May 13, 2024

Via electronic submission to CFTC comments portal

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

Re: Requirements for Designated Contract Markets and Swap Execution Facilities Regarding Governance and the Mitigation of Conflicts of Interest (RIN 3038–AF29)

Dear Mr. Kirkpatrick,

The Wholesale Markets Brokers' Association, Americas ("WMBAA")[1] appreciates the opportunity to comment on the U.S. Commodity Futures Trading Commission ("Commission" or the "CFTC") staff notice of proposed rulemaking ("NPRM") on proposed requirements for Designated Contract Markets ("DCMs") and Swap Execution Facilities ("SEFs") regarding governance and the mitigation of conflicts of interest (the "Proposed Rule" or the "Proposal").[2]

The WMBAA supports the Commission's objective that DCMs and SEFs have robust and effective compliance programs that promote a regulated, competitive, and liquid swaps market. As interdealer brokers and operators of global trading venues for financial instruments, including swap execution facilities ("SEFs"), WMBAA members have a significant interest in the Proposed Rule and any possible rulemakings that would govern the operations and activities of SEFs. In

[1] The WMBAA is an independent industry body representing the largest inter-dealer brokers. The members of the group—BGC Partners, GFI Group, Tradition, and TP ICAP— operate globally, including in the North American wholesale markets, in a broad range of financial products, and have received registration as swap execution facilities. The WMBAA membership collectively employs approximately 4,000 people in the United States; in New York City, Stamford and Norwalk, Connecticut; Chicago, Illinois; Jersey City and Piscataway, New Jersey; Raleigh, North Carolina; Miami and Juno Beach, Florida; Burlington, Massachusetts; and Dallas, Houston and Sugar Land, Texas. Our members and their employees arrange trades that enable sophisticated market participants to manage their commercial and market risk.

[2] Requirements for Designated Contract Markets and Swap Execution Facilities Regarding Governance and the Mitigation of Conflicts of Interest Impacting Market Regulation Functions, 89 Fed. Reg. 19646 (March 19, 2024).

consideration of this experience, the WMBAA offers the following comments on the Proposed Rule.[3]

I. General Comments

As the WMBAA is comprised of multiple operators of SEFs, we support the Proposed Rule's goal to safeguard the integrity of the decision-making process of SEFs and DCMs and reduce conflicts of interest. As a general matter, we also support the Proposed Rule as it broadly reflects and codifies existing practices and processes adopted by registered SEFs in alignment with the SEF Core Principles[4] and as a result of staff guidance. The WMBAA believes that the Proposed Rule would largely codify existing best practices and result in a more consistent and predictable approach to compliance among SEFs.

However, the WMBAA is concerned that the Proposal is overly prescriptive in its attempt to codify existing guidance as rules, resulting in certain highly technical and excessively burdensome requirements. Several of the proposed requirements would be impracticable or realistically impossible to implement, and in turn will make it much more challenging for SEFs to operate in a manner consistent with the Commodity Exchange Act's ("CEA") principles-based regime.

Further, these aspects of the Proposed Rule, if adopted, would represent a significant departure from the CEA's principles-based regime, which has functioned effectively for SEFs for over a decade. The WMBAA believes it is critical to the liquidity and stability of the swaps market to ensure that self-regulatory organizations ("SROs") such as SEFs retain adequate flexibility to maintain and enforce their rules pursuant to the principles-based approach set forth in the CEA and the existing SEF Core Principles. For example, Core Principle 12 requires a SEF to "establish and enforce rules to minimize conflicts of interest in its decision-making process; and establish a process for resolving the conflicts of interest."[5] For many years, SEFs have effectively implemented such rules and processes, pursuant to oversight and feedback of CFTC staff, as well as under the careful review of the SEF chief compliance officer ("CCO") and, as a practical matter, SEF's Board's Regulatory Oversight Committees ("ROCs"), which include or are exclusively made up of non-affiliated public directors who assesses the SEF's compliance program, including conflicts of interest on an annual basis. Adopting the Proposed Rule as drafted will impose significant rigidity and uniformity on SEFs, rather than encouraging properly controlled

[3] The WMBAA is responding to the CFTC's request for comment from the perspective of operators of multiple SEFs only. To the extent our comments may also be responsive to similar or exact proposed rules or language impacting DCMs, WMBAA does not offer direct commentary.

[4] *See* Section 5h of the Commodity Exchange Act, 7 U.S.C. 7b-3, and Part 37 of the CFTC's regulations.

