I am Terry Duffy, Chairman of Chicago Mercantile Exchange Holdings, Inc., which owns and operates the largest U.S. futures exchange, and by many standards, the largest futures exchange in the world. Chairman Chambliss and ladies and gentlemen of the Committee, I am very pleased to participate in this important hearing regarding reauthorization of the Commodity Futures Trading Commission and its key statutory framework, the Commodity Futures Modernization Act of 2000 ("CFMA"). This timely hearing provides the Committee the opportunity to consider whether CFMA set a course for the industry that should continue or if the CEA is ripe for revision. To that end, my testimony first will summarize the enormously positive changes that CME has experienced since enactment of the CFMA and then will conclude with our recommendations on issues which warrant the Committee's attention in reauthorizing the CFTC this year.

I. OVERVIEW OF CFMA: HISTORIC AND SUCCESSFUL LEGISLATION

Throughout the 20th Century, and especially so during the past three decades, the CME has earned a reputation as a premier innovator and industry pacesetter in developing new products and trading opportunities. Given this heritage of innovation and being an exchange that was eager to bring its business model into the 21st Century, CME strongly believes that the CFMA has been an enormous success. As many of you who were deeply involved in the reauthorization effort five years ago may recall, the established exchanges supported legal certainty for OTC products and reduced barriers to entry of new exchanges in return for an elimination of prescriptive regulation and freedom to innovate. And innovate we did, predominantly in four areas: governance (including our role as a self-regulatory organization (SRO)); expansion of market penetration; innovation in product offerings; and pursuit of a legitimate entrepreneurial business model that is premised on meeting customer needs.

In the judgment of CME, the CFMA of 2000 represents successful landmark legislation that materially and beneficially reformed some of the nation's most important financial markets. Specifically CME gained the right to demutualize and implement the form of governance necessary to complete a successful initial public offering (IPO) and to run a highly effective and efficient SRO. The scope and velocity of CME's expansion of its markets and product offerings has been unprecedented. CME's ability to expand its clearing services to other exchanges and to unregulated markets has been a boon to our customers and, as a consequence, to our bottom line.

U.S. futures markets are substantially stronger and more vibrant today as the direct result of Congress's enactment of the CFMA and, equally importantly, the CFTC's judicious and deliberate implementation of those reforms. Innovation has been encouraged and made less costly and more rewarding. The time between conception of a new product or trading system and its implementation has gone from years to days. Today, the vast majority of CME's investment in innovation is for products rather than paperwork and regulatory review. Our customers applaud CME's aggressive response to the CFMA's incentives for innovation and competition as evidenced by their enthusiastic response to our slate of products and services.

By illustration I would point out the following:

? Continuing the trend since the CFMA's enactment in late 2000, CME's average daily volume in February has increased more than 50% over the comparable period in 2004, when our average daily volume exceeded 3.8 million contracts, an all-time record.

? Electronic trading volume on CME® Globex® grew to more than 2.5 million contracts per day, representing 66% of total exchange volume in February.

? CME's Eurodollar futures contract remains the benchmark interest rate product around the world, commanding 97% of the daily trading volume. Average daily volume of CME Eurodollar futures on CME Globex in February exceeded 1.2 million contracts. This represented 77percent of total CME Eurodollar volume in February compared with 15 percent in February 2004.

? CME's FX markets hit an all-time volume record in February as average daily volume totaled more than 266,000 contracts, representing notional value of $35 billion per day and an increase of 49% from one year earlier. During the month, CME electronic foreign exchange products increased 83 percent from the same period one year ago to reach 210,000 contracts per day.

? Trading in CME E-mini? equity index products averaged 1.1 million contracts per day in February, up 16 percent versus the same period last year.

? CME's commodity products also continue to trade well, with average daily volume in February at 43,000 contracts, up 35 percent from one year ago.

? Finally, the historic transaction processing agreement between CME and CBOT has delivered on its promise of efficiencies and $1.8 billion in capital cost savings to our joint members, setting new industry standards for responsiveness and efficiency.

