, to the market, and to particular firms and end-users.

The CFTC should employ cost benefit analysis to ensure that the burdens imposed by requirements are proportionate to the intended benefits.

The issues involved in developing comprehensive rules are complex, and many prescriptives in this proposal have been advanced. The CFTC has an opportunity to embrace technology while ensuring that important customer protection concerns are addressed or to repudiate the benefits by

insisting on a regulatory preemptive strike to assert control and jurisdiction.

The advent of new technology that has the potential to make access more efficient and cost-effective and that enhances the trading and risk management capabilities of regulated intermediaries and market users should not lead to the perverse result that access is impeded rather than facilitated.

Finally, I am very concerned that the Commission could be setting a new standard for access to foreign exchanges that could have significant consequences for access to U.S. exchanges if adopted by foreign jurisdictions.

I apologize for reading a prepared statement, but it is really these points that I make here that go to the heart of this matter. I find myself in a position where I agree with parts of things that were said by practically everyone at this table, and I for one certainly agree that the bar needs to be lowered for U.S. exchanges and that we should get a level playing field. But the rules that have been proposed here universally have been commented upon by

industry leaders as being burdensome, overreaching and inappropriate, as I say, for the electronic marketplace, and I hope that rather than looking at this agenda point by point, we can make some progress here today by getting real and true comments about how these rules would affect our business and our exchanges.

Thank you.

CHAIRPERSON BORN: Thank you, Ron.

Danny Rappaport?

MR. RAPPAPORT: I do not have any response to Ron at this point.

MR. HERSCH: Why not?

[Laughter.]

MR. RAPPAPORT: My comments are really directed at the representative of LIFFE, saying that the current moratorium is unacceptable and that LIFFE and other foreign exchanges needed to be permitted to do businesses in the U.S. immediately. I would disagree with that and object to that in general.

The United States is the largest marketplace in the world, and it is actually a privilege to do business

here, and the people who want to be afforded the privilege of doing business in the United States have to conform to the rules and regulations of the United States. And I do not think that you would find it acceptable or analogous to say that it is the United States Food and Drug Administration that has no authority to say what pharmaceuticals are being brought into this country, and I do not think you would find it acceptable to say that it is the United States Environmental Protection Agency that says that foreign manufacturers or automobiles cannot bring their cars into this country unless they meet U.S. standards. If you want to do business in the United States, you have to meet U.S. standards.

CHAIRPERSON BORN: I had said that I would recognize Gary DeWaal next. I see interest to be recognized thereafter by Art Hahn, Leo Melamed, Volker Potthoff, and I guess that's the current list.

Gary?

MR. DeWAAL: Thank you.

Again, I guess George and I can just be playing tennis here. I am still struck by the fundamental nature of

what we are talking about. If the client called up somebody at a terminal--provided they went through the foreign order transmittal requirements, whatever they might be these days--they could place an order to somebody who would immediately get on a terminal and place the order on an electronic exchange.

So in reality, it is not the location of the non-U.S. exchange, it is not the product non-U.S. exchange; it is the mechanism of transmission of the order that we are talking about, because the product is approved. It is so distinguishable from Tradepoint because of that. And again, we are sitting here discussing whether a phone line that--in the old days, the equivalent discussion would have been is it okay to call the site of a floor on the LIFFE, is it okay to call directly to the floor on MATIF. That is sort of what we are discussing right now, because it is just 20 years later, and the technology has changed. And that ultimately is why this thing just seems odd to me. It is approved products; we are talking about a medium of transmission of an order; we are talking about a more efficient means of transmission of an order. I still do not

really follow why comparability is relevant. We crossed that threshold already.

CHAIRPERSON BORN: I recognize Art Hahn next.

MR. HAHN: I will be brief. I wanted to just quickly respond to Danny that I certainly recognize the appropriateness of people coming into the United States living by U.S. law. There is no question about that. The circumstance that we find ourselves in today, though, is an anomaly, and that is U.S. law allowed the Eurex Exchange to come in and ask for a no-action letter, and when the LIFFE Exchange came in and said we'd like the same thing, which is a U.S. tradition of kind of equality, we were told no, there is no more no-action business. And then we said we'll wait for a rule, and that has been an awfully long time in coming and has presented a problem.

So the net effect of what is happening right now is un-American in that what you have is a German exchange doing electronic business and a French/Chicago exchange doing electronic business, but a procedural impediment to UK and Italian exchanges coming in. And that is troublesome, and that is what I was trying to address.

CHAIRPERSON BORN: Let me just say that I am unaware of any expressions of interest by an Italian exchange. Perhaps they have been in contact with the staff, and the Commissioners are unaware of it.

I have next on my list Leo Melamed; thereafter, Volker Potthoff and David Pryde.

MR. MELAMED: I would like to make several points more or less in response to some of the things said. First, with respect to Art Hahn, Art, what was the time gap between the time Eurex applied and the time that LIFFE applied--in years?