[5] 17 C.F.R. § 37.1200.

innovation and competition, and require departure from long-standing market practices that do not pose systemic risk.

The WMBAA observes that in addition to the guidance set forth in the Core Principles, the CFTC Division of Market Oversight's Compliance Branch conducts regular reviews of each SEF's ongoing compliance with Core Principles and the implementing regulations under Part 37 through rule enforcement reviews. This process allows the Commission to regularly examine the self-regulatory programs operated by the SEFs to, among other things, enforce its rules, prevent market manipulation and customer and market abuses, and ensure the recording and safe storage of trade information. The WMBAA believes the current rule enforcement review process allows the CFTC to ensure SEFs are adequately meeting the guidance requirements set forth in the SEF Core Principles while providing flexibility to each SEF to conduct its self-regulatory functions in a manner that meets the needs of the markets in which it operates and the products and customers relevant to such markets.

The WMBAA urges the CFTC to reconsider some of the components of the Proposed Rule that are not supported by an articulated need for the introduction of new, complicated rules, particularly those with quantifiable metrics. Alternatively, the WMBAA requests the CFTC simplify the Proposed Rule to more closely reflect the Commission's longstanding principles-based approach in alignment with the statutory framework of the CEA, to ensure SEFs can continue to establish and enforce rules that are appropriate for the markets in which we operate and the market participants we serve, and to ensure that such rules do not pose an undue burden on SEFs.

II. Specific Comments to Proposed Changes and Commission Questions

To further elucidate on the WMBAA's position described above, we offer the following specific comments and responses to the Commission's questions posed in the NPRM.

A. Minimum Fitness Standards – Proposed § 37.207

Proposed Rule § 37.207 requires that SEFs establish and enforce appropriate fitness standards for officers; for members of its board of directors, committees, disciplinary panels, and dispute resolution panels (or anyone performing functions similar to the foregoing); for members of the SEF or DCM; for any other person with direct access to the SEF or DCM; and for any person who owns 10 percent or more of a SEF or DCM and who, either directly or indirectly, through agreement or otherwise, in any other manner, may control or direct the management or policies of the SEF or DCM, and any party affiliated with any of those persons. The Proposed Rule further includes that "the Commission's potential standard" for the SEF's officers and for members of its board of directors "must include the requirement that each such individuals be of *sufficiently good*

repute [emphasis in original]; provided, however, that SEFs…have flexibility to establish the criteria for how individuals demonstrate good repute, as appropriate for their respective markets."[6]

The WMBAA appreciates the Commission's goal to establish minimum fitness standards that enable SEFs to effectively operate as both a market and SRO and to perform their market regulation functions in accordance with SEF Core Principle 2.[7] We want to ensure, however, that in attempting to import the requirements of DCM Core Principle 15 onto SEFs, the Commission avoids both creating confusion for its registrants and market participants, as well as unintended consequences that could stifle the ability of SEFs to do business in an effective and responsible manner.

Specifically, as noted in the NPRM, the DCM Core Principle 15 Guidance states that minimum fitness standards for "'persons who have member voting privileges, governing obligations or responsibilities, or who exercise disciplinary authority,' and 'natural persons who directly or indirectly have greater than a ten percent ownership interest in a designated contract [market]' should include those bases for refusal to register a person under section 8a(2) of the CEA."[8]

However, Proposed Rule § 37.207 specifies that a SEF "must establish and enforce appropriate fitness standards for," among others, "any person who owns 10 percent or more of the SEF and who, either directly or indirectly, through agreement or otherwise, in any other manner, may control or direct the management or policies of the SEF, and for any party affiliated with any person described in this paragraph." Further, such minimum fitness standards, including for "any person who owns 10 percent or more of the SEF and who, either directly or indirectly, through agreement or otherwise, in any other manner, may control or direct the management or policies of the SEF" must "include the bases for refusal to register a person under sections 8a(2) and 8a(3) of the Act."

As drafted, the Proposed Rule does not specify that "persons" owning 10 percent or more of the SEF is limited to natural persons, as is the case with respect to the DCM Core Principle 15 Guidance, nor does it specify the scope of minimum fitness standards applicable to such persons should be aligned with the standards applicable to "members with voting rights."

While WMBAA is generally amenable to adhering to the equivalent requirements as those set forth in the DCM Core Principle 15 Guidance (specifically, that "natural persons who directly or indirectly have greater than a ten percent ownership interest in a SEF "should meet the fitness standards applicable to members with voting rights"), the Proposed Rule, as drafted, diverges significantly from this standard by leaving out the "natural person" qualifier. Should Proposed

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[6] 89 Fed. Reg. at 19659.