II. CFMA HAS FOSTERED INNOVATION IN SELF-REGULATION

CME takes considerable pride in our status as the first demutualized and publicly-traded exchange in the United States. CME is currently the largest futures exchange in the United States and the largest derivatives clearing organization in the world. Moreover, our business has steadily migrated from the trading pits to our open access electronic trading platform---CME Globex. These changes have had a profound, positive impact on our financial performance, but as importantly on our customers' perception of our performance of our self regulatory responsibilities.

With our IPO, CME is now subjected to the stringent corporate governance standards and listing requirements imposed by the New York Stock Exchange, public disclosure of all material aspects of its business, and continuous scrutiny from savvy analysts and institutional investors. In order to meet our obligations and to instill confidence in our shareholders, CME's Board of Directors has transitioned to one that is both fiercely independent of management and well beyond the control of floor brokers and traders. CME was the pioneer in including non-exchange members in its disciplinary processes and in insuring that its important standing Board Committees were led by and included significant representation of non-industry directors. The charters of all of these committees including the Market Regulatory Oversight Committee ("MROC"), which is composed entirely of non-industry directors and is directly responsible for the independence of the SRO function, are found at CME's website.

On April 30, 2004, CME became the first futures exchange to appoint a Board-level committee devoted to self-regulatory oversight. CME's MROC is comprised solely of independent, non-industry directors. As set forth in its charter, the MROC is charged with the following responsibilities:

? to review the scope of and make recommendations with respect to the responsibilities, budget and staffing of the Market Regulation Department and the Audit Department so that each department is able to fulfill its self-regulatory responsibilities;

? to oversee the performance of the Market Regulation Department and Audit Department so that each department is able to implement its self-regulatory responsibilities independent of any improper interference or conflict of interest that may arise as a result of a member of CME serving on the Board or participating in the implementation of CME's self-regulatory functions;

? to review the annual performance evaluations and compensation determinations and any termination decisions made by senior management of CME with respect to the Managing Director, Regulatory Affairs, and the Director, Audit Department, so that such determinations or decisions are not designed to influence improperly the independent exercise of their self-regulatory responsibilities;

? to review CME's compliance with its self-regulatory responsibilities as prescribed by statute and the rules and regulations promulgated thereunder; and

? to review changes (or proposed changes, as appropriate) to Exchange rules to the extent that such rules are likely to impact significantly the self-regulatory functions of the Exchange.

We believe that the newly empowered MROC represents an aggressive and appropriate step towards independence in self-regulation.

III. CFMA HAS FOSTERED PRODUCT AND MARKET INNOVATION
We have all witnessed dramatic change in our industry during the last five years. CME has responded to these opportunities by successfully executing a growth strategy based on:

? Technology innovation;

? Continued product innovation;

? Expanding global distribution; and

? Leveraging the convergence of the cash, derivatives and over-the-counter (OTC) markets.

Technology Innovation:

In terms of technology innovation, we have redesigned our business model to leverage our electronic trading capability. A sign of our successful transformation is that five years ago, CME had 125 people focused on technology. Today, we have over 400 talented technologists, reflecting our view of the future. CME Globex today significantly outperforms its competitors by facilitating trading around the world more than 23 hours a day, five days a week and with a 150 to 200 millisecond average turnaround time.

Technology innovation at CME has become equal in importance to product innovation. And our ability to innovate is multi-dimensional. It involves expanded user functionality and faster response times. It also involves increased reliability and the implementation of system features designed to enhance market integrity and protect customers from anomalous market conditions. Last January, we provided market users with the most sophisticated implied spreading functionality in the industry. As a result, CME Eurodollar futures on CME Globex went from 9.6 percent electronic in January 2004 to 75 percent last December.

A year ago, we acquired innovative patent-pending technology that now provides market users with a sophisticated electronic solution for complex options combination trading. CME is committed to preserving and enhancing transparency and competition among market makers in electronic options markets. Transparency and price competition are the hallmarks of CME's successful market model.