CHAIRPERSON BORN: LIFFE has never applied formally. They came and discussed with T&M the issue of screen-based trading in the U.S. in June 1998, last June.

MR. MELAMED: Well, thank you for those facts, because they are important in this discussion to understand that the world changed considerably--in fact it changed maybe five times over--from February 1996, I believe, when the ETB applied and what it is 2 or 3 years later, and we have all learned a lot in between, and it isn't simply that we want to keep the British out. I like the British. But

the truth is that you cannot blame anyone else for the lack of submission for this request by LIFFE. They waited, and perhaps they waited a bit too long, and there is a problem with that. But that isn't anybody's fault. It is certainly not the fault of American exchanges, and we certainly are not now going to be subjected to a time gap of a different sort, because if suddenly, today, the foreign exchanges were allowed to come in under a regulatory stricture that is substantially below the level that American exchanges have to live with, and if that time gap is only, say, 6 months, let alone it might only be 30 days to beat the living daylights out of us in competitive forum, I want to tell you it won't take very long for some other exchange to list our products, and if it has. And if it has that competitive advantage, bingo--we are out of business.

So I don't want any time gap. I wouldn't want a 30-day time gap. I wouldn't want a week time gap. If we are going to allow foreign exchange terminals in the United States, then lower the requirements for American exchanges so that we can compete fairly. That is number one.

Number two, I would like to make just one thing clear. Gary DeWaal is an excellent lawyer. By profession, I would hire him in a minute. I don't think I would take him much as a trader.

[Laughter.]

MR. DeWAAL: Neither do I, frankly.

MR. MELAMED: I am a trader, so let me explain something to him, perhaps, and others in this room who have this belief that a telephone is the same thing as a screen.

I'll tell you what--I'll take you on. All of you who believe that, you get the telephone, I get the screen, and I'll have your money in 30 days, because a screen is a biosphere of market knowledge, information, technology and graphics and information of a constant level that a telephone can't even touch. Are you kidding? I trade on the screen, and I have also traded in the pit, and I have also traded on the telephone, and I know the difference between the two. So anyone who tells me, oh, you allowed the telephone, so now you allow the screen simply is not a trader and doesn't know the differences between the two.

CHAIRPERSON BORN: Thank you, Leo.

Let me just go through my list so everybody knows when he or she will be recognized, and I'd be happy to add people to the end of the list.

Volker Potthoff is next. David Pryde has asked for recognition. Kyra Bergin is after David. Phil Johnson is thereafter, and Phillip Thorpe is at the end of my list.

Is anybody else seeking recognition?

[No response.]

CHAIRPERSON BORN: Okay. Volker Potthoff.

MR. POTTHOFF: That was an exciting issue. I tried not to be too excited about it.

[Laughter.]

MR. POTTHOFF: We are talking about competition, and I think that is the core element here, and I want to contribute to this.

I appreciate doing business in the United States, first of all, I really do, and I think you have great laws, great rules, and your FCMs are controlled in a great way.

[Laughter.]

MR. POTTHOFF: And that's the core. Maybe it is an issue where I should not interfere, but please, you

should not interfere in our business as well, because when we talk about competition--and I should also react to what Arthur Hahn is saying. He is saying, Eurex, you are so privileged. We have 20 members, and we cannot get any other member in because we are on a freeze from the CFTC to get any new members in from the United States. We cannot get any new product in.

For example--and now I turn to you--the CME/MATIF trade the EURIBOR [ph.], which is the euro short-interest-rate product, where there is a little battle in Europe about this contract. We cannot trade it here.

So what I am saying is let's have an equal level playing field. And I also support LIFFE that they can come in on the terms that we could come in. I think they were nice terms, and I think we can discuss those terms, but what is proposed today is going beyond that. That is all I am saying, no more than that. You have to act expeditiously, and I am afraid, Leo, that this might be competition going on also for the Chicago exchanges, but I think the U.S. always believed in competition, and I also say that we are not going to arguments of the European Commission in the

beef battle where they said, we have these regulatory concerns about getting beef from the U.S. in. I do not believe in that.

CHAIRPERSON BORN: Thank you, Volker.

David Pryde is next on my list.

MR. PRYDE: It has been so long, I have forgotten what I was going to say--just kidding.

Actually, first of all, I want to get back to Ron Hersch's comments and say that I--and I know virtually every other FCM that we talked to--fully endorse Ron's comments on the FIA approach, and that is rather than have very detailed prescriptive rules, we should be allowed to work on the basis of best practices and guidelines. And in its comment letter, the FIA enumerated some of these guidelines, and let me very briefly review five of them.

The first question we ask is: Is the foreign market a bona fide foreign futures exchange; that is, does the exchange have rules governing fair and orderly markets that are monitored by the relevant foreign market authority.

Secondly, is there a home regulatory that acknowledges its role as lead regulatory of the exchange?

