Written Testimony of Yesha Yadav

Milton R. Underwood Chair
Professor of Law and Associate Dean
Vanderbilt Law School

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Witness Biographical and Background Statement

I am Milton R. Underwood Chair, Professor of Law and Associate Dean at Vanderbilt Law School, where I research financial market regulation, securities regulation, and corporate bankruptcy, focusing on market structure, exchange design, digital asset regulation, payments, debt and restructuring. An area of particular specialization is market microstructure, examining the regulation of trading ecosystems for various asset classes, notably, equity, U.S. Treasuries, corporate bonds and cryptocurrencies. I have written extensively on U.S. Treasury market oversight and regulation, authoring *Failed Regulation of U.S. Treasury Markets* in the Columbia Law Review, *The Failed Promise of Treasuries in Financial Regulation* (with Pradeep Yadav) in the Southern California Law Review, *Central Clearing the Treasury Market?* (with Joshua Younger) in the University of Chicago Law Review, *Stablecoins and the US Treasury Market* (with Brendan Malone) in the Journal of International Economic Law, among other works. I have served on the CFTC's Technology Advisory Committee (2018–2022).

This testimony reflects my own views only. I have not received any federal funds or compensation for my testimony and do not speak on behalf of any organization.

Chairman Lucas, Ranking Member Vargas, Members of the Task Force

Thank you for the opportunity to appear before you today. It is an honor to contribute to the essential work of this Task Force in examining the interaction between derivatives markets and the U.S. Treasury market.

I. The Stakes: Why U.S. Treasury Markets Demand Vigilant Oversight

The U.S. Treasury market is the most important securities market in the world. With approximately $30.8 trillion in outstanding marketable securities,[1] it serves as the benchmark for pricing risk across the global financial system, the primary instrument for conducting monetary policy, the core reserve asset for foreign central banks, and the collateral backbone of the derivatives and repurchase ("repo") markets. U.S. Treasuries are the uncontested safe asset in the global economy. These facts bear repeating and emphasizing at every stage of this discussion: the costs of neglecting risks to this market are extraordinarily high.

In turn, derivatives are critical for the functioning of the U.S. Treasury market. This can be seen in at least three ways. First, derivatives ensure that asset managers can manage their interest rate risks across a diverse range of exposures in a way that is cost-effective. Futures and swaps need only margin payments when parties take on positions in Treasuries-linked contracts. This means participants can manage their risks without having to assume the full capital cost of buying (selling) Treasuries. With a carefully and efficiently managed balance sheet, market participants are better prepared to assume more varied and complex risk exposures.[2] Secondly, the futures market helps promote informational efficiencies in the Treasuries market, where new insights usually emerge first in the futures market before being reflected in the underlying cash market.[3] Because trading on margin is cheaper than buying a Treasury outright, information traders tend to move first in the futures market, helping shape prices to reflect latest developments, with the underlying seeing knock-on changes as traders seek to transact away price differences between two interlinked markets. The result is an overall positive where both futures and the cash market show informational and price efficiencies. Thirdly, derivatives help promote the creation of a liquid Treasury market by enhancing its economic usefulness, encouraging expert derivatives traders, hedgers and arbitrageurs to contribute to buying and selling in both the Treasuries and Treasuries-backed repo market.

These functions are not abstract. Interdependencies between U.S. Treasury markets and derivatives are extensive and run in both directions. Two areas of interaction attract particular attention.

First, the cash-futures basis trade. The basis trade involves the simultaneous purchase of cash Treasury securities and the sale of Treasury futures, profiting from any price differential that exists between two essentially equivalent assets or streams of cash flows. The spot and the futures markets usually remain well aligned, owing largely to arbitrage-focused traders (typically hedge funds). By March 2025, CFTC data showed that leveraged fund net short positions in Treasury futures with maturities up to ten years exceeded

[1] U.S. Dep't of Treasury, Bureau of the Fiscal Service, Monthly Statement of the Public Debt (Mar. 31, 2026). As of March 2026, total public debt outstanding stood at approximately $39.01 trillion, with approximately $30.8 trillion in marketable securities.