[7] 89 Fed. Reg. at 19656-57.

[8] *Id.* at 19656. *See* Appendix B to Part 38, Guidance on, and Acceptable Practices in, Compliance with Core Principles; Core Principle 15, Governance Fitness Standards.

Rule § 37.207 be adopted as drafted, it would create confusion between the rule and the existing DCM Core Principle 15 Guidance. Critically, if such a standard were to be applied to non-natural persons it would create unnecessary complications for SEFs to operate and to serve market participants effectively, particularly where actions of non-natural persons wholly unrelated to the SEF's operations or functions could have unintended collateral consequences on the SEF's ability to function prudently and efficiently. To apply this standard to non-natural persons is a misguided transcription of the DCM Core Principle 15 Guidance and a needless addition to the already robust minimum fitness standards and oversight of SEF governance processes and operations by the SEFs and the Commission. Accordingly, the CFTC should clarify that in the context of Proposed Rule § 37.207, the ownership threshold requirement is limited to natural persons to harmonize the scope of the requirement with DCM guidance.

Separately, in considering "whether additional fitness requirements would enhance the performance and accountability of the individuals who are charged with governing a SEF… or its operations, or have the ability to influence such functions," we believe that the CFTC has presented a "potential standard" relating to "good repute" in a manner that is neither sufficiently comprehensible nor in accordance with the Administrative Procedure Act.[9]

First, the Commission notes in the NPRM that "at least three SEFs have already implemented a 'good repute' requirement for members of their board of directors" and "at least five DCMs and one SEF require their members or market participants to be of 'good repute,' 'good moral character,' or 'good reputation'" along with citing a requirement in European Union law.[10] The Proposed Rule offers that "the purpose of a 'sufficiently good repute' standard would be to identify individuals with a well-established history of honesty, integrity, and fairness in their personal, public, and professional matters."

It is not clear from the various terms cited, nor the discussion of the topic in the NPRM, however, what the Commission intends to achieve by potentially imposing some version of these terms as requirements for the members of a SEF's board of directors, or how such a standard would function in practice. It is not apparent or easily ascertainable, for example, what the differences are between the terms "good repute", "sufficiently good repute," "good moral character," and "good reputation" or how the individuals subject to some standard related to those terms would not otherwise be captured and/or excluded from the board of directors on the basis of the already-included minimum fitness standards of the Proposed Rule, including those standards related to disciplinary offenses.[11] It is also not clear why the SEF entities cited by the CFTC in the NPRM currently include such terminology in some form, and the Commission does not offer reasoning for its inclusion in those instances. We note that in the case of the WMBAA affiliate included in

[9] 5 U.S.C. § § 551–559.

[10] 89 Fed. Reg. at 19659 n. 148.

[11] As a practical and procedural matter, it is also not clear to us how a SEF's board of directors would effectively conduct such an assessment on its own board members.

the NPRM's footnote, the entity is U.K.-based, not U.S.-based, and is dually registered as a SEF and a Multilateral Trading Facility.[12]

Moreover, the contemplated "good repute" related standard is not included in the text of the Proposed Rule. If the Commission believes such a standard is appropriate to include in rules applicable to SEFs, the WMBAA urges the Commission to re-propose the standard as part of the Proposed Rule text and seek public comment on its inclusion.

B. Conflicts of Interest in Decision-making – Proposed § 37.1202

Regarding conflicts of interest in decision-making, Proposed Rule § 37.1202 requires SEFs to "establish policies and procedures that require any *officer* or member of its board of directors, committees, or disciplinary panels to disclose any actual or potential conflicts of interest that may be present prior to considering any matter" and specifies that "such conflicts of interests include, but are not limited to, conflicts of interest that may arise when such member or *officer*… is the subject of any matter being considered [or] is an employer, employee, or *colleague* of the subject of any matter being considered."[13] The Proposed Rule further requires SEFs to "establish policies and procedures that require any *officer* or member of a board of directors, committee, or disciplinary panel of a swap execution facility that has an actual or potential conflict of interest, including any of the relationships listed in paragraphs (a)(1) and (a)(2) of this section, to abstain from deliberating or voting on such matter."[14]

The WMBAA believes that in this context, relating to conflicts of interest in decision-making, as well as in Proposed Rule § § 37.207 (minimum fitness standards) and 37.1201 (general requirements related to conflicts of interest), the term "officer" is used in an imprecise manner.[15] We note that in other areas of the Proposed Rule, the term "senior officer" is defined and used.[16]

We urge the CFTC to provide further clarification as to the scope of the term "officer" in these contexts and suggest that in a different Commission regulation related to derivatives clearing organizations ("DCOs"), the term "Key Personnel" may—as tailored to be appropriately applied

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[12] 89 Fed. Reg. at 19659 n. 148. ICAP Global Derivatives Ltd. is a U.K.-registered entity.