Thirdly, does the market adhere to the IOSCO principles for the oversight of screen-based trading systems for derivative products?

Fourthly, does the Commission have the ability to obtain data on general levels of trading volume originating from the U.S. and on the number and identity of U.S. members.

And fifthly and lastly, does the Commission have the ability to access necessary information?

We would propose under our guidelines that if the answer to all of these questions is yes, then we should be allowed to conduct business as we see fit based on these guidelines, rather than comply with every prescriptive and detailed rule.

CHAIRPERSON BORN: Thank you very much.

Kyra Bergin?

MS. BERGIN: I would like to say something that really buttresses what Gary DeWaal has been saying, because I do think that what we are discussing today is really an issue of market access as opposed to the appropriateness or

the comparability of various regulatory regimes throughout the world.

We live in a world today where technology is changing our familiar notions of speed and the nature of the marketplace for the buying and selling of all financial instruments, not just exchange-traded derivatives. At times, I personally wish the pace of change would slow down a bit, but I know that that is an unrealistic expectation, and I know that I benefit both personally and professionally from the introduction of various systems due to technology.

So when the pace of change becomes somewhat overwhelming, I sit back and try to say to myself what really is causing the problem; is it simply a fear of new systems development? I would say I am fairly cautious and analytical, and a lawyer on top of that, so I can generally identify whether my concerns have merit or whether they are just me fighting against change and wishing for the good old days.

So when I look at the discussion that is occurring at this roundtable, I say to myself there are various issues that are being presented, and there are different issues

relating to competition and competitiveness. But again, the critical issue is really the one relating to market access.

With respect to exchanges, which is what we are talking about now, the exchange-traded derivatives market along with all the securities markets are subject to the forces of healthy competition. Throughout the world, exchanges are rethinking their future strategies. The debate over open outcry and electronic trading continues. And what is clear is that the most liquid, innovative and reliable exchanges are the ones that will survive. Exchanges are wooing new customers. U.S. exchanges are putting their terminals and locations outside the United States to make access easier to non-U.S. customers. They are being accepted in jurisdictions, and new customers are being able from outside the United States to access the U.S. markets. So it should come as no surprises that foreign exchanges wish to do the same in the United States.

But if we come back to my way of stepping back and analyzing the situation from the vantage point of a regulator, what is the CFTC worried about today, since the

products themselves in general have already been deemed appropriate for trading by U.S. persons?

Well, I can understand being concerned about the safety and soundness of non-U.S. exchanges, but the CFTC is not alone in being concerned about exchanges outside of its territory. Groups such as the Technical Committee of IOSCO are looking at precisely the same issues and continue to look at these types of global issues.

But I think it is at this point that we come to the first pitfall of the CFTC's approach. The pitfall as I see it is that the premise is that non-U.S. exchanges must essentially be regulated by the CFTC. The CFTC is de facto becoming the foreign regulator by producing standards and then requiring information which is in many ways the role in which the foreign regulator operates and should continue to operate.

Viable and appropriate regulation may differ; it is the role of groups such as IOSCO to articulate shared vision and shared regulatory standards. I understand the issues related to competition amongst exchanges both within

the United States and outside the United States, but again, I think the real debate here relates to market access.

Thank you.

CHAIRPERSON BORN: Thank you, Kyra.

Phil Johnson?

MR. JOHNSON: I think I'd like to reserve most of my thoughts for the segment of the meeting where we get down to the really crushing fundamental issues--what is the validity of the underlying rationale; setting up a new regulatory program because of technological developments; and, if it is necessary, is this the best way to go about it. Is a petitioning process, in view of all of our experiences under 30.10, the best way to go, or is there some other way that might suit better. So I will reserve my comments on that.

I did want to make a factual point, though. The Sydney Futures Exchange applied for no-action relief in March of 1997. That application was being processed in the Division of Trading & Marketss at the time when the decision was made to no longer use that approach. So even from the standpoint of a no-action process, which by no means had

been completed by that time, my calculation is there was something in the nature of 17 months of processing already with respect to a no-action letter.

So in terms of the timing of things, I agree with Leo--things happen very quickly. But there was and continues to be within the Division of Trading & Marketss a March 1997 no-action request.

CHAIRPERSON BORN: Yes, Phil is quite right; that's the only no-action request or other specific request, formal request for action, that the Commission has gotten.

Phil, let me just say that I think the discussion has gone much more broadly than the comparability standard which we are supposed to be discussing, and I think this is an appropriate time for you to share with us any other thoughts you have on this approach.

MR. JOHNSON: Well, I have heard Kyra, among others, and Ron and others have certainly begun to look a little beyond the specific topics. I didn't want to presume it was open to the floor until you told me it was.

There are two concerns--and I should preface this by saying there are a handful of exchanges around the world,

like Arthur, that I represent, that are going electronic or have always been, that need to get into the United States, the largest market in the world, and that are eager to have this process come to a conclusion sooner rather than later, and without getting into the substance of how it ought to turn out.

