Testimony of James Cawley

Swaps & Derivatives Market Association

Javelin Capital Markets

for

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
SUBCOMMITTEE ON SECURITIES, INSURANCE, AND INVESTMENT

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Chairman Reed, Ranking Member Crapo, and Members of the Subcommittee, my name is James Cawley. I am CEO of Javelin Capital Markets, an electronic execution venue of OTC derivatives that expects to register as a SEF (or "Swaps Execution Facility,") under the Dodd Frank Act.

I am also here to represent the interests of the Swaps & Derivatives Market Association or 'SDMA,' which is comprised of multiple independent derivatives dealers and clearing brokers, some of whom are the largest in the world.

Thank you for inviting me to testify today.

To ensure that the US taxpayer is never again required to bail out Wall Street, we must move away from 'too inter connected to fail' where one bank pulls another three with it –in the event of its failure. Equally important, we must remove the systemic 'sting' currently associated with each bilateral derivatives swap contract that connects financial firms to each other and thus compel these swaps contracts into clearing houses as mandated under the Dodd Frank Act.

In order to have safe and successful central clearing of OTC derivatives, certain remaining impediments must be removed such that clearing houses ensure that they have truly representative governance structures, offer objective and proportionate risk models, provide open access to properly qualified and non correlated clearing members and accept trades on a 'real time' and 'execution blind' basis such that systemic risk is mitigated while transparency and market liquidity are increased.

Clearing House Governance & Membership
With regard to clearing house governance, we support CFTC Core Principles O, P & Q that require that governance arrangements be transparent, fair and representative of

the marketplace. Such governance bodies should represent the interests of the market as a whole and not just the interests of the few.

Importantly, clearing house membership requirements should be objective, publicly disclosed & permit fair and open access; as Dodd Frank requires.

This is important because clearing members act as the 'gatekeepers' to clearing. Without open access to clearing, you will not have universal clearing adoption, increased transparency, and lessened systemic risk.

Clearing houses should seek to be inclusive, not exclusive in their membership criteria.

We should dispense with the myth that swaps are somehow different from other cleared markets and thus the vast experience from those markets should be ignored.

Instead, clearing houses should learn from their own experience in the listed derivatives space --of futures and options.

In those markets, central clearing has operated successfully since the days of post Civil War Reconstruction nearly 150 years ago; long before spreadsheets and risk models. In those markets, counterparty risk is spread over a hundred disparate and non correlated clearing firms. It works well. No customer has ever lost money due to a clearing member failure.

To complement broad participation, clearing houses should not have unreasonable capital requirements. Capital should be a function of the risk a member contributes to the system; simply put, the more you or customers trade, the more capital you contribute.

The SDMA supports the CFTC's call for clearing broker capital requirements to be proportionate and scale relative to the risk introduced to the system.   We support the CFTC's call that a clearing firm's minimum capital be closer to $50 Million, rather than closer to the $5 billion or $1 billion threshold as certain clearing houses have originally suggested.

Certain clearing house operational requirements for membership that have no bearing on capital or capability should be seen for what they are—transparent attempts to limit competition.

Specifically, clearing members should not be required to operate swap dealer desks just so they can meet their obligation in the default management process. These requirements can easily be met contractually through agreements with third party firms or dealers.

With regard to conflicts of interest within a clearing member, Dodd Frank is clear; dealer desks should not be allowed to influence their clearing member colleagues and strict Chinese walls should exist.

Derivatives Trade Integrity

With regard to trade acceptance, clearing houses and their constituent clearing member firms should accept trades on an 'execution blind' basis. Clearing firms should be prevented from discriminating against certain customer trades, simply because they dislike the manner in which they have been executed or the fact that they may be anonymous.

Certain trade counterparties should be precluded from exploiting current market position to impose documentary barriers to entry that restrict customer choice of execution venue, execution method or dealer choice. Regulators should remain vigilant to ensure that such *restrictions on trade* do not manifest themselves in a post Dodd Frank world.

With regard to trade integrity, execution venues, clearing members and clearing houses should, as the regulators require, work together to ensure that executed trades settle or are accepted into clearing as quickly as possible.

The SDMA, joins with the MFA, and supports the CFTC requirement that trades be accepted into clearing *immediately* upon execution or trade submission. Regulators should be mindful not to allow clearing house workflows that seek to increase and not decrease trade latency. Such workflows should be seen for what they are—clear attempts to stifle successful OTC derivative clearing.

Conclusion

In conclusion, the CFTC and the SEC should be commended for their excellent work. Both agencies have been transparent and accessible throughout the entire process. They have adapted to industry suggestion when appropriate.

We must move away from 'too interconnected to fail.' As an industry, we must work together to ensure that OTC derivatives clearing is a success such that Wall Street never again has to come to Main street for another bail out.

Thank you.