[2] See Treasury Borrowing Advisory Committee, Discussion of Treasury Futures Positions Across Different Investor Types, TBAC Charge Q1 2024 (Jan. 30, 2024) (documenting that, asset managers, including mutual funds and pension funds, are structurally long Treasury futures because they use futures to match the duration of their bond benchmarks while allocating capital to higher-yielding assets such as corporate bonds and mortgage-backed securities. This persistent demand from asset managers for long futures exposure is met by hedge funds and other leveraged participants who take the short side of the futures market, creating a relationship that supports the functioning of both the cash and derivatives markets).

[3] See Michael W. Brandt, Kenneth A. Kavajecz & Shane E. Underwood, Price Discovery in the Treasury Futures Market, 27 J. Futures Mkts. 1021 (2007) (finding that order flow in the Treasury futures market contributes significantly to price discovery and documenting information flows from the futures market to the cash market).

$1 trillion in notional terms.[4] The trade relies on repo financing for the cash leg, creating a chain of interconnection across cash, futures, and repo markets.

But this interaction between cash and futures markets can transform during periods of abnormal volatility into one that acts as a transmission channel for cross-market instability. During the March 2020 market stress, notably, Treasuries prices became dislocated as the repo and cash markets came under heavy stress. Highly leveraged hedge funds, having borrowed to pay for their long positions in the repo market, were forced to join the selling as they struggled to meet margin calls and to roll over their repo loans. With Treasuries prices see-sawing, this "dash-for-cash" came as an ill-timed shock, draining liquidity from the Treasury market when it was most needed.[5]

Second, the interest rate swap spread trade. Swap spread trades involve taking positions in cash Treasuries against offsetting positions in interest rate swaps, exploiting the differential between Treasury yields and swap rates. These trades have attracted scrutiny through several recent stress episodes. Notably, the Federal Reserve Bank of New York documented in May 2025 that the unwinding of swap spread trades contributed to the sharp spike in Treasury yields in April 2025, when ten-year yields rose approximately 60 basis points over just two days.[6] Like the basis trade, the swap spread trade creates tight linkages between derivatives and cash Treasury markets that can become transmission channels for stress if events result in creating rapidly shifting expectations about the relative direction of future rates.

However, the linkages between derivatives markets and U.S. Treasury markets go much deeper than these two strategies. Treasuries constitute the primary form of collateral across clearinghouses supporting both over-the-counter and exchange-traded derivatives. Central counterparties collect margin overwhelmingly in the form of Treasury securities. The repo markets through which leverage is extended and liquidity is managed depend on Treasuries as collateral.[7] Bank liquidity buffers under the Liquidity Coverage Ratio are denominated heavily in Treasuries. In a fundamental sense, the stability of derivatives markets depends on the stability of the Treasury market, and derivatives activity in turn affects Treasury market conditions. Preserving the value, stability, and liquidity of U.S. Treasuries is therefore a prime objective in which derivatives markets are both essential contributors to that liquidity and deeply dependent on it.[8]

II. Information Gaps: What We Do Not Know and Why It Matters

Despite the depth of these interdependencies, our knowledge of the risks at the intersection of derivatives and Treasury markets is surprisingly thin. There are structural reasons for this, rooted in how participants are regulated, how data is collected, and how institutions are organized. These information gaps are not incidental. They are the product of a regulatory architecture that was not designed for the degree of cash-

[4]See CFTC Commitments of Traders Reports; See also Daniel Barth et al, The Cross-Border Trail of the Treasury Basis Trade, FEDs Notes (Oct. 15, 2025) (noting undercounting of Cayman Island-based hedge fund exposures to Treasuries securities).

[5]See Daniel Barth & R. Jay Kahn, Hedge Funds and the Treasury Cash-Futures Basis Trade, 155 J. Monetary Econ. (2025) (documenting that basis traders consistently account for more than 60% of all hedge fund Treasury positions and 70% of all hedge fund repo, and estimating that hedge funds sold more than $200 billion of cash Treasuries during the March 2020 stress).

[6]See Roberto Perli, Recent Developments in Treasury Market Liquidity and Funding Conditions, Speech, Federal Reserve Bank of New York (May 9, 2025) (noting that analyses suggest the unwinding of swap spread trades contributed to the yield spike).