The questions I am getting from them are basically these. We are talking about two electronic devices, neither of which can match an order, neither of which can execute a trade, neither of which can clear anything. In all three of those instances, the functionality continues to exist in Barcelona or Frankfurt or Sydney.

On that basis, how much sense does it really make to reach the conclusion that one has organized an exchange within the United States merely by reason of the fact that, as Leo points out, it has become infinitely more useful to do business on a terminal than to do it by telephone. That is one point.

The other point is that having been responsible for shepherding at least four 30.10 regulatory comparability petitions through the Commission--and I did a little

analysis for the benefit of myself and shared it with the members of the Commission--that the shortest duration of review was 7 months, the longest was 2-1/2 years, and that is only one feature of this proposal. To anyone who has in mind the idea of reaching the state sooner rather than later, the idea of the petitioning process that involves regulatory comparability on the one hand, some sort of vetting of technology, and a variety of other showings means that--and please do not consider me cynical in saying so--the American markets, if this particular procedure were adopted, would have absolutely nothing to fear for at least 18 months to 2 years, and I would be reminded at the end of that that I had underestimated the length of time required.

Thank you.

CHAIRPERSON BORN: Thank you, Phil.

Phillip Thorpe is the last one on my list. I see Leo asking for recognition thereafter.

MR. THORPE: Thank you, Chairperson.

I am glad that we have had the chance to expand the agenda to a wider range of topics, because I do feel that the standards for exemption does start our discussion

down the track a bit. I know that in our own consideration in the United Kingdom of the very important issues that the Commission is concerned with, we started back a few steps. And I was particularly aware of the comments made by Leo Melamed about how things have changed in the last year. Since this process started, things have changed, and we have been very much aware that our consideration of systems--exchange-based systems, with all due respect to those representing exchanges--has been an interesting process but rapidly overtaken by those who want to provide order routing systems. And the commingling of those two concepts has been a matter that has rather defeated ourselves regulatory.

One of the factors that we recognized from that--and I think it is a sensible thing for all regulators to recognize in looking at any change--is that we have incredibly good powers of hindsight, and that stands us in great stead particularly when we are undertaking enforcement action. We even have moderately good powers in the observational sense; we can see what is going on today. But we are our own worst enemies in trying to be predictive. We will never as regulators guess where the industry or its

technology is going to be in 6 months' time or probably in 6 weeks' time. And trying to legislate for the future is a notoriously and probably dangerous prospect for us.

I should in the usual fashion of regulators issue a health warning at this stage. This is very much a view based on the regulatory structure that I have to work in in the United Kingdom. We do have perhaps slightly more versatility when it comes to responding to change.

But with that understanding, I think it struck us that we had to look at what measures we should apply in looking at the developments that are coming down the pike, whether it is electronic screens, whether it is order routing systems. And we operate on the basis of four or five basic principles in looking at these processes.

First, we fasten on the fact that the primary responsibility for the safe operation of any business lies with the firm and not with us as regulators, and we do not want to shift the burden of that responsibility. In U.S. terms and very much at the heart of our system, that lies on the FCM. Whether exchanges come and go, whether new systems develop, the responsibility lies on the FCM.

Second, we are obliged and take very seriously the need to ensure that any regulatory response produces benefits that exceed the cost of that intervention.

Third, we are statutorily required to allow for innovation and to encourage innovation.

And fourth, we must avoid any regulatory intervention that is anticompetitive. That is the backdrop for our response to developments of the sort the Commission is considering at the moment.

Against that backdrop, neither the development of screens placed in foreign countries nor the development of order routing systems seems to be a change of regulatory substance to that which we already deal with, that is already utilized by exchanges, intermediaries or indeed, customers. It certainly does not appear to be a set of developments that should cause us in the United Kingdom to respond in a defensible, restrictive fashion to those developments.

On the contrary, we have been convinced that those systems do provide benefits to customers and to the industry

that, if exploited effectively, will be of benefit to everybody without incurring greater regulatory risk.

If we are forced to undertake some kind of rulemaking or offer some form of guidance, our preference in this area is to work with the industry and develop a code or practice that has the flexibility to evolve as the industry practices evolve. Again going back to my earlier point, trying to get a system in place that is black letter law and yet flexible enough to cope with the changes that are coming down the line seems fraught with difficulty.

We would rather go the process of a code and allow that to evolve as time goes on.

As I said, we are very good at looking backward, not so good at looking forward. We have, however, looked at the two systems on our plate--the idea of a screen and/or the routing systems. We do have in place a mechanism for approving the establishment of foreign exchanges in the United Kingdom. A number of U.S. exchanges have found that a very favorable route to pursue and have undertaken that and now are recognized for that purpose. I would say that that route does not look on paper as complex or as detailed

as the proposals that are here today. Again, that suits our system.