Another measure of our ability to innovate with technology is something most people never see. Over the last five years, and due to the unique processing demands of our enormously successful E-mini? contracts, CME has built an extensive and highly scalable set of platforms and infrastructure. We now process over 600,000 match transactions daily, more than any other exchange in our industry. Part of our growth strategy is to offer processing services - and other collateral and risk management services - to other exchanges and trading platforms around the world.

Products:

Throughout the last 30 years, CME has been the leading product innovator in our industry, from financial futures in 1972, to cash settlement in 1981, stock index futures in 1982, CME Globex in 1987 and E-mini contracts in 1997. And in every case the world followed.

That leadership role has positioned CME with the most diverse and successful product line in our industry. Like technology, product innovation today at CME is becoming increasingly sophisticated. We work closely with market users to continually reassess product design, delivery system, trading conventions, pricing structure and other features that drive demand for our products.

This has fueled growth in each of our major product lines. For example, electronic trading of CME Eurodollar futures increased by 1,248 percent from 2003 to 2004. Our success is attributable to enhanced technology functionality, significant reductions in CME Eurodollar trading fees on CME Globex, and the implementation of our new CME Eurodollar market maker program - all of which has substantially enhanced liquidity on CME Globex.

Our popular E-mini stock index futures products also set a new record in 2004 with almost 265 million contracts traded, up 13 percent compared to 2003. Today, nearly 92 percent of trading activity in our equity products is electronic.

And these products have significantly outperformed other competing products, such as ETFs and equity index options.

Our foreign exchange product line has experienced nothing short of a renaissance in the last two years. Our electronic FX products have achieved a compound annual growth rate of 127 percent in average daily volume during the last two years. Volume growth in this product line is attributable to the speed of our CME Globex electronic trading system, our increasing distribution and our clearing house guarantee, as well as the declining value of the dollar.

Today, more than 80 percent of trading in our FX futures products occurs electronically. And, our FX product line has tremendous growth potential when one considers the nearly $2 trillion dollar a day turnover in global FX trading.

In addition to enhancing our existing core product lines, we will continue to innovate new products. Many of these new products will be more complex and highly structured products that meet the needs of more narrowly defined customer segments. While such products could not be easily or economically launched in the past, electronic trading enhances our opportunity for success.

Expanding Global Distribution:

CME has been working diligently over the last three years to dramatically expand global distribution and access to our GLOBEX system. We have done this by streamlining our application programming interfaces. In addition, we have introduced more flexible connectivity options, including user defined solutions which significantly reduce costs.
To expand the global distribution of our products, last year we installed telecommunications hubs in Dublin, Gibraltar, Frankfurt, Amsterdam, Paris and Milan, in addition to the one we installed in London in 2002. This growth initiative has been successful, allowing European customers to dramatically reduce their trans-Atlantic telecommunications costs. We plan to launch a similar hub in Singapore later this year.

In tandem with these technology enhancements and cost efficiencies, we put in place aggressive incentive pricing plans in both Europe and Asia to promote CME products and accessibility to CME Globex to new customers in those parts of the world.

The strong early response to this program suggests that we are succeeding in our strategy to bring new customers to CME who will find our products to be an attractive alternative to comparable euro-denominated products.

Another avenue of growth for us is to attract new distribution channel partners with the capacity to reach large numbers of nontraditional futures customers. We increased access to our products through an agreement with Bloomberg which allows all 180,000 screens worldwide to access CME products on CME Globex. Additionally, as we continue to expand trading activity in our popular E-mini contracts, we are implementing connectivity agreements with E*TRADE and Schwab's CyberTrader. These new distribution channels allow us to reach the emerging professional equity retail sector who increasingly find E-mini contracts more attractive than cash equities, equity options and ETFs.

Most recently, we announced a growth initiative with Reuters, where we will be offering CME's electronic foreign exchange markets to Reuters' global customer base. This initiative marks the first major linkage of sell side traders in the interbank FX market to CME eFX futures markets, where hedge funds and other major buy side participants play a major role, paving the way for more dynamic and efficient markets.

