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Goldman Sachs

November 18, 2010

David A. Stawick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

Elizabeth M. Murphy
Secretary of the Commission
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

Re: Proposed Ownership Limitations and Governance Requirements for Clearinghouses, Execution Facilities and Trading Platforms (CFTC RIN 3028-AD01, SEC File No. S7-27-10)

Dear Mr. Stawick and Ms. Murphy:

Goldman, Sachs & Co. ("Goldman Sachs")[1] appreciates the opportunity to provide comments to the Commodity Futures Trading Commission (the "CFTC") and the Securities and Exchange Commission (the "SEC" and, together with the CFTC, the "Commissions") on the proposed rules[2] (each a "Proposal" and together, the "Proposals")

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[2] Requirements for Derivatives Clearing Organizations, Designated Contract Markets, and Swap Execution Facilities Regarding the Mitigation of Conflicts of Interest, 75 Fed. Reg. 63732 (proposed October 18, 2010) (to be codified at 17 CFR pts. 1, 37, 38, 39 and 40); Ownership Limitations and Governance Requirements for Security-Based Swap Clearing Agencies, Security-Based Swap Execution Facilities, and National Securities Exchanges With Respect to Security-Based Swaps Under Regulation MC, 75 Fed. Reg. 65882 (proposed October 26, 2010) (to be codified at 17 CFR pt. 242).

to mitigate conflicts of interest in the operation of derivatives clearing organizations ("DCOs") and clearing agencies ("SBSCAs").

The Proposals implement Sections 726 and 765 of the Dodd-Frank Wall Street Reform and Customer Protection Act ("Dodd-Frank") by, among other things, imposing requirements with respect to the composition of the boards of directors of DCOs and SBSCAs and committees of such boards and by limiting the ownership interests in DCOs and SBSCAs that may be held by member firms.

We are concerned that the rules contained in the Proposals regarding the composition of DCO and SBSCA Risk Management Committees would undermine the ability of the Commissions to achieve the systemic risk reduction objectives of Dodd-Frank.[3] Further, we do not believe that potential conflicts of interests necessitate the imposition of limits on the ownership of DCOs and SBSCAs by member firms. However, to the extent that such limitations are imposed, we support the approach set forth in the Proposals which allows DCOs and SBSCAs to choose an alternative that does not involve an aggregate ownership cap across members so that DCOs and SBSCAs have the ability to pursue the model that has been effective in supporting the Dodd-Frank's risk reduction objectives—the utility model.

I. Requirements on Board and Board Committee Composition

The Proposals contain requirements with respect to the composition of the boards of directors and board committees of DCOs and SBSCAs. The CFTC's Proposal requires that the board of directors of each DCO establish a Risk Management Committee that would be composed of at least 35% "public directors"[4] and at least 10% representatives of "customers". The SEC's Proposal does not mandate that the boards of directors of SBSCAs establish Risk Management Committees but imposes composition requirements to the extent that such a committee is established and has the authority to act on behalf of the board. The SEC Proposal requires either at least 35% or a majority of the board committee to be "independent directors" depending on whether the first or second alternative ownership restriction (as described under the caption "II Restrictions on the Ownership of DCOs and SBSCAs" below) is in effect.

We support a requirement for the boards of clearinghouses to maintain Risk Management Committees. In addition to other responsibilities, Risk Management Committees should be responsible for determining product and member eligibility and the level of margin requirements for cleared products. In light of the central role that is to be assumed by DCOs and SBSCAs under Dodd-Frank, ensuring that members of Risk Management Committees are qualified to make the correct judgments with regard to these critical matters is essential not only to the safety and soundness of the clearinghouses themselves but also to the broader financial system as a whole.

[3] Each of the Proposals notes that the Title VII provisions of Dodd-Frank were enacted to reduce risk and promote the integrity of the financial system and that a primary means of achieving this is by mandating that clearable swaps be cleared.

[4] The terms "public director" and "independent director" (which are referred to herein as "public director") are both defined with reference to the independence of the relevant individual from clearing member firms.

We believe that the individuals most qualified to make these judgments are those who have significant expertise in swaps and who are motivated by appropriate incentives. In our view, individuals associated with member firms satisfy both of these criteria. These individuals have current experience in the swaps markets which provides them with an understanding of the characteristics, pricing and market dynamics of swaps. In addition, because the capital of member firms is at risk in the event of a default at the clearinghouse, representatives of such firms have a significant incentive to ensure that the risk management decisions are prudent and appropriate.

Clearing swaps is different than clearing listed futures. There are significantly more distinct swaps than listed futures contracts. In comparison to listed futures contracts, swaps generally involve a higher level of customization either to achieve hedging objectives of parties or to reflect factors relevant to particular swaps. The number of swaps and tendency for certain swaps to be more customized requires clearinghouses to develop sophisticated and rigorous practices with respect to the clearing of swaps.