In respect to order routing systems, we do not intend to make rules in this area. At best, we might be issuing guidance to customers and to the industry in respect of the particularities of those systems that might affect their relationship. Our focus is that relationship, customer to intermediary. And if indeed we were to issue a statement of best practice, we would very much welcome the ability to do that via a mechanism like IOSCO or some other international grouping wherein we could see international standards that facilitate cross-border trade.

I thank the chair.

CHAIRPERSON BORN: Thank you.

For the people here who are not members of the IOSCO Technical Committee which FSA and Phillip and I, on behalf of the CFTC, are, you should all know that there is a working party that is actively pursuing the issues of screen-based trading. As Kyra mentioned, our staff is very involved in that. There is an ongoing survey and an attempt to arrive at standards for cross-border trading on screens.

Leo Melamed is next on my list and then David Pryde.

MR. MELAMED: Just briefly to respond to something Volker said, I want the record straight on that subject. The American exchanges are nowhere need anticompetitive philosophies. We welcome competition at every level and would welcome foreign exchanges and boards of trade in the United States. All we are asking for is regulatory parity in that competitive trade. So do not place us in an anticompetitive mold, because certainly, that is not our history, that is not our present, and it will not be our future. But we do request that we have regulatory parity in order to be able to compete fairly.

CHAIRPERSON BORN: Thank you very much, Leo.

David Pryde?

MR. PRYDE: Well, so far, the discussion or debate on foreign terminals or order routing systems has really focused on the competitive impact in the U.S. I happen to agree with Leo--I think it is imperative that U.S. exchanges are given regulatory parity, and that does not mean more regulation for oversees markets; it means less regulation

here. But that is only one part of the equation. We have forgotten to discuss what I think is the most important part, and that is the impact on U.S. clients, the most important people as far as I am concerned.

What I hear from my clients is that because they do not have access to order routing systems, they are being disadvantaged relative to their foreign competitors. If this situation continues for much longer, there is no question that we will lose significant business out of the U.S., and already within my own firm, we have seen examples of business being transferred out of the U.S. into another regulatory environment, into Europe, that is.

So I would really call for a speedy process that will enable all market participants to have flexibility in how they proceed.

CHAIRPERSON BORN: Let me just say at this point that the access of customers to order routing system is something that is lower on the agenda. Maybe we should finish this issue about the standards in the rule applicable to the foreign exchange petitions and go on, then, to some of these other issues like the one that David is raising.

Let me just call on David Brennan.

MR. BRENNAN: I would just like to echo the last two comments. I think it is imperative that we get this simultaneous regulatory parity, and I think it is imperative that we do this rather quickly. We can't take months to do this. That would be my comment.

MR. HAHN: I think that's the core of it at a certain point. I do not think you can get simultaneous regulatory parity. I think the issues of changing the regulation of U.S. contract markets is very important. I agree, David, with you and Leo that there needs to be relief; it needs to be significant and deep and broad-reaching. I am in favor of it. But you cannot hold up foreign terminals coming into the United States waiting for that set of relief to go forward.

I know the board of trade initiated pro-market requests, and they have not gotten as far as they might want to. That is part of the process. But we cannot stop the foreign terminal issue waiting for that, and I would object to making the two coupled.

CHAIRPERSON BORN: I am going to recognize Bob Wilmouth, who has been asking for recognition, but after that, we are going to go on to the next standard. Otherwise, time is fleeing, and we are not going to cover the subject matter here.

Bob?

MR. WILMOUTH: Could I just ask both Arthur and Phil a question? Both of them, particularly Arthur, have been specifically saying that it is necessary to do something right away to get foreign terminals in here as soon as possible. Coterminous, does that mean that you would at the same time accept the regulatory burdens that Leo and others talk about so that they could say there was regulatory parity? I would like you to answer that, and I would also like Phil to answer that on behalf of his clients.

MR. HAHN: We certainly are prepared to come into this country and fulfill the requirements that the Commission puts down. One specific that Leo has talked about is trade practices, and as I read the mandate of this

Commission from Congress, it is that this Commission is not to legislate foreign trade practice.

I think the only way, therefore, to get relief for Leo and for other U.S. exchanges is for them to petition to the Commission and ask for the relief they are looking for in order to be competitive with the foreign markets.

CHAIRPERSON BORN: Phil?

MR. MELAMED: I didn't know Art was an expert on Congress, but assuming that he was, I would take a different tack, Art. I think it is this Commission that can establish this regulatory environment that we are looking for, and I don't think we need Congress to tell us what to do.

What we are looking for is for this Commission to lower the regulatory bar. We don't have to go beyond that.

MR. HAHN: I am totally comfortable with that.

CHAIRPERSON BORN: Phil?

MR. JOHNSON: My clients are business people, Bob, and if they were told that short of jumping off a cliff, that's what it takes to get terminals in the United States, they would go to the edge. Do they want to? No. Does it

make sense? We all have to make up our own minds about that.