[13] Proposed Rule § 37.1202(a)(1) (emphasis added).

[14] Proposed Rule § 37.1202(a)(3) (emphasis added); *see also* Proposed Rule § 37.1202(b)(1) and (2).

[15] Proposed Rule § § 37.1201(b)(16) and § 37.1501.

[16] The text of Proposed Rule § 37.1201 specifies that a "material relationship" with the SEF for purposes of the composition of the board of directors includes where "such director is an offer or employee" of the SEF (Proposed Rule § 37.1201(b)(13)(i)(A)), "such director is … an officer…of either a member or an affiliate of a member" (Proposed Rule § 37.1201(b)(13)(i)(B)), "such director… is an officer … of an entity that directly or indirectly owns more than 10 percent" of the SEF (Proposed Rule § 37.1201(b)(13)(i)(C)), and "such director, or an entity in which the director is … an officer…receives more than $100,000 in aggregate annual payments" from the SEF or an affiliate of the SEF (Proposed Rule § 37.1201(b)(13)(i)(D)).

to SEFs—be instructive to capture the scope intended by the Commission when using "officer" in the Proposed Rule.[17]

Similarly, the Commission notes in the NPRM that it "proposes replacing the current term 'fellow employee' with 'colleague' to include individuals with whom the officer or director may have a collegial relationship, but may not be employed by the same employer. As an example, two individuals who worked in the same office, where the first is a full-time employee of the organization, and the other works alongside the first but is employed by an outside contractor, would be considered colleagues for purposes of proposed §§ 37.1202."[18]

The plain English definition of "colleague" is "an associate or coworker typically in a profession or in a civil or ecclesiastical office and often of similar rank or status: a fellow worker or professional,"[19] and Black's Law Dictionary defines "colleague" as "a known employee or peer in the same profession, business or organization[;] known also as coworker."[20] In the example offered in the NPRM, it is not apparent that a full-time employee and an outside contractor would be considered "of similar rank or status." We also do not think that the employment relationship of a full-time employee and an outside or independent contractor, agent or consultant could commonly be described as a "coworker" relationship or would necessarily imply a collegial relationship such that a conflict of interest would necessarily be implied. As the footnote offered in the NPRM diverges from the common understanding and plain meaning of the word "colleague" and the Proposed Rule does not offer clarification around the definition of the term, we encourage the Commission to carefully consider the intended meaning of this word in the Proposed Rule.

C. Limitations on the Use and Disclosure of Material Non-public Information – Proposed § 37.1203

The WMBAA agrees with the Commission that "preventing the misuse and disclosure of material non-public information at SEFs … further[s] the objectives of promoting self-regulation of exchanges and maintaining public confidence in SEF … markets."[21] As noted in the NPRM,

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[17] "Key personnel means derivatives clearing organization personnel who play a significant role in the operations of the derivatives clearing organization, the provision of clearing and settlement services, risk management, or oversight of compliance with the Act and Commission regulations in this chapter, and orders promulgated thereunder. Key personnel include, but are not limited to, those persons who are or perform the functions of any of the following: Chief executive officer; president; chief compliance officer; chief operating officer; chief risk officer; chief financial officer; chief technology officer; chief information security officer; and emergency contacts or persons who are responsible for business continuity or disaster recovery planning or program execution." 17 C.F.R. § 39.2.

[18] 89 Fed. Reg. at 19662 n. 162.

[19] *See* Merriam-Webster Dictionary, https://www.merriam-webster.com/dictionary/colleague (retrieved on April 17, 2024).

[20] *See* Black's Law Dictionary, https://thelawdictionary.org/colleague/ (retrieved on April 17, 2024).