[7]For a detailed discussion, see generally, Yesha Yadav & Pradeep Yadav, The Failed Promise of Treasuries in Financial Regulation, 97 Southern California Law Review 1349 (2024). On the fragmented oversight structure across Treasuries and Treasuries-backed repo and its implications, see generally, Yesha Yadav, Failed Regulation of U.S. Treasury Markets, 121 Columbia Law Review 1173 (2021).

[8]See e.g., Bank for International Settlements, The Role of Margin Requirements and Haircuts in Procyclicality (CGFS Papers No. 36, Mar. 2010).

derivatives interconnection that now characterizes the Treasury ecosystem. I discuss several of the most consequential gaps below.

Hedge Fund Activity in the Cash Treasury Market. Hedge funds are among the largest and most active participants in U.S. Treasury markets. They are the major operators of the basis trade and the swap spread trade. But learning how they transact in real time has long proven a challenge. In 2017, FINRA expanded TRACE reporting to cover transactions in U.S. Treasury securities, with subsequent revisions in 2019.[9] However, these reporting obligations attach to FINRA-member broker-dealers, not to end-user, non-broker-dealer counterparties like hedge funds. When a hedge fund transacts in the cash Treasury market, the trade is captured only indirectly in real-time from the broker-dealer's side. The fund's overall position, trading strategy, and aggregate leverage remain largely invisible to regulators through TRACE. As I have also documented in prior research, the regulatory framework applicable to Treasury broker-dealers is significantly thinner than that governing equity broker-dealers.[10]

Repo Market Opacity. The repo market is where hedge funds finance the long leg of the basis trade, and where collateral chains and leverage multiply. Yet the bilateral repo market has historically offered regulators very little visibility. Primary dealers file weekly position reports with the Federal Reserve Bank of New York, but these are aggregate data, not transaction-level. The bilateral segment, where much non-cleared activity resides, has been a persistent source of regulatory concern especially since at least the September 2019 repo market seizure.[11] The Office of Financial Research adopted a rule in 2024 to introduce systematic data collection for non-centrally cleared bilateral repo,[12] but the implementation of this surveillance risks severe headwinds with the reduction of OFR's workforce, a point I return to below. Critically, when hedge funds' repo borrowing is intermediated by multiple dealers, no entity is aggregating the total repo-financed leverage of a given fund across all its counterparties. That the extent of the exposure is poorly understood became painfully apparent during the March 2020 basis trade unwind.

Interest Rate Swap Data. Interest rate swaps are reported to swap data repositories under the CFTC's regulatory framework.[13] This is a significant improvement over the pre-Dodd-Frank era. But there are important limitations. The quality and completeness of swap data have been a persistent challenge, and the CFTC has been working to improve data standards since 2017. More fundamentally, swaps data sits at the CFTC while cash Treasury position data resides with the SEC and FINRA (via TRACE) and with the Federal Reserve (via position reports). To reconstruct a swap spread trade and assess its risk, a regulator would need to see three things simultaneously: the cash Treasury position, the repo financing, and the interest rate swap. No single regulator currently sees all three.

III. Institutional Constraints on Oversight

These information gaps in the reporting of market activity are compounded by institutional constraints that limit regulators' ability to share and act on whatever data they do collect. These constraints are not new.

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[9] See FINRA Rule 6730 (Transaction Reporting). Under the 2017 amendments (effective July 2017) and subsequent 2019 revisions, TRACE reporting was expanded to cover transactions in U.S. Treasury securities. However, reporting obligations attach to FINRA member broker-dealers, not to end-user counterparties such as hedge funds.

[10] See Yadav, supra note 7, at 1222–1224 (documenting the relatively thin regulatory framework applicable to Treasury broker-dealers compared to equity broker-dealers).

[11] See Gara Afonso, Marco Cipriani, Adam Copeland, Anna Kovner, Gabriele La Spada, Antoine Martin, The Events of Mid-September 2019, Federal Reserve Bank of New York Staff Report 918 (March 2020).

[12] The OFR adopted the final rule for its Centrally Cleared and Bilateral Repo Data Collection (12 C.F.R. Part 1610) in 2024.

[13] See 17 C.F.R. Parts 43, 45, 49 (CFTC swap data reporting rules). For discussion of persistent data quality challenges, see CFTC Division of Market Oversight, Roadmap to Achieve High Quality Swaps Data (Jul. 2017).

