

ALBERTO GIOVANNINI

January 14, 2013

The Honorable Gary Gensler  
U.S. Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21st Street, N.W.  
Washington, D.C. 20581

Dear Chairman Gensler:

I am writing to express concerns over the pending CME Rule 1001. Over the years I have attempted to increase the public's and authorities' awareness of the importance of an efficient and robust infrastructure for financial markets. I have been pursuing this objective first as the chairman of the Giovannini Group, sponsored by DG ECFIN and DG MARKT in the European Commission, which has proposed a series of reforms of technical standards, conventions, regulations and laws aimed at creating a barrier-free environment for clearing and settlement in the European Union. Currently, I am a member of the Advisory Scientific Committee of the European Systemic Risk Board, which has a keen interest in the development of infrastructures to help strengthen the financial system and prevent systemic events. In addition, I am an independent board member of DTCC DerivServ LLC, an entity that is pursuing the task of offering authorities and market participants the opportunity to minimize the informational externality that characterizes our transactions-based system, and of developing what I regard as the most significant innovation in the infrastructure of financial markets in the past couple of decades.

The fundamental nature of financial market infrastructures is the mix of private and public character of the services they offer. Preventing private interests to jeopardize the public functions of infrastructure providers has been a recurrent challenge in my experience. Indeed, I recall that even our brief conversations at the 2009 EC Conference on Derivatives hosted by Commissioner McCreevy highlighted this problem, as we observed that the very large, and largely offsetting, derivative books of global broker dealers are equivalent to internal central counterparties, and have proven to be a weak link in the system in case of extreme events—hence the appropriateness of mandating the use of central counterparties, to the practically possible extent. This is just one of the many cases in which private and public interests may collide: the most frequent being the survival of governance models ill-suited to the natural-monopoly character of many of these businesses, the vertical integration of services—which limit the choice of users typically with the objective of subsidizing segments of the business more exposed to competition, and, in many countries, the close relation between infrastructural

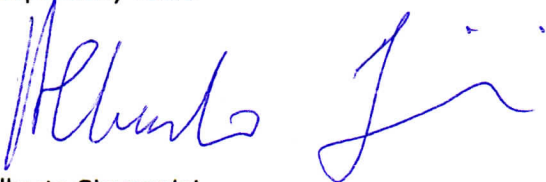
providers and supervisors, which in some cases has hindered the development of open and integrated systems which are essential in our global financial market.

The objective of building a truly effective global public good containing all information on derivative transactions of market participants—and therefore capable of providing a complete and accurate picture of the distribution of risk in the financial system—is meeting the same problems mentioned in the above paragraph. In this specific case, however, the consequences of allowing fragmentation and preventing open and fair access are more serious than just increasing the cost of the service: they defeat the public good purpose of the project, to the extent that they prevent accurate reconciliation of all trades—thus precluding the accurate picture of the distribution of risk in the financial system. This problem is especially critical because of the global nature of many derivative transactions: only 20 percent of credit derivatives are domestic, the rest cross border (see <http://www.bis.org/statistics/otcder/dt27.pdf>), while in foreign exchange and interest rate derivatives, US based turnover represents respectively 18 percent and 24 percent of global data (<http://www.bis.org/publ/rpfx10t.pdf>), and the majority of this is again cross border, e.g. approximately 70 percent of activity for interest rate swaps. The majority are transactions that occur outside the US, and a majority of those within the US are cross-border.

Thus, the creation of this essential public good in the financial system is threatened by the incentive that some infrastructure providers see in developing trade repositories as a means to protect revenue, or by the concern of some regulators to apply the principle “every country its own trade repository,” a principle fundamentally inconsistent with the international nature of most derivative trades.

Such challenges can only be met with shared awareness between market participants and regulatory authorities. I believe there is still a lot to be done and some difficult problems to be tackled, especially in developing the right governance structures for these global public goods, but I am also quite optimistic that authorities will see more clearly the value of the public good and accompany its development in the interest of a more robust financial system.

Respectfully Yours



Alberto Giovannini