



November 17, 2010

Mr. David Stawick  
Secretary  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21st Street, NW  
Washington, DC 20581

Via Electronic Mail

SUBJECT: RIN 3038-AD01

Dear Mr. Secretary:

The Minneapolis Grain Exchange, Inc. ("MGEX" or "Exchange") would like to thank the Commodity Futures Trading Commission ("CFTC" or "Commission") for this opportunity to respond to the Commission's request for comment on the above referenced matter published in the October 18, 2010 Federal Register Vol. 75, No. 200.

MGEX recognizes the value that the proposed CFTC rulemaking can provide certain sections of the commodities industry and its market participants, particularly the large swaps area which lacks sufficient regulatory oversight as well as those parties trading swaps. MGEX is both a Designated Contract Market ("DCM") and Derivatives Clearing Organization ("DCO") and, while MGEX does not currently trade or clear swaps, the Exchange will be impacted since the Commission is applying much of the proposed rulemaking to DCMs and DCOs not trading or clearing swaps. The proposed rulemaking covers all DCMs and DCOs under a single blanket, and the Commission has presented various arguments for doing so. However, MGEX would like to ensure that as a single legal entity that is both a DCM and DCO, the Commission's final rulemaking will account for such a combined structure and make clear that the rules for DCMs and DCOs do not overlap or have unintended interpretations in areas such as ownership control and voting which we will describe later.

### **Mitigation of Conflicts of Interest**

MGEX agrees with the Commission that mitigating conflicts of interest plays an important role in the proper functioning of DCMs and DCOs. MGEX applauds the efforts taken by the Commission and its staff and agrees with many but not all of the proposed rules to mitigate conflicts of interest. Please find below our comments and concerns.

## **Board of Director Requirements**

Independent public directors assist in mitigating structural conflicts of interest and provide unique insight that might not otherwise be represented by member directors. The proposed requirements require that the board of directors for DCMs, DCOs and Swap Execution Facilities (“SEFs”) be comprised of at least 35 percent public directors. As an additional layer to the 35 percent requirement, the Commission also proposed to require at least two independent directors be on the board. MGEX already exceeds both of these requirements and agrees with the Commission that the 35 percent minimum threshold for public directors on the board and executive committees operating with board powers strikes a fair balance between the need to mitigate conflicts of interest and the need for expertise and efficiency. The Commission asked for comments relating to whether 35 percent was high enough or whether the board should be 51 percent public or some percent in-between. One of the main factors driving the increased concern over conflicts of interest regarding public directors being on a DCM or DCO’s board revolves around swaps. The type of product traded or cleared should not be determinative as to percentage of public directors. Therefore, MGEX as a non-swap DCO/DCM, suggests the Commission consider the totality of the impact of the proposed rule and not focus solely on the issues arising from the swap area.

Regarding two substantive requirements proposed by the Commission, MGEX believes the proposed requirements could use clarification as to value and purpose. First, requiring annual performance reviews of a board of directors and its individual board members appears excessive and unnecessary. In our case, the board and its members are already accountable to its members and owners and for ensuring the Exchange is complying with Commission requirements. The Regulatory Oversight Committee was established to monitor the latter. Furthermore, term limits already provide as good, if not better, means for removing directors who are not performing in the best interest of shareholders. In addition, what does the Commission foresee doing with the annual reviews – is it for shareholders, the Commission or someone else? Shareholders, owners and others may well request disclosure of such reviews which will have a tendency to impede debate on controversial topics, or even move to the other extreme where board members will conduct exhaustive debate in order to ensure they can be given a good grade. Worse yet, highly qualified board candidates may choose to avoid the scrutiny of the proposed requirements which could lead to a less qualified and effective board. MGEX is not convinced that an annual performance review’s benefit will outweigh the cost of conducting the review since the voting shareholders have no obligation to utilize the review. As a last point, publicly traded exchanges might be served better by this requirement than a nonpublicly traded and mutually owned exchange.

MGEX notes that the Commission states “each member of a DCO, DCM, or SEF Board of Directors have sufficient expertise, where applicable, in financial services, risk management, and clearing services.” Every entity naturally seeks such qualified individuals. However, the Commission also stated its desire to “balance between (i) the need to minimize conflict of interest in DCM decision-making processes with (ii) the need for expertise and efficiency in such processes.” It seems that the Commission’s

statement regarding balancing will be the most practical and feasible guidepost to use. The former standard seems too subjective without employing guidelines to provide clarity. Further, MGEX cannot guarantee the election of member directors, even if a Nominations Committee vets a candidate's qualifications.

