

**HOUSE AGRICULTURE COMMITTEE REAFFIRMS PREFERENCE
FOR COMMODITY FUTURES TRADING COMMISSION AS OVERSEER
OF CREDIT DEFAULT SWAPS**

The House Agriculture Committee (the “Committee”) held a hearing on Thursday, November 20, 2008, on credit default swaps (“CDS”) as part of its continuing review of the role of credit derivatives in the U.S. financial market. The Committee has legislative jurisdiction and oversight authority over the Commodity Futures Trading Commission (the “CFTC”). At a hearing last month, the Committee considered the role of CDS in the failure of a number of large financial institutions and reviewed the existing system of regulated exchanges and the market for over-the-counter (“OTC”) derivatives. The November 20 hearing focused on the current plans for the establishment of a clearing mechanism for CDS and the November 14, 2008 Memorandum of Understanding (the “MOU”) on CDS markets signed by the CFTC, the Securities and Exchange Commission (the “SEC”), and the Federal Reserve with respect to CDS.

There was a clear consensus among Committee members that the CFTC is better suited than either the SEC or the Federal Reserve to oversee the central clearinghouses currently being organized to settle CDS because of the CFTC’s experience in regulating swap products.

The Committee repeatedly challenged the SEC and the Federal Reserve witnesses to defend their agencies’ interest in CDS and also made clear that the Committee opposes proposals to merge the CFTC with the SEC. The Committee also heard from the New York State Insurance Department, which announced at the hearing that it will delay previously announced plans to begin regulating certain CDS as insurance in January 2009.

Only one panel of witnesses was called to testify, consisting of Ananda Radhakrishnan, Director of the CFTC’s Division of Clearing and Intermediary Oversight; Patrick Parkinson, Deputy Director of the Federal Reserve Board’s Division of Research and Statistics; Erik Sirri, Director of the SEC’s Division of Trading and Markets; and Eric Dinallo, Superintendent of the New York Insurance Department. Their prepared testimony is available at <http://agriculture.house.gov/hearings/statements.html>.

Chairman Peterson’s opening statement noted that “at some point, our regulators and the next Congress will have to get to the root of the [CDS] problem before it is too late and allow for some real oversight of these markets, to provide transparency and accountability for both buyers and sellers, and to reduce systemic risk.” In the meantime, Peterson spoke favorably of the creation of one or more central-party clearinghouses for CDS because they would “improve transparency and risk management” and “create a method for price discovery.” Other Committee members agreed that a system of central counterparties would contribute to greater understanding of the CDS market.

In its testimony, the CFTC highlighted the extensive institutional knowledge and regulatory expertise in derivatives clearing that it had developed through its supervision of the derivatives clearing organizations (“DCOs”) established by the Commodity Futures Modernization Act (the “CFMA”). Mr. Radhakrishnan described the DCO clearing model as working well for a wide variety of products and asserted that it should work equally well for CDS transactions.

The Federal Reserve (Mr. Parkinson) testified that it could become the primary regulator of one of the proposed clearinghouses that may be organized as a limited-purpose trust company chartered as a state bank in New York, which would be a member of the Federal Reserve System. In response, Chairman Peterson was skeptical as to why the Fed should have this “new job” of regulating a clearinghouse, which he characterized as “an area in which [the Fed] has no history.” Mr. Peterson emphasized that the CFTC is already able to assume this function “within its existing mission.”

The SEC (Mr. Sirri) observed that OTC market participants typically structure their CDS activity under the swap exclusion in the CFMA. Mr. Sirri asserted that, if CDS were standardized as a result of centralized clearing, exchange trading, or other market developments and were thus no longer individually negotiated, the CFMA’s swap exclusion would no longer be available and CDS would become standardized contracts and thus securities subject to SEC jurisdiction. The CFTC and several committee members disputed this conclusion. In addition, one committee member called swaps traders “sophisticated market players” that, historically, have not required the SEC’s protection.

Several committee members expressed concern over the prospect of “split jurisdiction” over CDS because it might create either a “fragmented market” or excessive “piling on” of regulatory oversight by multiple agencies. Each agency also pointed to the MOU as evidence of its willingness to cooperate and collaborate.¹ In the MOU, the CFTC, the Federal Reserve, and the SEC each stated that it has responsibilities in “overseeing certain systemically important payment, clearing, and settlement activities and certain market utilities that support those activities.” Regarding central counterparties for CDS, the three agencies agreed to “cooperate, coordinate and share information” to advance their “common interest in strengthening the infrastructure supporting the clearing and settlement of [CDS].”

The New York Insurance Department (Mr. Dinallo) announced the suspension of its plan to regulate some swaps as insurance products, citing the progress made at the federal level and its reluctance to complicate development of a federal regulatory scheme. He recommended that federal regulation of CDS be comprehensive and mandatory and that it include, among other provisions, capital requirements, a dispute resolution mechanism, and a guaranty fund.

¹ The MOU and related information may be viewed at <http://www.ustreas.gov/press/releases/hp1272.htm>.

In a separate development on November 20, Senate Agriculture Chairman Tom Harkin (D-IA) introduced the Derivatives Trading Integrity Act, which Harkin said would establish stronger standards of openness, transparency, and integrity in the trading of swaps and other over-the-counter financial derivatives. Among other provisions, the legislation would eliminate the statutory exclusion of swap transactions and terminate the CFTC's authority to exempt such transactions from the general requirement that a contract for the purchase or sale of a commodity for future delivery can trade only on a regulated board of trade.² Harkin's committee has jurisdiction in the Senate over the CFTC.

