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BEFORE THE
U.S. SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
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Good morning Chairman Johnson, Ranking Member Shelby and members of the Committee. I thank you for inviting me to today's hearing on implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act. I also thank my fellow Commissioners and CFTC staff for their hard work and commitment on implementing the legislation.

Lessons of 2008

Three years ago, the financial system failed, and the financial regulatory system failed as well. We are still feeling the aftershocks of these twin failures.

There are many lessons to be learned from the crisis. Foremost, when financial institutions fail, real people's lives are affected. More than eight million jobs were lost, and the unemployment rate remains stubbornly high. Millions of Americans lost their homes. Millions more live in homes that are worth less than their mortgages. And millions of Americans continue struggling to make ends meet.

Second, it is only with the backing of the government and taxpayers that many financial institutions survived the 2008 crisis. A perverse outcome of this crisis may be that people in the markets believe that a handful of large financial firms will – if in trouble – have the backing of taxpayers. We can never ensure that all financial institutions will be safe from failure. Surely, some will fail in the future because that is the nature of markets and risk. When these challenges arise though, it is critical that taxpayers are not forced to pick up the bill – financial institutions must have the freedom to fail.

Third, high levels of debt – and particularly short-term funding at financial institutions – was at the core of the 2008 crisis. When market uncertainty grows, firms quickly find that their challenges in securing financing, so called problems of “liquidity,” threaten their solvency.

Fourth, the financial system is very interconnected – both here at home and abroad. Sober evidence from 2008 was AIG’s swaps affiliate, AIG Financial Products, which had its major operations in London. When it failed, U.S. taxpayers paid the price. We must ensure that Europe’s ongoing debt crisis does not pose a similar risk to the U.S. economy.

Lastly, while the 2008 crisis had many causes, it is evident that swaps played a central role.

Swaps added leverage to the financial system with more risk being backed by less capital. They contributed, particularly through credit default swaps, to the bubble in the housing market. They contributed to a system where large financial institutions were considered not only too big

to fail, but too interconnected to fail. Swaps – developed to help manage and lower risk for end-users – also concentrated and heightened risk in the financial system and to the public.

Dodd-Frank Reform

Congress and the President responded to the lessons of the 2008 crisis – they came together to pass the historic Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act).

The law gave the Commodity Futures Trading Commission (CFTC) and the Securities and Exchange Commission (SEC) oversight of the more than \$300 trillion swaps market. That's over \$20 of swaps for every dollar of goods and services produced in the U.S. economy. At such size and complexity, it is essential that these markets work for the benefit of the American public; that they are transparent, open and competitive; and that they do not allow excessive risk to spread through the economy.

The CFTC has benefited from significant public input throughout the rule-writing process. We have received more than 25,000 comment letters. CFTC staff and Commissioners have met more than 1,100 times with market participants and members of the public to discuss the rules, and have held more than 600 meetings with domestic and foreign regulators. We also have conducted 14 public roundtables on Dodd-Frank, many of them with the SEC.

The CFTC has substantially completed the proposal phase of Dodd-Frank rules. We have held 21 public meetings and issued more than 50 proposed rules on the many important areas of reform called for by the new law, including transparency, lowering risk through clearing, market integrity and regulating swap dealers.

The agency turned the corner this summer and began finalizing rules to make the swaps marketplace more open and transparent for participants and safer for taxpayers. To date, we have finished 20 rules, and we have a full schedule of public meetings into next year.

FSOC

To help protect the public, the Dodd-Frank Act included the establishment of the Financial Stability Oversight Council (FSOC). This Council is an opportunity for regulators – now and in the future – to ensure that the financial system works better for all Americans. There has been a tremendous amount of coordination and consultation amongst the eight FSOC agencies on the Dodd-Frank rule-writing process, and the CFTC will continue to work closely with other FSOC members as we finalize additional important rules.

In July, the FSOC approved a rule enabling the Council to identify and designate systemically important financial market utilities, including clearinghouses. Comprehensive and robust regulatory oversight of clearinghouses, in particular their risk management activities, is essential to our country's financial stability. This rule complements the CFTC's final rule

establishing risk management and other regulatory requirements for derivatives clearing organizations.