But as far as the particular proposal is concerned, some of them say they could swallow hard, and maybe they could live with it--but then, they immediately ask, But Phil, why is this happening in the first place?

CHAIRPERSON BORN: With that, let us go on to the next standard, which is that "the board of trade is present in the U.S. (except for incidental contracts) only by virtue of being accessible from within the U.S. via an automated trading system."

This standard is designed to attempt to ensure that the board of trade is not trying to evade U.S. law and regulations in a contract market by looking at all of its contacts with the United States. It is also intended to ensure that it is a bona fide offshore electronic exchange except for its U.S. screen-based trading.

All contacts with the U.S. would be examined by the Commission to determine whether equity and U.S. regulatory needs suggest that the exchange should be designated in the U.S.

I would welcome comments on this standard, if any.

[No response.]

CHAIRPERSON BORN: No comments on that standard--Danny Rappaport.

MR. RAPPAPORT: I have just a minor comment related to everything else that we've said. In terms of the foreign board of trade's contact with the U.S. other than by the automated trading system, I think that the product that they trade can be viewed as being relevant to the degree of contact that they have with the U.S. In a sense, if they trade a T-bond contract or something that has a warehouse in the U.S. or is based upon a cash market that is principally located in the U.S., then I think that that invokes a higher level of regulatory interest on the part of the CFTC--the potential for manipulation of the pricing integrity of those markets.

CHAIRPERSON BORN: Does anyone else want to be recognized on this point?

[No response.]

CHAIRPERSON BORN: Let's go to the fourth point, then. "The board of trade is willing to submit to the

jurisdiction of the Commission and U.S. courts in connection with its activities under the exemptive order."

Comments on this standard?

Volker Potthoff?

MR. POTTHOFF: Well, in principle, saying that with regard to U.S. activities of a foreign board of trade that the CFTC has a kind of regulatory power, we have no objection to that, of course. But this goes along with the initial comment I made on jurisdiction over foreign trade in general. If we explicitly submit to the jurisdiction of the CFTC, this might cause a problem because we might all of a sudden be subject to two regulators--our home country regulator and the CFTC. We would try to avoid this.

The CFTC has the power at all times to withdraw the exemption, and I think that is the power it needs to have regulatory oversight over the foreign board of trade, and therefore, we are very reluctant to think that this is an appropriate item.

CHAIRPERSON BORN: Of course, I think DTB agreed to appoint someone here for service of process as part of the no-action process, for the very same purpose. This may

be stating what U.S. law is, but the activities of otherwise foreign institutions within the United States are subject to the jurisdiction of U.S. courts and the Commission.

Phil Thorpe has asked to be recognized.

MR. THORPE: Thank you, Chairperson. I think you may have partly dealt with the question I was going to ask.

This provision, whilst apparently innocuous in itself, does represent a different formulation from that which appeared I think under 30.10, and indeed, under some of the no-actions, and indeed, since the matter was brought up under the Tradepoint decision that the SEC issued, where agent for process has been the formulation.

I am not suggesting this is behind the change in formulation, but for those looking for an escalation in detail, this seems to fall into that category. Your assurance that it is merely an alternative form of wording would probably eliminate that.

CHAIRPERSON BORN: I think what it does is probably articulate what the law would be anyway to the extent that it goes beyond appointment of an agent for service of process purposes.

Are there any other comments on this?

Arthur, and then Gary DeWaal.

MR. HAHN: I think the right formulation would be simply to appoint agent for service of process. Certainly, as articulated in your proposed rules, it goes beyond the law in that it has, for example, foreign exchanges submitting to the jurisdiction of every State in the Union right now, and I didn't understand why that would be so broad.

I think the right way to go is to consent to service of process.

CHAIRPERSON BORN: Gary DeWaal?

MR. DeWAAL: Interesting--actually, I agree with something you just said, and I don't know if everybody realized the significance. I think you just said it probably is what the law is anyway. To me, that is a very important statement, because if it is what the law is anyway, why change it? Why make a new law? Why make a new regulation?

One could argue that if a foreign exchange is going to put a terminal in the United States under doctrines

of minimal contacts and various fancy cases on the subject, the courts would exercise jurisdiction over the parties just by their presence, and they might view the terminals. But if they wouldn't, why change that status quo?

It is interesting, because listening to a lot of what I am hearing here--and I was very struck by what Phil Thorpe said and what Ron Hersch said, and part of the motif we discussed before--a lot of what we are discussing here today is probably dealt with already, and what we are seeing is coming up with an overlap on top of stuff that is probably out there already and probably mostly already works. If that is the case, is the right route making new rules, or is the right route maybe coming up with interpretations or best practices? And that becomes even more relevant to the discussion of AORS, which I will defer until later.

CHAIRPERSON BORN: David Pryde?