We believe that it would be quite challenging to populate the Risk Management Committees of DCOs and SBSCAs with a significant number of individuals who both qualify as public directors or customer representatives and have the necessary expertise.[5] We do believe that there is a benefit in having public directors and customer representatives participate on Risk Management Committees to ensure that a range of perspectives are considered in the deliberations of such committees. However, we believe that requiring significant representation of such individuals on a Risk Management Committee would cause it to be less effective in performing its function.

Finally, we believe that the potential conflicts that the Proposals seek to mitigate are overstated. The Proposals describe the possibility that clearing member firms that are active market participants in the swaps market will seek to prevent such swaps from being cleared as a means of preserving the profitability of bilateral trading. We expect that the clearing of swaps will increase the number of market participants that actively trade such products, thereby increasing the volumes and liquidity of swaps markets. Moreover, we believe that, because Dodd-Frank requires higher capital charges on non-cleared swaps than on cleared swaps, there are natural incentives for market participants to promote clearing.

Recommendations

We recommend that the Proposals with respect to the composition of Risk Management Committees be revised to emphasize the expertise of candidates over their independence from clearing firms as follows:

[5] In this regard, we note that the Proposals call for public directors not only at DCOs and SBSCAs but also at swap execution facilities and security-based swap execution facilities, which we further strain the limited pool of qualified candidates.

- Reduce the minimum requirements for representation of public director and customer representative participation from 35% (or a majority, as applicable) and 10%, respectively, to one of each.

- Broaden the definition of public director, by, at a minimum, shortening or eliminating the look-back period and allowing former employees of financial institutions to serve in this capacity.

- Require that all candidates be nominated and approved by the Nominating Committee of the board based on defined standards of experience and be subject to confirmation by the full board of directors.

In addition to the foregoing, we recommend that the Commissions require enhanced supervision of Risk Management Committees. Specifically, we suggest that DCOs and SBSCAs be required to create and implement detailed risk standards that are subject to the oversight of the relevant Commission. In addition, each DCO and SBSCA should be required to provide the relevant Commission with notice of any Risk Management Committee decision that is vetoed by, or the subject of a dispute with, the organization's board of directors. We believe that these controls will likely address any remaining concerns with respect to the composition of the Risk Management Committee.

II. Restrictions on the Ownership of DCOs and SBSCAs

The Proposals would require DCOs and SBSCAs to choose between one of two alternative structures for the ownership of voting equity in, or the exercise of voting power over, the entity. The first alternative would impose an individual ownership cap of 20% on each member firm (and its related persons) and a 40% aggregate ownership cap. In the SEC Proposal, the aggregate ownership cap applies across all members (and their related persons). In the CFTC Proposal, the aggregate ownership cap applies across all "enumerated entities" and their related persons. The second alternative would impose an individual ownership cap of 5% on each member firm (and its related persons) but no aggregate cap.

We do not believe the potential conflicts described in the Proposals necessitate the imposition of ownership limitations. However, to the extent that such limitations are imposed, we support the approach taken by the Commissions that allows DCOs and SBSCAs to choose an alternative that would not involve aggregate caps across all members/enumerated entities. We believe that having a cap on ownership that would apply on an aggregate basis would be inconsistent with the ownership structure of the types of clearinghouses that have been very effective in addressing risk management considerations—namely, utility-model based clearinghouses.

In our experience, utility-model clearinghouses are generally characterized by the following: a broad ownership structure among members; initial funding by member firms; tiered pricing based on volume discounts; practice of allocating revenue above operating costs to members in the form of rebates, fee discounts or dividends; and open access architecture to execution platforms, trade repositories and other clearinghouses.

This model is desirable for clearinghouses insofar as it emphasizes risk mitigation above return on invested capital. We note that this model has been favored by a number of clearing organizations, including The Depository Trust & Clearing Corporation and LCH.Clearnet, both of which were very effective in their management of the Lehman Brothers bankruptcy.

In addition, we believe that DCOs and SBSCAs that are based on the utility model are more likely to promote innovation by maximizing the number and range of products introduced for clearing, thereby advancing key objectives of Dodd-Frank. The utility model, in which a greater number of members bear the risks presented by the DCO's or SBSCA's clearing activities, also provides the appropriate incentives for members to commit necessary resources to create a stable, liquid market to manage those risks.

III. Conclusion

We believe that with the modifications described above, the Proposals will satisfy the Commissions' goal of mitigating conflicts of interest while reducing systemic risk, fostering the development of cleared markets and improving the governance of DCOs and SBSCAs. We would be pleased to provide the Commissions with any additional information in relation to the Proposals.

Sincerely,

John S. Willian
Managing Director
Goldman, Sachs & Co.