Common Clearing Link:

Our transaction processing agreement with the Chicago Board of Trade (CBOT) is up, running successfully and producing even more synergies than any of us could have imagined. This common clearing link with CBOT is providing $1.8 billion in capital cost savings to our joint members.

IV. CME's RECOMMENDATIONS FOR REAUTHORIZATION

While CME enthusiastically applauds the success of the CFMA and recommends that we retain its historic statutory framework, the upcoming Congressional reauthorization process offers a valuable opportunity to fine tune that statutory framework based on industry experience garnered since the CFMA's enactment in 2000. In that regard, CME offers two recommendations for consideration:

Off-Exchange Retail Futures Trading:

The first area in need of fine tuning involves the jurisdictional issues regarding retail trading of futures-like products. In particular, over the past four years of the CFMA, the CFTC has brought 70 enforcement actions involving 267 companies and individuals for illegal retail foreign exchange trading. CFTC estimates that these cases involved trading with over 20,000 customers and resulted in imposition of over $240 million in penalties and restitution orders. The confluence of the massive continuing frauds committed against retail customers in the OTC foreign exchange ("FX") market, and the recent, unfortunate decision of the 7th Circuit Court of Appeals in CFTC v. Zelener, compel this industry to reexamine the public policy implications of how the CFMA addresses retail foreign exchange futures and the threshold definition of what transactions should be subject to CFTC jurisdiction.

The fact that the CFTC is compelled to devote such substantial resources to protecting retail customers from significant fraud is evidence enough that a serious problem exists with the CFMA that cries out for reform. Moreover, in the aftermath of the Zelener decision, a retail product that most would agree is a futures contract--- but which has now been defined by the court to be a cash product---can be offered outside of the CFTC's jurisdiction. The sharp operators and bucket shops have already figured out that the rationale of the Zelener opinion can apply to commodities other than FX. How soon will it be before the CFTC's jurisdiction and its retail consumer protections are reduced to irrelevance?

At a minimum, we need an amendment that will preclude dealers from end-running CFTC's jurisdiction by simply inserting a one line caveat on their internet sites notifying counterparties that the dealer is not absolutely obligated to enter into an opposite, offsetting transaction or that under some circumstances an opposite transaction will not offset existing positions. The challenge for the futures industry---and this Committee--- is to find an effective solution that will politically survive the reauthorization process.

Security Futures Products:

The second area in which the CFMA needs to be modified is with regard to Single Stock Futures. In my Congressional testimony of June of 2003, I characterized single stock futures as "the CFMA's unfulfilled promise". I am sad to say what was true then remains so even today. As evidenced by their long-time successful use and acceptance in European markets, single stock futures can be a great product with enormous benefits to market users. However, inter-exchange competitive concerns combined with regulatory and legislative turf contests largely mitigated the hope for this product even before it was launched in this country. The regulatory system that has slowly evolved between CFTC and SEC has yet to address various key issues and several of the regulations that have been produced thus far are overly burdensome and inflexible, frustrating development of products that would be both useful and desirable to market participants.

It is time to let futures exchanges trade the product as a pure futures contract and to let securities exchanges trade it as a securities product. Let the relevant exchanges deal solely with their respective regulator, the CFTC or the SEC, which is what I believe the Congress intended in 2000 in authorizing single stock futures. We want competitive forces to determine the outcome--not government. Fulfilling that promise made in 2000 will advance the customers' interest substantially. We would encourage the Committee to use its oversight jurisdiction to insist that the respective regulatory agencies eliminate undue regulatory impediments that have been erected to frustrate the introduction of security futures products.

V. CONCLUSION:

The CME and its customers have prospered to the substantial benefit of the nation's economy under the CFMA. CME looks forward to engaging significantly in the upcoming reauthorization process and to achieving legislation that maintains the significant successes of the CFMA while making discreet corrections designed to materially improves the efficiency, competitiveness and fairness of our futures markets for our customers and all market participants.