U.S. House of Representatives
Committee on Agriculture
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July 14, 2011

Honorable Gary Gensler
Chairman
U.S. Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Dear Chairman Gensler:

Thank you for your continued efforts, and for the tireless work of your staff, to implement Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank").

As you begin to shift the Commission's focus from proposed rules to final rules, there are many steps your Agency can take to improve the rule-making process and facilitate a more orderly implementation of Dodd-Frank. We believe a process that is transparent, deliberate, and appropriately rooted in economic analysis will best achieve the objectives of Title VII. Therefore, we write today to recommend you take the following specific actions through the remainder of the implementation process:

Improve the Cost-Benefit Analysis for Final Rules

Particularly in light of the wide-ranging impact Title VII will have for businesses throughout the economy, it is imperative that your agency conduct thorough and thoughtful economic analysis regarding the costs and benefits of each rule. We believe that the Commission's current approach does not satisfy statutory cost-benefit analysis provisions, which do not "simply require the Commission to 'consider the costs and benefits' of its action," as the Commission has stated in previous rulemakings.[1] Instead, the statute goes on to direct that "[t]he costs and benefits of the proposed Commission action

[1] 75 Fed. Reg. 80754; *see also, e.g.*, 76 Fed. Reg. 3698; 75 Fed. Reg. 81519; 75 Fed. Reg. 80638.

shall be evaluated . . . ."[2] This term connotes more than consideration of costs and benefits; it requires that they be weighed. Unfortunately, in a report issued in April, your Inspector General found significant weaknesses in your Agency's economic analysis, and a general bare-minimum approach that ignored input from your Chief Economist. Specifically, and consistent with the recommendations issued by your Inspector General, we recommend that you incorporate and elevate the Office of the Chief Economist in the cost-benefit analysis performed pursuant to any final rule proposal.

Rationalize the Sequence of Rules

Throughout this process, Members of Congress on both sides of the aisle have urged you to issue rules proposing product and entity definitions prior to moving forward with any further rule proposals. This is more critical than ever before as you bring final rules before the Commission. It is impossible for both Commissioners and stakeholders to know the full impact of the proposed rules without a clear understanding of the scope of entities and products that will be impacted. For example, the Commission recently voted to finalize the rule "Large Trader Reporting for Physical Commodity Swaps". This rule imposes new reporting requirements on, among others, swap dealers. Yet at the same time, the rule further defining "swap dealer" is still in proposed form, leaving stakeholders unclear about their own status and whether they will need to begin to comply with the new rule upon its effective date. This creates needless uncertainty in the process, and hampers the ability of Commissioners and stakeholders to assess the rule. In addition, it ties the hands of the staff responsible for conducting cost benefit analysis as they couldn't possibly know the full scope of entities impacted, and therefore costs associated with new requirements. We strongly recommend you progress the rules relating to product and entity definitions before any further final rules are proposed.

Improve the Transparency of Final Rules

We recognize the CFTC has taken new and unprecedented steps to increase the transparency of the rulemaking process, and we appreciate and commend you for those improvements. Now that you've moved into the final rule stage, we believe there are specific actions that you can take to further guarantee a transparent process that facilitates thoughtful review and analysis of the pending rules.

New rules governing the House of Representatives ensure the transparency of legislative proposals prior to their consideration on the House Floor. Any bill or joint resolution that has not been reported by a committee must be made publicly available three days prior to Floor consideration. We believe such a policy is appropriate for the CFTC as well, and in light of the sheer volume of rules that will be considered in the coming months, we recommend that you make final rule proposals publicly available seven days prior to the Commission's meeting to consider them.

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[2] 7 U.S.C. § 19(a)(1).

In addition, due to the complexity and length of the rules, it would be prudent for the Commission to limit the number of rule proposals it will consider in any public meeting to 3 or fewer. Not only will this facilitate the ability of Commissioners to carefully consider each proposal, it will reduce the subsequent piling on impact for stakeholders as they wade through hundreds of pages of final regulations.

Publish an Implementation Plan

The Commission should publish an implementation plan and timeline and subject it to public comment. To help market participants prepare to comply with dozens of new rules, including many that will require significant and costly infrastructure and technology builds, it would be extremely helpful for the Commission to publish a plan for the phasing of Title VII requirements, consistent with your public remarks that you will not pursue a "big-bang" approach to implementation. This transparency will help to mitigate any potential market disruption as rules become effective.

