



Bloomberg L.P.

731 Lexington Avenue  
New York, NY 10022Tel +1 212 318 2000  
bloomberg.com

November 17, 2010

Mr. David A. Stawick  
Secretary  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21<sup>st</sup> Street, N.W.  
Washington, DC 20581

Re: Requirements for Derivatives Clearing Organizations, Designated Contract Markets, and Swap Execution Facilities Regarding Mitigation of Conflicts of Interest (RIN 3038-AD01)

Dear Mr. Stawick:

Bloomberg LP appreciates the opportunity to provide the Commodity Futures Trading Commission ("CFTC") with our comments regarding proposed rules to mitigate conflicts of interest in the operation of a Swap Execution Facility ("SEF") under Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Act").

Section 726 of the Act requires the CFTC to adopt rules to mitigate conflicts of interest with regards to swap market facilities including SEFs.<sup>1</sup> Bloomberg is one of the largest, privately-held independent platforms for electronic trading and processing of OTC derivatives. Bloomberg intends to register as a SEF in order to facilitate trading in the swap markets.

I. Conflicts of Interest in Market Facilities

Section 726 of the Act requires the CFTC to promulgate rules regarding conflicts that may arise in the operation of SEFs. In particular, Section 726 (a) requires the adoption of rules that may, but are not required to, include numerical limits on the control or voting rights with respect to SEFs by enumerated entities.<sup>2</sup> Section 726 (b) mandates the CFTC to determine the manner in which its rules may be deemed necessary or appropriate to improve governance, or to mitigate systemic risk, promote competition, or mitigate conflicts of interest in connection with the interaction between swap dealers and major swap participants on the one hand and SEFs on the other. Finally, Section 726 (c) requires the

---

<sup>1</sup> The CFTC proposal also addresses mitigating conflicts of interest associated with Derivatives Clearing Organizations ("DCO") and Designated Contract Markets ("DCM")(collectively "market facilities").

<sup>2</sup> The enumerated entities are bank holding companies with \$50 billion or more in total consolidated assets, a nonbank financial company supervised by the Board of Governors of the Federal Reserve System, an affiliate of such bank holding company or nonbank financial company, a swap dealer or a major swap participant.

# Bloomberg

CFTC to consider the manner in which its rules address conflicts of interest arising from SEF equity ownership, voting structure, or other governance arrangements.

The focus of Section 726 is to address conflicts of interest arising from control of market facilities, including SEFs, by OTC derivative market participants such as swap dealers, major swap participants and bank holding companies. Specifically, the concern is that these enumerated entities may have economic incentives inconsistent with the public policy objectives of the Act and their ownership in market facilities may exacerbate structural conflicts of interest.

## II. Conflicts of Interest and Governance Proposals

The CFTC proposes to mitigate potential conflicts of interest through ownership limits and structural governance requirements. The proposal includes ownership or voting interest limitations by SEF members.<sup>3</sup> The structural governance proposal requires that a SEF Board of Directors be composed of 35% public directors.<sup>4</sup> In addition, the SEF must establish governance committees including a Nominating Committee to administer the process of nominating individuals as public directors of the Board<sup>5</sup>, a Membership or Participation Committee to insure fair access to the SEF by market participants<sup>6</sup>, and a Regulatory Oversight Committee ("ROC") to oversee the SEF regulatory program.<sup>7</sup>

Bloomberg supports efforts to address potential conflicts of interest that arise when market participants have ownership interest in a SEF. We believe, however, that the conflicts of interest rules must be appropriately designed and applied. The proposed rules should recognize that there may be circumstances where imposition of rigid governance requirements may not be appropriate for certain SEFs. Imposition of rigid conflicts of interest protections where there is little if any prospect for a conflict of interest is not good public policy. The primary rationale for ownership and governance requirements stems from a concern about conflicts that may arise from SEFs owned by market participants. Where a SEF is not owned by its members or other market participants and where the SEF can demonstrate that its relevant facts diminish or eliminate the risk of a conflict of interest, the CFTC should allow a waiver procedure to alleviate the obligation to conform with any of the proposed governance requirements, just as the CFTC proposes with regards to DCO ownership limits and voting rights and contemplates with respect to DCMs and SEFs.<sup>8</sup>

---

<sup>3</sup> The CFTC proposal essentially imposes a restriction on a SEF member from individually owning or voting more than 20% of any class of equity in the SEF.