They have a well-documented history in Treasury markets, where oversight is divided among at least five major federal bodies without a single lead regulator.

The Flash Rally of October 15, 2014, demonstrated the costs of this fragmentation vividly. During that episode, Treasury prices surged to some of their highest historic levels for no discernible reason, sending markets into chaos before reverting within minutes. Five federal regulators undertook a yearlong joint investigation. The resulting Joint Staff Report found no single cause, but the investigation itself was illuminating: the CFTC required time to conclude an information-sharing agreement before it could forward its data to other agencies, and regulators discovered they had been unaware of the extent to which high-frequency principal trading firms had come to dominate Treasury trading volumes.[14] That was more than a decade ago. The fact that the data-sharing infrastructure between the SEC and CFTC is still being formalized in 2026 tells us something about the pace of institutional reform relative to the pace of market evolution.

SEC-CFTC Information Sharing. Section 8(a) of the Commodity Exchange Act imposes confidentiality requirements on the CFTC with respect to business transactions, market positions, trade secrets, and customer information.[15] This underlying confidentiality regime means that cross-agency data sharing requires formal arrangements that can take time and institutional energy to establish.

In March 2026, SEC Chairman Atkins and CFTC Chairman Selig signed a Memorandum of Understanding on regulatory harmonization, which included commitments to share data regarding matters and transactions of common regulatory interest.[16] This is a welcome step. However, the MOU itself notes that the agencies must still "work expeditiously to enter into the necessary confidentiality arrangements" to enable direct data access. As of the MOU's signing, those arrangements had not been finalized. The MOU is an executive agreement, not a statutory solution, and its durability depends on the priorities of current agency leadership.

FSOC and the OFR. The Financial Stability Oversight Council and the Office of Financial Research were created by the Dodd-Frank Act precisely to address the kind of cross-market, cross-regulatory blind spots I have described.[17] The OFR was designed to collect and standardize data across regulatory boundaries and support FSOC's systemic risk monitoring function.

The OFR is currently being significantly reduced in capacity. Its workforce has been cut from 196 employees to approximately 100, with reported plans to reach a target of 70.[18] The data team, charged with processing and analyzing the bilateral repo data collection and other surveillance inputs, is facing

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[14]See U.S. Dep't of the Treasury et al., Joint Staff Report: The U.S. Treasury Market on October 15, 2014, at 4, 15–19 (July 13, 2015) (finding "no single cause" for the price volatility). As I have documented, the investigation revealed that the CFTC required time to conclude an information-sharing agreement before it could forward data to other regulators, and the report disclosed that regulators had been unaware of major structural transformations in the market, including the shift to high-speed automated trading. See Yadav, supra note 7, at 1195–1203; 1223-1225. It should be noted that the Interagency Working Group on Treasury Market Surveillance provides a coordinating forum across the system without acting as a regulator with authority to mandate how the different agencies oversee this market.

[15]Section 8a of the Commodity Exchange Act, 7 U.S.C. § 12, imposes confidentiality requirements on the CFTC with respect to business transactions, market positions, trade secrets, and names of customers. Sections 21(c)(7) and 21(d) of the CEA incorporate Section 8 in establishing the disclosure restrictions applicable to swap data repositories.

[16]SEC and CFTC, Memorandum of Understanding on Regulatory Harmonization (Mar. 11, 2026). The MOU establishes procedures for sharing data regarding matters and transactions of common regulatory interest and commits the agencies to entering into the confidentiality arrangements necessary to enable direct access to data from swap and security-based swap data repositories.

[17]See Dodd-Frank Wall Street Reform and Consumer Protection Act §§ 111 (establishing FSOC); Dodd-Frank Act §§ 152 (establishing the OFR).

[18]See Government Executive, A Federal Office Designed to Stave Off the Next Financial Crisis is Being Dismantled (Mar. 2026) (reporting that OFR's data team has been reduced to a few people and that the agency's headcount is being cut from 196 to approximately 70).

reductions. In June 2025, a group of more than fifty former Federal Reserve chairs, former government officials, and academics, including former Fed Chairs Ben Bernanke and Janet Yellen, wrote to Congress warning that defunding or seriously downsizing the OFR would be a mistake.[19] It is unclear at this point what role FSOC is prepared to play in providing an overarching data architecture for monitoring risks. Its ability to function as a coordinating body depends on having institutional infrastructure and data capacity and especially in light of the complex interconnections between the Treasury, Treasury-backed repo and related derivatives markets.