Minimize Differences Among Agency Proposals

Substantial differences remain among proposals issued by the CFTC, the Securities and Exchange Commission (SEC) and the prudential regulators. Creating divergent regulatory regimes for different products or market participants will only further complicate compliance, and impose undue and unnecessary costs for market participants. For example, despite a nearly identical statutory directive, the CFTC and SEC proposals with regard to Swap Execution Facilities contain significant differences that could force market participants to comply with two different regulatory regimes for economically comparable products. We believe that the SEC's approach to a "request for quote (RFQ)" system that requires the RFQ be transmitted to only 1 or more market participants strikes the right balance. It achieves the objective of enhanced transparency while retaining a market participant's ability to choose and preserving market liquidity. We would urge the CFTC to follow the SEC's interpretation, and further minimize any significant differences between agency proposals before the rules are proposed as final.

Provide Clarity on the Treatment of Affiliate Trades and Extraterritorial Scope

It is not clear whether, through multiple rules, the Commission will impose various regulatory requirements, appropriate for certain street-facing trades, to trades that occur between commonly owned or controlled affiliates. We strongly recommend that the CFTC issue guidance, through a proposed rule or other means and with sufficient time for stakeholders to comment, clarifying the treatment of transactions between affiliates. We urge the Commission to recognize that regulating trades among affiliates would tie up capital and cost jobs, increase consumer costs, and undermine efficiencies that end-users currently realize through centralized hedging affiliates. These consequences would not be offset by reductions in systemic risk, as inter-affiliate swaps are used to allocate risk within a corporate group.

Significant uncertainty also remains regarding the territorial scope of Title VII. Because the implications of the territorial reach of Title VII span multiple rule proposals, we strongly recommend that you provide clarity and guidance regarding the territorial scope of Title VII before you propose any further and relevant final rules, and provide stakeholders an opportunity to comment. In doing so, we urge you to consider the historical practice of U.S. regulators in recognizing and deferring to foreign regulatory oversight for activities occurring outside the U.S., consistent with recognized principles of international law.

Prioritize Mandatory Rulemakings

In light of the volume of rules that are required by Title VII, it is prudent to prioritize the time and resources of your staff. We recommend that you promulgate rules that are required before moving to rules that are not explicitly required by Dodd-Frank. For example, the CFTC has proposed to amend certain exemptions and exceptions to the Commission's Commodity Pool Operators (CPOs) and Commodity Trading Advisors (CTAs) registration requirements, potentially requiring the registration of tens-of-thousands of new entities. While we appreciate that you held a roundtable to take stakeholder input on this proposed rule, it is not explicitly required by Dodd-Frank and will impose a significant and generally duplicative regulatory regime on entities that will already face significant new regulation under Title VII. We recommend that you focus the Commission's attention and resources on rules that are required by Dodd-Frank, and postpone any additional or discretionary rulemakings until the Commission has fulfilled its mandates under Dodd-Frank.

Provide Clarity Regarding Standards for Rule Re-proposals

In light of the extensive number of public comments your agency has received that include suggestions to modify the proposed rules to better align with market practices and realities, we expect many rules will indeed change and will likely change substantially. We ask that you respond to the following questions by July 29th:

1.) How will the CFTC determine when a rule has changed so substantially that it will be re-proposed?
2.) How will you determine when changes meet the "logical outgrowth" standard that is the test devised by the courts when deciding whether sufficient notice and comment has been provided under the Administrative Procedures Act?
3.) Will the Commission view questions seeking additional input as part of a Notice of Proposed Rulemaking (NPRM) as a basis for meeting the "logical outgrowth" standard?
4.) Will guidance be provided to staff to ensure a consistent approach between the various rulemakings?

Thank you for your consideration of this letter, and for responding by July 29th. We would like to continue to work with you to ensure the implementation of Title VII

results in a robust regulatory regime for derivatives, while upholding the critical function the derivatives markets serve to businesses throughout the economy.

Sincerely,

Frank D. Lucas
Chairman
Committee on Agriculture

K. Michael Conaway
Chairman, Subcommittee
Subcommittee on General Farm
Commodities and Risk Management