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Senate confirmation for CFTC chair spotlights past mistakes

By Jon H. Harsch

When the Senate Agriculture Committee met Wednesday to consider President Obama's nomination for the new chairman of the Commodity Futures Trading Commission (CFTC), there were lots of regrets. In 1999, a former Goldman Sachs partner fought successfully to free derivatives trading from government regulation when he was a U.S. Treasury Department official. He now regrets his past defense of derivates and promises to support tough derivatives market regulation today – if he's appointed CFTC chair.

Senate Agriculture Committee Chair Tom Harkin (D-IA) considers it likely that former Goldman partner and Treasury official Gary Gensler will be confirmed by the Senate. But to make sure that Gensler has learned from his earlier mistakes, Harkin dredged up the past. Harkin noted that on May the 18, 1999, Gensler testified in House Agriculture Subcommittee hearings that he "positively, unambiguously" agreed with then Treasury Secretary Larry Summers in opposing additional regulation of the over-the-counter derivatives market. Harkin reminded Gensler that "You went on to refer to the 'vibrancy and importance' of the global over-the-counter derivatives market. You said 'that large and vibrant market is part of, I believe, the American success and we should recognize that and put the burden on those who are suggesting changes and further regulation, put the burden on them, before we tamper on some of the successes of this marketplace for the economy.'"

Harkin pointed out to Gensler that in 1999 when the CFTC itself was fighting for more authority to regulate derivatives trading, "you were part of the team arguing. . . for a statutory enactment to take away all CFTC regulatory power over these over-the-counter derivatives."

Gensler responded with this explanation: "Looking back now, it is clear to me that all of us that were involved at the time, and certainly myself, should have done more to protect the American public through aggressive regulation, comprehensive regulation. We should have fought harder for some of the things that we raised with Congress at the time, whether that be regulating derivates dealers or keeping the oil and metals markets consistently regulated with the corn and wheat and soybeans markets. . . I believe there were many things at the time that we could not foresee or didn't see. They were just dots on the landscape. . . We have to do a far better job of seeing that which is out on the horizon."

Senator Ken Conrad (D-ND) had his own regrets. In Gensler's confirmation hearing, Conrad blamed the current economic crisis on serious mistakes including "bum advice" from Gensler and others. He said today's problems began with "a combination of a very loose monetary policy, very loose fiscal policy, very loose trade policy, all coupled with deregulation that created the seedbed for bubbles to form. And we didn't get just a housing bubble. We got an energy bubble. We got a commodity bubble. And when those bubbles burst, it did enormous damage. There's a lot of wreckage here. And all of us have responsibilities."

Conrad said deregulating the derivatives markets was "very, very wrong and I regret deeply of my own going along with it." Charging that "You too have responsibility," Conrad then asked for Gensler's comments. Gensler replied: "Looking back now, it is clear to me that those of us involved at the time should have done more to protect the American public through strong, comprehensive and aggressive regulation."

Clearly differentiating himself from his 1999 former self, Gensler made the same points in his opening statement to the committee, telling Senators:

> "I firmly believe that strong, intelligent regulation with aggressive enforcement is what our economy needs and benefits the public. The current economic crisis clearly has shown that our financial and regulatory systems have failed the American public terribly. Those of us who have spent our professional lives around markets have to approach the current crisis with humility following these broad failures. We have learned the limits of our ability to foresee how markets may evolve, we have learned the importance of being candid with the public about the risks we face and the need for unceasing vigilance to address them. We have learned that there is no substitute for strong independent regulation and that transparency and accountability are essential throughout the system. We must always err on the side of protecting the American people."

Well aware of the committee's concerns about his past mistakes, Gensler continued:

> "Those are the lessons that I draw from what has dramatically transpired over the past decade. If confirmed by the Senate, I pledge to this committee that I will not forget these lessons. We must now repair our regulatory system by enacting much-needed reforms that promote transparency, fairness and safety. . . I am a proud believer in financial reform, though regulation and enforcement."

Following the hearing, Harkin said that "Mr. Gensler was very forthright in saying that his views have changed over the years" and said he expects Gensler's nomination to go forward quickly, without opposition. But he said he remains concerned – particularly by suggestions that some "customized" OTC derivatives trading should be allowed to continue. He said he continues to believe that all derivatives ought to be traded on regulated exchanges, "and if they are not, they shouldn't exist."

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