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CHAIRMAN'S CORRESPONDENCE UNIT

Congress of the United States
Washington, D.C. 20515

December 16, 2010

The Honorable Timothy Geithner
Secretary
The Department of Treasury
1500 Pennsylvania Ave, NW
Washington, DC 20220

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

The Honorable Mary Schapiro
Chairman
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

The Honorable Ben Bernanke
Chairman
Federal Reserve
20th Street and Constitution Avenue, NW
Washington, DC 20429

Dear Secretary Geithner and Chairmen Gensler, Schapiro and Bernanke:

As the 112th Congress approaches, we would like to express our desire to work with you on implementation of the derivatives title ("Title VII") of the Dodd-Frank Act (P.L. 111-203). While you and your staffs are to be commended on the open and transparent implementation process surrounding Dodd-Frank to date, we would like to take this opportunity to voice concerns with the scope and direction of several proposed and pending agency rulemakings mandated under the Act.

As an initial matter, it is critically important that the commercial end-user exemption from the requirements of Title VII be implemented in a manner that is consistent with congressional intent. Both the June 30, 2010 letter written by Senators Dodd and Lincoln and the colloquy that occurred on the House floor that same day between Representatives Frank and Peterson made it clear that margin requirements should not be applied to end-users. To impose such requirements on companies that engage in the hedging of legitimate business risks would therefore defeat the purpose of the end-user exemption and contravene Congressional intent.

As our economy slowly recovers, we have serious concerns that Dodd-Frank will force American companies, which did not cause nor contribute to the financial crisis, to move billions of dollars in capital onto the sidelines to comply with the law. Requiring end-users to post margin will delay or prevent businesses from expanding and will limit the creation of badly needed jobs. End-users must be able to rely upon their exemption from the clearing and exchange trading requirements without having to overcome unnecessary bureaucratic obstacles. Regulators must also not apply margin to existing derivative contracts as doing so would retroactively upset the rational expectations of thousands of end-users. Further, creating a prohibitively expensive and rigid climate for the use and trading of derivatives in the United States could shift this market overseas. Undoubtedly, foreign markets are closely examining how U.S. regulators are implementing Dodd-Frank and stand ready to create a competing non-punitive derivatives marketplace.

Your agencies should also carefully consider the scope of who is defined as a swap dealer, security-based swap dealer, major swap participant, and major security-based swap participant. Casting an overly-broad net in defining these terms could force some smaller participants to leave the marketplace as a result of increased costs, or eliminate certain types of contracts used for hedging. If either occurs, businesses will be left exposed to market volatility and the consequences will ultimately be felt by Americans in the form of increased consumer costs.

Our other concerns with Dodd-Frank implementation go beyond the end-user exemption. It is vital that foreign exchange (FX) swaps and forwards should be exempt from the clearing and exchange trading requirements because they are unlike other derivatives products regulated under Dodd-Frank. The FX market is stable, and will become more transparent with the imposition of the Dodd-Frank reporting requirements. So too, real-time reporting and trade execution requirements, if implemented without adequate safeguards, could unnecessarily increase the price of entering into a derivatives contract to hedge risk by, among other things, facilitating speculative "front running." No one disagrees that regulators should have real-time access to derivatives data. However, mandating real-time reporting of thinly-traded products and illiquid markets in an attempt to force derivatives to trade similarly to exchange-listed products is a fundamentally flawed approach that demonstrates a lack of understanding of the existing market structure.

Further, regulators must preserve the sanctity of existing derivatives agreements to allow businesses to effectively hedge against future risks. Also, it is imperative that we bring transparency to the derivatives marketplace without increasing the potential for systemic risk. As Title VIII of the Dodd-Frank Act allows "financial market utilities" to have access to the Federal Reserve's discount window in times of crisis, regulators must avoid the forced concentration of risk onto a few exchanges, trading platforms, or execution facilities which meet narrow and pre-determined regulatory expectations. Concentrating this risk could create, rather than diminish, systemic risk. As we have seen time and time again, any provision which enables government funding has the potential to precipitate taxpayer-funded bailouts, which we unalterably oppose.

We hope that your agencies will make use of the exemptive authority granted by the Act to avoid establishing position limits which would force widely-held funds or firms to divest their current holdings in highly regulated products. Overly-prescriptive position limits would drain existing liquidity from the capital markets, impair price discovery for commercial producers and their counterparties, and cause unnecessary harm to the futures markets and small investors.

Finally, an overarching concern regarding implementation of Title VII is the need to get it done right, not necessarily get it done quickly. If implemented hastily or without due care, these regulations could damage America's economic engine – the manufacturers, technology companies, real estate developers, and companies that provide vital financing to consumers and American businesses. Accordingly, as you move forward with your agencies' implementation of the Dodd-Frank Act, we encourage you to carefully deliberate and take the time necessary to ensure that implementation of the Act's major overhaul of the derivatives market is done correctly the first time.

We stand ready to work with you even if that means we all consider delaying statutory deadlines or moving forward with legislation to preserve a viable American derivatives marketplace.

Sincerely,

Spencer Bachus
Ranking Member
Committee on Financial Services

Frank Lucas
Ranking Member
Committee on Agriculture