These institutional limitations mean that at the very moment when derivatives-Treasury interconnections are deepening, the infrastructure designed to monitor those interconnections is losing capacity. This is the backdrop against which the expansion of central clearing and cross-margining is taking place.

IV. Cross-Margining: An Important but Incomplete Step

One important recent development is the expansion of cross-margining between the CME and the Fixed Income Clearing Corporation. On April 15, 2026, the CFTC and the SEC jointly approved the extension of the existing cross-margining arrangement to cover customer positions, with a launch date of April 30, 2026.[20] This expansion allows customers of dually registered broker-dealer/futures commission merchants to achieve margin efficiencies of up to 80 percent on correlated cash Treasury and Treasury futures positions held at FICC and CME respectively.[21]

This is a significant and broadly welcomed development. Cross-margining can reduce the overall margin burden on market participants, improve capital efficiency, and reduce the costs of engaging in legitimate hedging activity. By recognizing the risk-reducing effects of correlated positions across cash and futures, it produces margin requirements that more accurately reflect the economic risk of a combined portfolio. It has been a long time coming: the original FICC-CME cross-margining arrangement for proprietary accounts dates to 2004, and the CFTC's Global Markets Advisory Committee formally recommended expansion to customers in February 2024.[22]

However, the journey to this expansion reveals something important about the state of our regulatory architecture. Achieving customer cross-margining required both the CFTC and the SEC to grant exemptive relief from their respective statutory frameworks. FICC is not a registered Derivatives Clearing Organization under the Commodity Exchange Act, so CFTC segregation rules would ordinarily prohibit futures customer funds from being held at FICC. The exemptive order carves out a limited exception to CFTC Regulations 1.20 and 1.49, permitting dually registered BD-FCMs to hold futures customer funds in a commingled account at FICC under specified conditions. Simultaneously, the SEC had to approve FICC establishing the novel "XM Customer Margin Account" structure. The fact that it took more than two years from the GMAC recommendation to an operational launch, and that achieving this result required ad hoc exemptions rather than a framework designed for this purpose, illustrates the coordination costs that the current multi-regulator structure imposes on even broadly supported reforms.

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[19] See Eliminating the OFR through H.R. 1 Would Undermine America's Capacity to Maintain a Stable Financial System, Letter, (June 16, 2025) (signed by, among others, former Fed Chairs Ben Bernanke and Janet Yellen, warning that defunding OFR would undermine America's capacity to maintain a stable financial system).

[20] See CFTC, Order Pursuant to Section 4(c) of the Commodity Exchange Act, 91 Fed. Reg. (Apr. 20, 2026); SEC, Exchange Act Release No. 34-105249 (Apr. 15, 2026) (on FICC rule changes for customer cross-margining).

[21] See CME Group, CME-FICC Cross-Margin Program, https://www.cmegroup.com/solutions/clearing/cme-ficc-cross-margin-program.html (noting that the program will expand to customer accounts on April 30, 2026).

[22] See CFTC, Global Markets Advisory Committee Advances Key Recommendations, Release No. 8860-24 (Feb. 8, 2024) (advancing the GMAC recommendation to expand customer cross-margining). The original FICC-CME cross-margining arrangement for proprietary accounts dates to 2004.

In addition, the arrangement has structural limitations. Participation is available only through dually registered BD-FCMs that are common members of both FICC and CME. Many market participants clear their Treasury positions through bank intermediaries at FICC. But banks are typically not FCMs. Those customers cannot currently access cross-margining because the bank on the FICC side and the FCM on the CME side are separate legal entities.[23] The arrangement can exclude a meaningful segment of the market.