### **Committee Public Director Requirements**

MGEX agrees with the Commission that public directors help ensure a high level of integrity to many committees. MGEX also agrees that DCMs and DCOs should generally adhere to the same public director requirements. However, the Exchange requests that the Commission consider the impact of its public director requirements for single legal entities that are both a DCM and DCO.

For example, consider an eleven-member board of directors of a combined DCM/DCO entity. At least four of the members must qualify as public directors. The four also serve on a number of internal committees such as executive, finance and personnel. Based on the proposed requirements for the nominating, risk management, membership and regulatory oversight committees as well as for disciplinary panels, the Commission's proposals will require the four public directors to sit on perhaps ten committee seats or more. That is in addition to their normal board obligations. These steep additional time demands may function as a large disincentive for potential quality public members to join a board as they may well be spending more time on non-governing matters. MGEX understands the need for all serving directors to be fully engaged but also knows there are other non-exchange related issues and duties that most board members must contend with outside of their director duties. In essence, the proposed requirements further spread thin the ability of the public directors to effectively serve on each committee and also inhibit the DCO/DCM from efficiently using the expertise of its public directors' qualifications. As an alternative, the Exchange proposes that the Commission promulgate suggested guidelines for public directors serving on committees as opposed to hard-number requirements of public directors serving on committees.

### **Specific Committee Requirements: Nominating Committee**

Notwithstanding the forgoing, MGEX currently has a nominating committee and agrees with the Commission that public directors are valuable asset to help ensure the process of electing directors maintains a high level of independence and integrity.

If the nominating committee should function as a gatekeeper instead of an overseer, it would be beneficial to DCOs, DCMs, and SEFs for the Commission to perhaps provide safe harbor provisions as to who are those "individuals qualified to serve" on the board. As previously stated, this is a natural goal that any nominating committee attempts to do. However, limiting who members or owners can vote for may open the DCO, DCM or SEF to claims of discrimination or other legal claims. Therefore, the Exchange believes the Commission's proposal is not necessary. Regardless, it is best to allow DCOs, DCMs, and SEFs to determine how they wish to set standards or encourage qualified individuals to serve.

### **Specific Committee Requirements: Risk Management Committee**

Regarding the risk management committee, MGEX finds it interesting that the Commission proposes to require a non-swap DCO to have 10 percent of the committee be composed of “customers of clearing members, who also routinely execute swap contracts (as well as commodity futures and options).” Having risk management committee members who have experience with pricing models is reasonable; however, the clear focus on swaps indicates that the requirements being promulgated should not necessarily be applied universally to DCOs not clearing swaps. The Commission seems to put commodity futures and options as an afterthought, parenthetically speaking. Considering the difference between swaps and commodity futures, it does not necessarily make sense to put all DCOs under one umbrella. MGEX respectfully requests that the Commission instead consider the issues that swap activity represents and not consistently lump such products with commodity futures and options. MGEX respectfully suggests that the Commission consider having the 10 percent of the risk management committee consist of expertise in the type of business that the DCO primarily does. In the alternative, if the Commission is particularly concerned with swaps, then if the DCO’s business consists of say, 25 percent or more of swaps, then that 10 percent of the risk management committee should have expertise in swaps.

### **Voting Rights and Ownership**

The Commission proposes two alternatives for DCOs to limit ownership and voting rights. The first alternative limits single-member ownership of voting equity to 20 percent and an aggregate limit for enumerated entities to 40 percent. The second alternative proposes a 5 percent limit on the voting equity that any DCO member or enumerated entity may own. Remember, MGEX is both a single entity DCM/DCO and already limits ownership and voting rights to 20 percent of the Exchange’s outstanding membership. Requiring an entity that is both a DCM and DCO to comply with the higher DCO standards is discriminatory to us as a DCM. Therefore, this DCO requirement should not apply to DCMs that are also DCOs, and also not trading or clearing swaps.

The Exchange thanks the Commission for the opportunity to comment on the notice of proposed rulemaking. If there are any questions regarding these comments, please contact me at (612) 321-7169 or lcarlson@mgex.com. Thank you for your attention to this matter.

Regards,



Layne G. Carlson  
Corporate Secretary

cc: Mark G. Bagan, CEO, MGEX  
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