MR. PRYDE: I guess I would seek a point of clarification from the Commission. Why does the Commission feel it needs jurisdiction for order routing systems but

does not actually right now have jurisdiction for orders that are transmitted by phone or fax?

CHAIRPERSON BORN: Well, of course, we do have jurisdiction for U.S. activities related to orders transmitted by fax or telephone.

MR. PRYDE: Why has this become an issue, then?

CHAIRPERSON BORN: Well, our Part 30.10 and the other Part 30 rules deal with the jurisdiction. We have 10 subparts of Part 30 already. This would add an 11th.

MR. PRYDE: But why is there some opposition to this jurisdictional issue now, and it has not been voiced previously, to my knowledge, anyway?

CHAIRPERSON BORN: I don't understand the question. I think what is being said here is that because the DTB order only required appointment for service of process, why are we requiring both appointment and an express consent to jurisdiction, when probably the state of U.S. law is that anyplace where there were operations of the foreign exchange, there would be U.S. jurisdiction for purposes of scrutinizing at least things that happened in the U.S. It may be unnecessary, and that's one of the

benefits of having proposed rules and getting public comment on them. This may be just a reiteration of existing law and may be unnecessary to put in. But we will certainly take that into consideration along with all the rest of the comments we receive.

Should we go on to the next point? The next point involves the automated trading system, and it says "the board of trade has its automated trading system approved by its home regulatory in accordance with IOSCO's Principles on Screen-Based Trading or similar standards."

This standard, as I understand it, is designed to ensure that the electronic trading system incorporates some basic protections and is unlikely to be a source of major market disruption and harm to U.S. investors. The IOSCO principles are currently well-accepted by international regulators. No kind of formal certification by the foreign regulator would be required if the regulator has generally given its approval to the operation of the system, as I understand it.

This is open to comments.

Arthur Hahn?

MR. HAHN: This is a technical point on the rule. I read it to be that you ere seeking an actual approval by the home regulator, and as I understand the home regulator in the UK, they do not approve it, they do not do it.

Certainly as a starting point, the IOSCO standards are correct, and we would certify that as an exchange, we are abiding by them. But you are prescribing a regulation for a foreigner, and it is not their system, it is not the way they do things.

CHAIRPERSON BORN: As I understand it, our staff has had discussions with the FSA about the process that is followed there. The FSA is I think fully aware of your client's proposed electronic system which I guess started to trade last week, did it--

MR. HAHN: That's what I understand.

CHAIRPERSON BORN: --on at least one of its contracts. And I think the staff feels that either that constitutes foreign regulator approval, or the rule can be amended in such a way that makes it clear that when there is oversight by the foreign regulator including some attention to the electronic system and the foreign regulator has

allowed trading to go forward, that is essentially what we are looking for.

Also, I know that the staff is discussing in instances where there is no regulatory oversight at all--and I don't know if there are any instances, because I think IOSCO members pretty well agree that there should be oversight of this--but in instances where there was not, one thing that I have heard the staff discussing is whether an examination by an independent consulting company of the adequacy of an electronic exchange, which I know our domestic exchanges have done before they start operating, could take the place of this, and the rule could be adjusted accordingly.

Any comments on how best to do this I think would be welcome by the staff.

George Crapple?

MR. CRAPPLE: At the risk of being repetitive, once again, these are contracts that have been determined to be lawful for Americans to trade, and I don't see why there has to be a revisiting of how the electronic system works,

just to avail ourselves of a more efficient way of placing orders.

CHAIRPERSON BORN: Jerry Tellefsen?

MR. TELLEFSEN: Yes. I think that if a foreign board of trade has a proven track record with an electronic trading system, and if that trading system has been observed and monitored by regulatory authorities, and if you have access to that, I think that probably ought to suffice. I would suggest that I find it very unlikely that the Commission or anybody else would be able to attract the technical expertise necessary to evaluate multiple different kinds of electronic trading systems on different platforms that cost tens of millions of dollars that change regularly. To get that kind of staff and to do it would take a long time.

The SEC has a rule that says equity exchanges have to submit and present an external or internal audit of many of their trading systems every year, and it kind of works. It keeps the exchanges on their toes. However, the amount of time it takes to do that and the cost that it takes to do that is very, very significant. These systems slow down,

and they go down, and you don't know when that is going to happen. If you just did an audit and a review of an electronic trading system, and it passed muster, and then it gets changed considerably over the next 2 months or whatever else and fails, you have no way of monitoring whether it has failed or not.

So unless you do the due diligence up front and continue to do it all the time, all you have done is a one-time look at whether the IOSCO principles are being met and other kinds of conditions relative to security and integrity are being met. So it is either an ongoing thing, or you take the track record that currently exists and go with it and monitor performance as it goes along.

CHAIRPERSON BORN: I think that that is the intention, that is the reason behind the approach here, which is to defer to the foreign regulator completely in its assessment. I think this is a real change from the DTB approach where our staff analyzed the electronic system that DTB had there and made an assessment as to whether it was sufficiently accurate and secure and stable and all those things, and I think the staff has recognized and the

Commission has recognized that that is not a business that we want to be in.

