SEQUOIA

May 10, 2022

Submitted electronically via CFTC.gov

Mr. Christopher Kirkpatrick, Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, DC 20581

Re: Comments Responding to Commission Publication of FTX's Request for Amended DCO Registration Order

Dear Mr. Kirkpatrick:

We, the partners of Sequoia Capital, are responding to the CFTC's request for comment on FTX US Derivatives' Request for Amended DCO Registration Order submitted February 8, 2022.

Sequoia Capital ("Sequoia") is a nearly 50-year old venture capital firm, known for its investments in companies including 23&Me, Airbnb, Apple, Cisco, DoorDash, Google, Instagram, NVIDIA, Oracle, SpaceX, WhatsApp, YouTube, Zoom, and more. While we are known for our work in technology broadly, we have had decades of experience working with financial technology companies, including Block (formerly Square), Citadel Securities, Kalshi (a CFTC-regulated events platform), Klarna, Nubank, PayPal, Robinhood, Stripe, and more.

Sequoia Capital has been an investor in FTX International and FTX US since August 2021. Sequoia invested in FTX due to our conviction in Sam Bankman-Fried, co-founder and CEO of FTX, and the FTX team, but also because we saw an opportunity for a new entrant in the derivatives market to change it for the better. Given our experience partnering with companies across the financial system for decades, we've seen the value created for businesses and consumers by companies that disrupt the status quo to offer fundamentally better, more efficient services. We see in FTX the opportunity for a new entrant in the derivatives market to (1) increase competition among incumbent exchanges and banks that will ultimately benefit retail and institutional investors, (2) increase access to investment products for a wider range of investors while ensuring appropriate protections, and (3) improve risk management for investors and regulators by offering 24/7/365 financial markets for a 24/7/365 world. We discuss each of these features below.

1. <u>FTX's direct clearing model will increase competition for clearing services and promote more efficient markets</u>. Other than derivative clearing organizations (DCOs) with limited authority to clear fully collateralized transactions, there are only six active registered DCOs; and even among those, the vast majority of market volume is concentrated in the top two. Among exchanges, US trading volumes of cryptocurrency derivatives (specifically Bitcoin and Ethereum futures) are heavily concentrated in the CME, reflecting little meaningful competition on cryptocurrency or other derivatives. In addition, the existing clearing model means that futures commission merchants (FCMs) – typically banks and bank affiliates – are required to have intermediate access to clearing, and FCM activity has also been increasingly concentrated in a smaller number of large institutions. FTX's direct-to-investor model represents a source of healthy competition for this existing structure. FCMs have substantial documentation and operational costs, costs of capital, and other expenses associated with intermediation and margining arrangements with end users – and these costs are borne indirectly by FCM customers. Direct access on the FTX model makes transaction and clearing available for specific products in a targeted, efficient manner – efficient enough even to enable access through a mobile app for consumers. At the same time, FTX's model is not exclusive – end users who wish to rely on FCM intermediation can clear through an FCM not only through other DCOs, but within FTX itself. End users' ability to choose between competing modes of access is a key to making market structures responsive to competition and to increasing overall efficiency.

2. <u>FTX's direct clearing model will create broader, more equitable access to financial products, with investor protections</u>. A consequence of the additional costs associated with an FCM intermediated-only clearing model is a limitation on the range of prospective market participants who have a meaningful ability to transact in the market for cleared derivative products. There is a wide range of end users who would seek to participate in the exchange-traded derivatives markets but may effectively be denied access because they are interested in limited individual transaction volumes, or only in specific cryptocurrency or other derivative products. An FCM will tend to incur the documentation, credit analysis and other costs of a customer clearing relationship only for institutional, higher net worth and higher volume traders. FTX's direct, more efficient clearing model affords the prospect of broadening customer access, with attendant beneficial effects on overall market liquidity, price discovery and fairness.

3. <u>FTX's margining methodology will improve risk management by offering 24/7/365 markets for a 24/7/365 world</u>. Traditional FCM-intermediated clearing involves margin calls from the relevant DCO to the FCM responsible for customer positions during the business day, and an overnight demand by the FCM to the customer for margin to be transferred on the next business day. But values of cryptocurrency or other derivative products move in a continuous, globally integrated information environment that cannot be tied to trading hours or

business days. FTX’s margining model accordingly will begin to unwind an undermargined customer position immediately, in a manner that will create real-time market feedback on pricing and valuation from FTX’s central limit order book and from FTX’s committed liquidity providers. FTX’s model represents a modern, efficient approach to margining cleared positions that is manifestly more compatible with emerging technologies in digital payment and transfer systems, as well as with a global derivatives market. At a minimum – again, with the goal of promoting healthy competition between models – the CFTC should encourage a comparison between customer access and experience with margining on the FCM overnight credit model, and the faster, more market-disciplined approach under the FTX model.

Sequoia encourages the CFTC to foster innovation, competition and superior customer access by granting the amendment sought by FTX.

Sincerely,

Partners of Sequoia Capital