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U.S. House of Representatives

Committee on Energy and Commerce

SUBCOMMITTEE ON TELECOMMUNICATIONS AND FINANCE

Washington, DC 20515-6119

HERBERT H. BROWN
CHIEF COUNSEL AND STAFF DIRECTOR

November 24, 1992

The Honorable Wendy L. Gramm
Chairman
Commodity Futures Trading Commission
2033 K Street, N.W.
Washington, D.C. 20581

Dear Chairman Gramm:

I am writing to express the Subcommittee's concerns regarding the potentially anti-competitive implications of a recent request by the Chicago Board of Trade (CBOT) for the submission of risk assessment information by certain registered broker-dealers.

As you may recall, two years ago Congress enacted the Market Reform Act of 1990, which contained provisions authorizing the Securities and Exchange Commission (SEC) to obtain information regarding the financial and operating condition of broker-dealer holding company systems.

The Subcommittee on Telecommunications and Finance initiated Congressional efforts to provide the SEC with this authority in order to facilitate the Commission's ability to monitor potentially risky activities conducted outside of the regulated broker-dealer which might involve significant potential exposure to the broker-dealer entity (such as interest rate swaps, bridge loan financing, and foreign currency transactions). The Congress determined that it was particularly important for the SEC to have access to information regarding the extent of such activities in order to assess the stability of broker-dealer participants in the securities marketplace during adverse market conditions. Because of the extremely sensitive proprietary nature of the financial information required to be provided to the SEC under the risk assessment provisions of the Act, the Congress directed that the SEC be given an exemption from Freedom of Information Act (FOIA) public disclosure requirements.

Using the risk assessment authority granted by Congress in the Market Reform Act of 1990, the SEC has adopted new rules 17h-1T and 17h-2T, which, together with new Form 17-H, require broker-dealers to maintain and file with the SEC certain information concerning the financial and securities activities of "Material Associated Persons."

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It has recently come to the Subcommittee's attention that on October 15, 1992, the Chicago Board of Trade asked those broker-dealers who are also member futures commission merchants (FCMs) to provide the CBOT with copies of such filings and to provide written notification to the CBOT describing what information, if any, they are required to file with the SEC under the new rules. A copy of the CBOT letter which made this request is enclosed (See Attachment A). On October 26, 1992, the Securities Industry Association requested that the CBOT withdraw its request for routine submission of risk assessment data (see Attachment B). In response, the CBOT, in an October 28, 1992 letter, announced that it "has subsequently reconsidered this requirement and has determined that this information need not be filed with the CBOT on a routine basis" (See Attachment C). This letter also indicated that "the CBOT may, however, require Broker/Dealers to file this information on an as needed basis."

This episode raises a number of troubling questions. During the last few months, the CBOT has expressed a clear interest in entering into the \$4 trillion international swaps market to compete with the banks and broker-dealer affiliates who presently offer these risk-shifting instruments. Indeed, during recent Congressional consideration of H.R. 707, the Futures Trading Practices Act of 1992, the CBOT lobbied intensively for modifications in provisions granting the CFTC authority to exempt swaps from regulation as futures contracts precisely because it hoped to improve its competitive position vis-a-vis the over-the-counter swaps market.

Given this background, the Subcommittee is troubled by the CBOT's recent request for sensitive proprietary information from broker-dealers who are also member FCMs. The initial CBOT request failed to indicate why the exchange was seeking routine access to this type of financial information or how it intended to use make use of the data it was seeking. While the CBOT has reconsidered its request for routine submission of risk assessment data for the time being, it has indicated that it may require broker-dealers to file risk assessment data at some point in the future.

Given the apparent conflict between the CBOT's self-regulatory role as a futures exchange and its apparent desire to become a competitor in the swaps market, the Subcommittee is concerned that any risk assessment information provided to the CBOT in the future might be utilized by the CBOT or associated persons to gain a competitive advantage over other participants in the swaps market. Moreover, it is unclear what legitimate self-regulatory purpose is served by requiring broker-dealer FCMs to provide risk assessment information directly to the CBOT, when

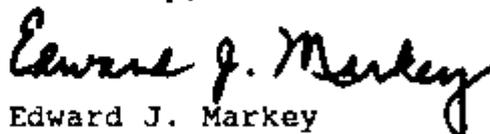
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the Congress, as part of the recently enacted CFTC reauthorization bill, has granted the CFTC authority to obtain this type of financial information directly from the entities it regulates. The Subcommittee notes that the grant of risk assessment rulemaking authority to the CFTC also included a FOIA exemption in order to assure confidential treatment of this sensitive proprietary information.

Given this situation, the Subcommittee requests that the CFTC commence a review of the CBOT's request for risk assessment data from broker-dealer FCM's in order to determine: 1) whether it is appropriate for such information to be provided directly to the CBOT in light of its competitive interests; and, 2) whether direct FCM provision of risk assessment information to the CFTC would better serve the objective of assuring that regulators are able to monitor risks assumed by associated persons of regulated entities. In addition, the Subcommittee requests that the CFTC take whatever actions are necessary to prevent the futures exchanges from gaining competitive advantages by obtaining access to sensitive risk assessment data in the future, including, if it is deemed necessary and in the public interest, undertaking steps to deny the CBOT the authority to compel the direct submission of such information.

Thank you for your consideration in this matter. Should you have any questions regarding the Subcommittee's request, please have your staff contact Mr. Jeffrey S. Duncan of the Subcommittee staff at 202-226-2424.

Sincerely,



Edward J. Markey
Chairman

Attachments