In view of the significant interest of both the House and the Senate Agriculture Committees in CDS, it appears that legislative proposals to increase federal regulation and oversight of these and other derivative instruments will be actively considered by Congress next year. It is likely that debate on such legislation will include attempts to clarify federal regulatory oversight of central counterparties or to consolidate oversight in the CFTC.

* * * * *

This memorandum was prepared by Russell L. Smith, Leah Campbell, Jack I. Habert and Barbara Anne Block. If you have any questions about this memorandum, please contact any of the members of the WF&G New Administration/Congress Task Force listed below or the attorney with whom you regularly work. The New Administration/Congress Task Force has been formed to provide information and targeted advice, and to respond to questions from clients in connection with the legislative, regulatory, and enforcement and compliance initiatives, and potential litigation, that will result from the new U.S. presidential administration and Congress.

² Links to a more detailed description of Chairman Harkin's legislation, and the text of the bill itself, may be found at <http://agriculture.senate.gov/>.

NEW ADMINISTRATION/CONGRESS TASK FORCE		
<i>Antitrust</i>	<i>Compliance, Investigations and Enforcement</i>	<i>Derivatives and Structured Products</i>
Bernard Nigro, Jr. (202) 303-1125 bnigro@willkie.com	Jeffrey Clark (202) 303-1139 jdclark@willkie.com	Thomas French (212) 728-8124 tfrench@willkie.com
William Rooney (212) 728-8259 wrooney@willkie.com	Robert Meyer (202) 303-1123 rmeyer@willkie.com	Jack Habert (212) 728-8952 jhabert@willkie.com
Theodore Whitehouse (202) 303-1118 twhitehouse@willkie.com	Martin Weinstein (202) 303-1122 mweinstein@willkie.com	<i>Environment, Health & Safety</i>
<i>Asset Management</i>	<i>Corporate and Financial Services</i>	E. Donald Elliott (202) 303-1120 delliott@willkie.com
Barry Barbash (202) 303-1201 bbarbash@willkie.com	Gregory Astrachan (212) 728-8608 gastrachan@willkie.com	<i>Estate Tax</i>
Larry Bergmann (202) 303-1103 lbergmann@willkie.com	Thomas Cerabino (212) 728-8208 tcerabino@willkie.com	David McCabe (212) 728-8723 dmccabe@willkie.com
Benjamin Haskin (202) 303-1124 bhaskin@willkie.com	Steven Gartner (212) 728-8222 sgartner@willkie.com	<i>Government Relations</i>
Rita Molesworth (212) 728-8727 rmolesworth@willkie.com	Bruce Herzog (212) 728-8220 bherzog@willkie.com	Russell Smith (202) 303-1116 rsmith@willkie.com
<i>Biotech/Pharmaceutical Regulation</i>	Bruce Kraus (212) 728-8237 bkraus@willkie.com	<i>Insurance</i>
Peter Jakes (212) 728-8230 pjakes@willkie.com	Jack Nusbaum (212) 728-8060 jnusbaum@willkie.com	Mitchell Auslander (212) 728-8201 mauslander@willkie.com
<i>Business Reorganization & Restructuring</i>	Steven Seidman (212) 728-8763 sseidman@willkie.com	Leah Campbell (212) 728-8217 lcampbell@willkie.com
Marc Abrams (212) 728-8200 mabrams@willkie.com		

<i>Litigation</i>	<i>Securities Litigation & Enforcement</i>	<i>Tax</i>
David Murray (202) 303-1112 dmurray@willkie.com	Richard Bernstein (202) 303-1108 rbernstein@willkie.com	Richard Reinhold (212) 728-8292 rreinhold@willkie.com
Jeanne Luboja (212) 728-8241 jluboja@willkie.com	Gregory Bruch (202) 303-1205 gbruch@willkie.com	<i>Telecommunications and Data Privacy</i>
<i>Purchases of Real Estate Assets and Real Estate Related Securities</i>	Mei Lin Kwan-Gett (212) 728-8503 mkwangett@willkie.com	Francis Buono (202) 303-1104 fbuono@willkie.com
Eugene Pinover (212) 728-8254 epinover@willkie.com	Julie Smith (202) 303-1209 jasmith@willkie.com	Thomas Jones (202) 303-1111 tjones@willkie.com
	Michael Young (212) 728-8280 myoung@willkie.com	Philip Verveer (202) 303-1117 pverveer@willkie.com

Willkie Farr & Gallagher LLP is headquartered at 787 Seventh Avenue, New York, NY 10019-6099 and has an office located at 1875 K Street, NW, Washington, DC 20006-1238. Our New York telephone number is (212) 728-8000 and our facsimile number is (212) 728-8111. Our Washington, DC telephone number is (202) 303-1000 and our facsimile number is (202) 303-2000. Our website is located at www.willkie.com.

November 24, 2008

Copyright © 2008 by Willkie Farr & Gallagher LLP.

All Rights Reserved. This memorandum may not be reproduced or disseminated in any form without the express permission of Willkie Farr & Gallagher LLP. This memorandum is provided for news and information purposes only and does not constitute legal advice or an invitation to an attorney-client relationship. While every effort has been made to ensure the accuracy of the information contained herein, Willkie Farr & Gallagher LLP does not guarantee such accuracy and cannot be held liable for any errors in or any reliance upon this information. Under New York's Code of Professional Responsibility, this material may constitute attorney advertising. Prior results do not guarantee a similar outcome.