Promoting Transparency

The more transparent a marketplace is, the more liquid it is and the more competitive it is. When markets are open and transparent, prices are more competitive, markets are more efficient, and costs are lowered for companies and their customers. Transparency benefits the entire economy.

To increase market transparency, we have completed rules that, for the first time, provide a detailed and up-to-date view of the physical commodity swaps markets so regulators can police for fraud, manipulation and other abuses. The large trader reporting rule we finalized establishes that clearinghouses and swap dealers must report to the CFTC information about large trader activity in the physical commodity swaps markets. The rule went into effect November 21. For decades, the American public has benefitted from the Commission's gathering of large trader data in the futures market, and now will benefit from the CFTC's new ability to monitor swaps markets for agricultural, energy and metal products.

We also finished a rule, which became effective October 31, establishing registration and regulatory requirements for Swap Data Repositories, which will gather data on all swaps transactions. By contrast, in the fall of 2008, there was no required reporting about swaps trading.

Moving forward, we are working to finish rules relating to the specific data that will have to be reported to the CFTC. These reforms will provide the Commission with a comprehensive view of the entire swaps market, furthering our ability to monitor market participants and to protect against systemic risk.

We also are looking to soon finalize real-time reporting rules, which will give the public critical information on transactions – similar to what has been working for decades in the securities and futures markets.

In addition, we are working on final regulations for trading platforms, such as Designated Contract Markets, Swap Execution Facilities and Foreign Boards of Trade – all of which will help make the swaps market more open and transparent. Yesterday, the Commission approved a final rule implementing the Dodd-Frank provision for registration of Foreign Boards of Trade.

Lowering Risk Through Clearing

Another significant Dodd-Frank reform is lowering risk to the economy by mandating central clearing of standardized swaps. Centralized clearing will protect banks and their customers from the risk of a default by one of the parties to a swap. Clearinghouses reduce the interconnectedness between financial entities. They have lowered risk for the public in the futures markets since the late 19th century. In October, we finalized a significant rule

establishing risk management and other regulatory requirements for derivatives clearing organizations.

Yesterday, the CFTC approved a final rule enhancing customer protections regarding where clearinghouses and futures commission merchants can invest customer funds. We also are looking to soon finalize a rule on segregation for cleared swaps. Segregation of funds is the core foundation of customer protection. Both of these rules are critical for the safeguarding of customer funds.

In addition, after the first of the year, we hope to consider finalizing rules that will broaden access to the markets, including straight-through processing, or sending transactions immediately to the clearinghouse upon execution; and the exemption for non-financial end users. The Dodd-Frank Act does not require non-financial end-users that are using swaps to hedge or mitigate commercial risk to bring their swaps into central clearing. The law leaves that decision to individual end-users. In addition, the CFTC's proposal on margin states that non-financial end-users will not be required to post margin for their uncleared swaps. Lastly, the Dodd-Frank Act maintains a company's ability to hedge particularized risk through customized transactions.

Market Integrity

To enhance market integrity, we finished an important rule Congress included in the Dodd-Frank Act giving the Commission more authority to effectively prosecute wrongdoers who recklessly manipulate the markets. The rule, which went into effect August 15, broadens the

types of enforcement cases the Commission can pursue and improves the agency's chances of prevailing over wrongdoers. The new authority expands the CFTC's arsenal of enforcement tools so the Commission can be a more effective cop on the beat.

We also finalized a rule to reward whistleblowers for their help in catching fraud, manipulation and other misconduct in the financial markets, which will enhance our ability to protect the public. It went into effect October 24.

In addition, we recently completed speculative position limit rules that, for the first time, limit aggregate positions in the futures and swaps market.

To further enhance market integrity, we are looking to finalize guidance on disruptive trading practices, as well as regulations for trading platforms.

Regulating Dealers

It is also crucial that swap dealers are comprehensively regulated to protect their customers and lower risk to taxpayers.