Other comments? Phil Thorpe and then Volker.

MR. THORPE: Just to really agree with that point that we in the FSA do not have a set of rules that says this is what should happen with a particular automated system. And in a technical sense, I guess we don't approve of the system, either, because we fall foul of the technology ignorance problem that most regulators have at varying stages.

What we do put our attention to is whether the exchange has conducted due process in looking at the system and is tested for durability and for delivering what it says it will do. And we would continue to do that. But we haven't reduced that to a set of rules or specific requirements. It will be on a case-by-case basis.

CHAIRPERSON BORN: Volker Potthoff?

MR. POTTHOFF: Along the lines of what Phillip what just said, our regulator is not giving a stamp or anything, but while giving formal approval to the application, they look at the system. So you should have

alternative routes to have that certified if you wish to, for example, auditors' statements or representatives by executives of the exchange. I think that that would give more flexibility to that.

CHAIRPERSON BORN: Are there any other comments on this standard?

[No response.]

CHAIRPERSON BORN: If not, we will go on to the last standard, which is that "satisfactory information-sharing arrangements are in effect between the Commission and the board of trade and the board of trade's regulatory authority."

This standard is intended to ensure that the Commission has access to the information it needs to protect U.S. investors. We currently have information-sharing arrangements with a great many countries including all of the countries with 30.10 exemptions that I mentioned earlier and also with Germany.

The staff is currently examining whether any of the existing agreements would need any modification to meet the standards in the rule. I think that preliminarily, the

assessment is that most of the existing arrangements would meet or would virtually meet the needs, but we have in discussions with foreign regulators assured them that we will complete this assessment quickly so that if any amendments to existing arrangements are necessary, there could be early warning thereof, and we could start negotiating.

Discussion on this point?

Gary DeWaal.

MR. DeWAAL: Thank you.

Again, this one strikes me as sort of odd, again, partly because of something that David Pryde mentioned before, and I don't think we have stated enough here. We are talking principally of institutional clients, and we are saying that institutional clients who pick up a phone do not require a regulatory system where there is information-sharing among regulators, but institutional clients that place electronic orders somehow need information-sharing among regulators.

CHAIRPERSON BORN: Could I just correct that--

MR. DeWAAL: Sure.

CHAIRPERSON BORN: --because right now to have 30.10 comparability treatment, and therefore to allow a U.S. institutional client to pick up a phone and talk to somebody in the UK, we have required information-sharing arrangements.

MR. DeWAAL: I understand. Again, if the interpretation is to go abroad, I understand that. But you can still pick up the phone domestically, certainly, and a client can call my U.S. desk and these information-sharing arrangements are implicated. Simply what Leo pointed to was the speed which it granted is of tremendous benefit, and that is causing the issue here. But I think, again, that as we go forward, we must keep in mind who we are talking about out there, because I do not think it has been stated enough so far in this meeting--we are talking about institutional clients for the most part, a very sophisticated kind of individual.

CHAIRPERSON BORN: I think Phillip Thorpe had asked for recognition; then Art Hahn.

MR. THORPE: Thank you, Chairperson.

Just to confirm, we have agreements in place, so I think this brings us back to a point that has popped up from time to time. If it works now, and if we are not looking at anything that is fundamentally different, I hope the presumption will be that it will work in the future.

And perhaps a cautionary word. As in all regulation, trying to predict where you might want information of what type, of what value, at what speed, 6 months out, is a recipe for delay and certainly a recipe for getting it wrong. I think these agreements can always be amended as time goes on. We shouldn't be seeking perfection at day one.

CHAIRPERSON BORN: Well, as we have done with the UK and with a number of other regulators as new needs arise.

Art Hahn.

MR. HAHN: Chairperson, two points to be made about information-sharing. One, it would be LIFFE and IPE's strong preference that to the extent the Commission wants information from them, that it be provided to our own regulator and that the information be passed down the MOU. I think that is consistent with the overall regulatory

scheme and that the information-sharing between the exchange and the CFTC directly ought to be at a bare minimum, but that the main communication be, as it is working well now, between regulators.

The second point is a related one, and I am jumping ahead to the last point in your Section II, but I think it ties in, and that is the tag line in the proposed rules was that we want information concerning the petitions and so on, and then any other information we want. That felt a little overly broad, and I would hope that when a final rule emerges, it has some limit to it and that the communication will go down in the MOU.

CHAIRPERSON BORN: Volker?

MR. POTTHOFF: Just to add to this, the principle should be, because you are supervising what is happening with regard to U.S. customers and U.S. intermediaries, that it is the kind of information that you are interested in and not all of a sudden ask whether we in Deutschebank have--what is happening over there with respect to their activities. It should be somehow made clear that it is