I would also draw the Task Force's attention to the likely impact of cross-margining on market activity. The basis trade has been roughly flat at the $1 trillion level in notional terms since late 2023. By contrast, the broader interest rate derivatives market has experienced explosive growth. Overall OTC derivatives notional rose 16 percent to $846 trillion by mid-2025, the largest annual increase since 2008, and interest rate derivatives traded notional grew over 46 percent in 2025 alone.[24] Cross-margining changes the economics of the basis trade materially. With margin savings of up to 80 percent on correlated cash-futures positions, the cost of holding these positions drops dramatically. Research from the Chicago Fed highlights that market experts expect the basis trade to see a boost in demand, also increasing repo market activity.[25]

This growth carries significant implications. As the basis trade expands, its cash leg will increase activity in the repo market, where hedge funds finance their Treasury purchases. More repo activity from basis traders means more leverage flowing through a market segment where, as I have described, bilateral repo remains poorly monitored and the OFR's capacity to process its newly adopted data collection risks significant cuts. In other words, the margin efficiency improves, but the ability to monitor the activity benefiting from that efficiency does not improve in parallel.

It is also worth noting a potential divergence between the two major Treasury-linked derivatives strategies. Cross-margining specifically benefits the cash-futures basis trade because it is the combination of cash Treasuries at FICC and Treasury futures at CME that generates the margin offset. The interest rate swap spread trade, by contrast, does not benefit from this particular arrangement in the same way, because interest rate swaps clear through different infrastructure. During the April 2025 tariff-related volatility, this asymmetry was already apparent. The Federal Reserve Bank of Dallas documented that basis trade positions remained notably stable while swap spreads experienced surging volatility.[26] If cross-margining makes the basis trade relatively more attractive, we should expect growth in precisely the strategy that concentrates the most risk at the cash-repo-futures intersection, with all the information gap consequences that entails.

V. Central Clearing and the Circularity of Treasury Collateral

As the SEC's central clearing mandate for Treasury securities moves toward implementation clearinghouses are going to play an increasingly important role in U.S. Treasury markets.[27] Central clearing

[23]See GMAC Recommendation, FICC-CME Customer Position Cross-Margining Structure (Nov. 6, 2023), at 3–4 (noting that participation by customers clearing through bank intermediaries presents additional challenges in the context of cross-margining).

[24]See Bank for International Settlements, OTC Derivatives Statistics at End-June 2025 (Dec. 2025) (reporting that overall OTC derivatives notional rose 16% to $846 trillion, the largest year-on-year increase since 2008); see also ISDA, SwapsInfo Full Year 2025 Review (Feb. 2026) (reporting that IRD traded notional grew 46.1% to $536.5 trillion in 2025 from $367.1 trillion in 2024).

[25]See Ketan Patel, How the U.S. Treasury Futures Market and the Basis Trade Could Be Affected by the Treasury Clearing Mandate, Fed. Rsrv. Bank of Chi., Chicago Fed Letter No. 516 (2026); Ketan Patel, How the U.S. Treasury Futures Market and the Basis Trade Could Be Affected by the Treasury Clearing Mandate: Part 2—The Possible Role of Cross-Margining, Fed. Rsrv. Bank of Chi., Chicago Fed Letter No. 516 (Jan. 2026) (documenting that the basis trade has evolved into a cornerstone of Treasury market structure and noting that cross-margining arrangements meaningfully help encourage market activity).

[26]See Srini Ramaswamy et al., How Sensitive Is the Treasury Cash-Futures Basis Trade to Funding Condition Shifts?, Fed. Rsrv. Bank of Dallas (July 2025) (documenting that during the April 2025 tariff-related volatility, basis positions were notably stable while swap spreads experienced surging volatility and noting that the alignment of favorable conditions may not always persist).

[27]Yesha Yadav & Joshua Younger, Central Clearing the Treasury Market?, 92 University of Chicago Law Review 545 (2025). See also SEC, Securities Exchange Act Release No. 34-99149 (Dec. 13, 2023) (adopting Treasury clearing mandate).

offers meaningful benefits: multilateral netting, standardized risk management, default management procedures, and enhanced regulatory transparency. CCPs and their operators are making substantial and genuine efforts to provide rigorous risk management in this space.

Nevertheless, CCPs in the Treasury market face headwinds that deserve careful attention. The information gaps I have described create a particularly thorny challenge. CCPs calibrate their margin models and stress tests based on the data they can observe. But as I have outlined, the aggregate leverage of the hedge funds that are the most active participants in basis trades and swap spread trades is not fully visible to CCPs through existing reporting channels. The bilateral repo financing that supports these strategies is opaque. And when a client splits positions across multiple CCPs, as may become possible with the entry of multiple CCPs in the future into Treasury clearing, no single CCP will directly observe the client's total exposure. Margin models can end up calibrated against an incomplete picture of the risk landscape that may systematically struggle to map out correlated stress scenarios.