The CFTC is working closely with the SEC and other regulators to finalize a rule further defining the term swap dealer. We also are planning to finalize a rule on the registration process for swap dealers and major swap participants. The agency is looking to soon consider final external business conduct rules to establish and enforce robust sales practices in the swaps

markets. We also will consider final internal business conduct rules, which will lower the risk that dealers pose to the economy. In addition, we have been working closely with other regulators, both domestic and international, on capital and margin rules.

Implementation Phasing

The CFTC has reached out broadly on what we call “phasing of implementation,” which is the timeline that our rules will take effect for various market participants. We held a roundtable with the SEC in May to hear directly from the public about the timing of implementation. Prior to the roundtable, CFTC staff released a document that set forth concepts the Commission may consider on effective dates of final rules, and we offered a 60-day public comment file to hear specifically on this issue. The roundtable and public comment letters helped inform the Commission as to what requirements can be met sooner and which ones will take a bit more time.

In September, the Commission issued for public comment a proposal for phasing in compliance with the swap clearing and trading mandates. We also proposed an implementation schedule for previously proposed rules on swap trading documentation requirements and margin requirements for uncleared swaps. These proposals are designed to smooth the transition from an unregulated market structure to a safer market structure. As we progress in finishing major rules, we will continue looking at appropriate timing for compliance, which balances the Commission’s desire to protect the public while providing adequate time for industry to comply with these new rules.

In addition, much like we did on July 14, we will soon consider further exemptive relief regarding the effective dates of certain Dodd-Frank Act provisions. Commission staff is working very closely with the SEC on rules relating to entity and product definitions. Staff is making great progress, and we anticipate taking up the further definition of entities in the near term and product definitions shortly thereafter. As these definitional rulemakings have yet to be finalized, the order would provide relief beyond December 31, 2011.

International Coordination

The global nature of the swaps markets makes it imperative that the United States consults and coordinates with foreign authorities. The Commission is actively communicating internationally to promote robust and consistent standards and avoid conflicting requirements, wherever possible. CFTC staff is sharing many of our comment summaries and drafts of final rules with international regulators. We are engaged in bilateral discussions with foreign authorities, and have ongoing dialogues with regulators in the European Union (EU), Japan, Hong Kong, Singapore and Canada. On Thursday, Chairman Schapiro and I will meet with the CFTC's counterparts from these four countries and the EU to discuss how to regulate the global swaps market in a consistent, comprehensive and coordinated manner.

The Commission also participates in numerous international working groups regarding swaps, including the International Organization of Securities Commissions Task Force on OTC Derivatives, which the CFTC co-chairs. In August, the CFTC and SEC staff held a daylong,

joint roundtable to discuss international issues related to implementation of Title VII of the Dodd-Frank Act. I anticipate that the Commission will explicitly seek public input on the extraterritorial application of Title VII of the Dodd-Frank Act.

Resources

As the CFTC finalizes these Dodd-Frank rules, the agency will need additional resources consistent with the CFTC's significantly expanded mission and scope. The swaps market is seven times the size of the futures market that we currently oversee.

The agency has the necessary funding to complete rules called for in the Dodd-Frank Act. Moving forward though, the CFTC will need greater resources to protect the public. With just over 700 staff members, we are but 10 percent larger than our peak in the 1990s. Since then, though, the futures market has grown more than fivefold, and Congress added oversight of the swaps market, which is far more complex and seven times the size of the futures market we currently oversee.

Without sufficient funding for the Commission, the nation cannot be assured that this agency can oversee the swaps market and enforce rules that promote transparency, lower risk and protect against another crisis.

Conclusion

The CFTC is working to complete our rule-writing under the Dodd-Frank Act thoughtfully – not against a clock.

But until the agency implements and enforces these new rules, the public remains unprotected.

This is why the CFTC is working so hard to ensure that swaps-market reforms promote more open and transparent markets, lower costs for companies and their customers, and protect taxpayers.

Thank you, and I would be happy to take questions.