<sup>4</sup> The CFTC proposal requires no fewer than two public directors. The CFTC's term "public director" essentially excludes individuals as qualifying as a public director if they have a material relationship with the SEF or its members.

<sup>5</sup> Under the CFTC proposal a Nominating Committee must have at least a 51% majority of public directors and the chairman must be a public director.

<sup>6</sup> Under the CFTC proposal the Membership or Participation Committee must be composed of 35% public directors.

<sup>7</sup> Under the CFTC proposal the ROC must be composed entirely of public directors.

<sup>8</sup> Requirements for Derivatives Clearing Organizations, Designated Contract Markets, and Swap Execution Facilities Regarding the Mitigation of Conflicts of Interest, 75 Fed. Reg. 63732 at 63744 (Oct. 18, 2010).

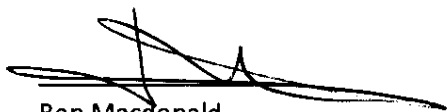
# Bloomberg

A waiver procedure that applies to any provision of the proposed conflicts of interest rule would provide flexibility for a SEF to request that governance requirements be waived if the CFTC determined that the requirements were not necessary or appropriate to mitigate conflicts of interest either because under the circumstances presented the prospect for the conflict of interest did not exist or was unlikely to occur, or the SEF's organization and other attendant mechanisms sufficiently mitigated risk of the conflicts of interest. As part of the registration process a SEF would be provided the opportunity to submit facts and circumstances which may demonstrate to the CFTC's satisfaction that a rigid governance structure is not necessary or appropriate, including information regarding a SEF's ownership structure, its fee structure, and the means by which it seeks to fulfill its regulatory responsibilities including the use of an independent utility to meet its self-regulatory organization obligations.<sup>9</sup> The waiver should apply to any provision of the governance requirements including the ROC requirement where we believe such a requirement is unnecessarily redundant in light of the requirement to have a Chief Compliance Officer ("CCO") who reports directly to the SEF Board.<sup>10</sup> As with the ownership limit waiver suggested in the instant proposed rule, the CFTC would be able to revoke the waiver at any time if subsequent events or circumstances warranted such action; in such case, the CFTC could require a SEF to institute the requisite governance structure upon the CFTC's order.

We think the CFTC appropriately identifies the key variables in identifying conflicts of interest and generally proposes appropriate measures to improve the governance of SEFs. We respectfully submit, however, that the rule proposals should include a degree of flexibility and discretion in imposing governance requirements on SEFs depending on their ownership structure and other relevant facts and circumstances so that any conflicts of interest requirements are applied meaningfully and appropriately.

We appreciate the opportunity to provide our comments on the proposed rules, and would be pleased to discuss any questions that the CFTC may have with respect to this letter.

Very Truly Yours,



Ben Macdonald  
Global Head Fixed Income  
Bloomberg LP

---

<sup>9</sup> A utility with direct authority to enforce compliance with SEF rules and monitoring of trade and trade processing would provide a level of independence oversight consistent with a self-regulatory organization. See Comment Letter from the National Futures Association to the CFTC dated August 31, 2010, with respect to SEF Registration Requirements and Core Principle Rulemaking.

<sup>10</sup> The CFTC requested specific comment as to whether it is necessary for a SEF to establish a ROC consisting of public directors where the Act requires a SEF to have a CCO that reports directly to the SEF Board. We believe a CCO who responsibly undertakes the duties impressed on that officer by the Act and who reports to the SEF Board is fully adequate protection against any relevant conflicts of interest concerns.