There is a further fundamental structural concern that I wish to highlight for the Task Force. U.S. Treasuries serve as the primary form of collateral that CCPs collect as margin from their clearing members and their members' clients. FICC's own liquidity resources, including the Capped Contingency Liquidity Facility, depend in significant part on the ability to monetize Treasury holdings through repo markets.[28] Default management frameworks essentially assume that Treasuries can be converted to cash on demand.[29]

This creates a potential circularity.[30] The scenarios in which a Treasury CCP is most likely to face a member default are precisely the scenarios in which Treasury markets are most likely to be under stress. A basis trade blowup, a swap spread trade unwind, a broader flight from risk. These are the kinds of events that would trigger margin calls, potential member failures, and CCP default management processes. In those scenarios, the Treasury securities that the CCP holds as a source of solvency and strength may be difficult to liquidate. The repo markets through which the CCLF operates may be impaired. The value of the collateral may be declining at the moment the CCP most needs to realize it. If Treasury market conditions deteriorate, clearinghouses must rely on Treasuries for their own survival. In a market where Treasuries themselves face a potential liquidity crisis, that risk management architecture faces a very difficult test.[31]

This circularity is made more dangerous by the information gaps I have described. If regulators and CCPs cannot observe the aggregate basis trade exposure, the aggregate repo leverage, or the cross-market positions of key participants, they will face serious hurdles in being able to adequately model the scenarios under which Treasury collateral becomes correlated and illiquid across the system simultaneously. The stress tests are only as good as the information and assumptions that drive them.

VI. Conclusion and Recommendations

Derivatives are essential to the functioning of U.S. Treasury markets. They provide price discovery, hedging, and liquidity. The expansion of cross-margining and the move toward central clearing represent

[28]The Capped Contingency Liquidity Facility (CCLF) requires FICC clearing members to commit to lending cash to FICC in the event of a liquidity shortfall. See FICC Government Securities Division Rulebook, Rule 22A. The CCLF's effectiveness depends on the willingness and ability of clearing members to provide liquidity in a stress scenario, precisely when they may be experiencing their own liquidity constraints.

[29] See Yadav & Younger, supra note 27, at 591-593.

[30]See Yadav & Younger, supra note 27, at 588-593(analyzing CCP risk management in the context of the Treasury clearing mandate, including the circularity of relying on Treasury collateral).

[31]See generally Yadav & Yadav, supra note 7 (analyzing U.S. Treasuries' role as the foundational collateral asset in the financial system and the implications of Treasury market stress for the broader financial architecture).

meaningful progress toward more efficient and resilient market infrastructure. I do not question the importance or the value of these developments.

What I urge this Task Force to consider is whether the informational and institutional infrastructure underpinning these developments is adequate for the systemic importance of the market they serve. At present, the answer is no. Hedge fund activity in the cash Treasury market, in the repo market, and in the interest rate swap market remains insufficiently transparent. The institutional capacity to monitor risks across regulatory boundaries is, in key parts, being diminished rather than strengthened. The agencies responsible for the two sides of the cash-derivatives divide are still building the data-sharing arrangements necessary for coordinated oversight. And the clearing infrastructure that is absorbing an increasing share of the Treasury market's systemic risk relies on the very asset whose stability it is designed to protect.

Getting this right depends on three things: (i) comprehensive informational collection that provides visibility into the activity of key market participants across cash, repo, futures, and swap markets; (ii) institutional capacity to analyze that information across regulatory boundaries; and (iii) the ability to translate that analysis into effective risk management by both public regulators and private market infrastructure. All three of these conditions are compromised by the gaps I have described.

I respectfully urge this Task Force to prioritize ensuring that the data infrastructure and institutional capacity supporting Treasury market oversight match the ambition of the clearing and cross-margining reforms now being implemented. The U.S. Treasury market is too important to the American economy and to global financial stability to operate with the informational blind spots that currently exist.

Thank you for this opportunity. I welcome any questions that Members may have.