[21] 89 Fed. Reg. at 19663.

the CEA and Commission Rules already include prohibitions on the misuse and disclosure of material non-public information, and the SEFs operated by WMBAA members already include substantial policies and procedures related to such prohibitions.[22] The WMBAA believes that the Proposed Rule is unnecessarily prescriptive and duplicative of existing regulatory requirements. To the extent the Commission adopts them, the WMBAA agrees with the position enunciated by Commissioner Pham in her statement in the NPRM. [23] We similarly encourage the Commission to ensure consistency in terminology related to the definition of "material non-public information" to avoid unnecessary confusion among market participants or inconsistency between regulations applicable to SEFs and to ensure that the rule does not "undermine[] robust compliance programs by introducing uncertainty."[24]

D. Composition and Related Requirements for Board of Directors – Proposed § 37.1204

Under current DCM Core Principle 16 Acceptable Practices, a DCM's board of directors or executive committees must include at least 35 percent public directors.[25] The NPRM cites the rule release related to adopting the DCM acceptable practice, stating that the 35 percent figure "struck an appropriate balance between (1) the need to minimize conflicts of interest in DCM decision-making processes and (2) the need for expertise and efficiency in such processes."[26]

Proposed Rule § 37.1204 imports this acceptable practice into a rule for SEFs, requiring a SEF's board of directors, and any executive committee, to include at least 35 percent public directors.[27]

This proposed threshold is the same as that proposed in the withdrawn 2010 conflicts of interest rule proposal.[28] In that proposal, the Commission did not offer reasoning for proposing the 35 percent requirement for SEFs, beyond stating the rationale it argued for DCMs—as cited

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[22] 17 C.F.R. § 1.59.

[23] *See* 89 Fed. Reg. at 19725-26 (Statement of Commissioner Caroline D. Pham).

[24] *See id.* at 19725-26 (Statement of Commissioner Caroline D. Pham).

[25] Part 38, Appendix B, Core Principle 16 Acceptable Practices (b)(1).

[26] 89 Fed. Reg. at 19666.

[27] *Id*.

[28] Requirements for Derivatives Clearing Organizations, Designated Contract Markets, and Swap Execution Facilities Regarding the Mitigation of Conflicts of Interest, 75 Fed. Reg. 63732 (October 18, 2010); *see also* 89 Fed. Reg. at 19650.

above—"would appear to apply to SEF … Boards of Directors as well."[29] Aside from this unsupported statement, it does not appear that the Commission has otherwise articulated a cogent rationale for the proposed requirement (in the context of the adoption of the SEF Core Principles or otherwise). In any case, we do not believe that each executive committee must also be comprised of at least 35 percent public directors because such a requirement may be operationally impracticable and overly burdensome.

The Commission states in the NPRM that its "goal with respect to Core Principle 16 is to ensure that the commercial interests of SEFs and DCMs and of its constituencies do not compromise market regulation functions" in its recognition that SEF boards of directors "need to have individuals … with sufficient background and expertise to support the SEF's … market functions."[30] The WMBAA agrees with this sentiment and also understands the Commission's view that "individuals with sufficient independent perspectives on the board of directors" should be included "to ensure that the SEF … can properly manage conflicts in its decision-making."[31] The Commission further states that it "believes that imposing a majority threshold in all circumstances may deny SEFs … the flexibility necessary to ensure that the board of directors includes individuals with adequate market expertise" and that "the Commission is currently unaware of any circumstances that would support requiring public directors to constitute a majority of the board of directors of every SEF."[32]

The WMBAA strongly agrees that requiring a majority threshold of public directors on the board of directors of SEFs is not necessary or warranted and may be overly burdensome to a SEF. We further believe that it is not necessary to impose a strict 35 percent threshold on SEFs in order to address the concerns articulated by the Commission. As the CFTC recognizes, it is important for SEFs to retain flexibility in the composition of their boards of directors to ensure that such boards have appropriate levels of market expertise. We believe that imposing a prescriptive numerical threshold constrains SEFs from that important flexibility under the CFTC's principle-based regime, which may stifle the SRO function of SEFs.

Finally, in response to one of the Commission's questions, the WMBAA strongly opposes a 51 percent public director requirement, which would be overly burdensome and uneconomical to SEFs. The WMBAA knows of no policy objective that would be achieved with such a requirement. Further, the WMBAA points out that the Commission has not articulated such a rationale in the Proposed Rule. If the Commission determines to move to a 51 percent public director requirement, that should be the subject of a future proposal.

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[29] 75 Fed. Reg. at 63738 ("In the DCM Conflicts of Interest Release, the Commission stated that the 35 percent requirement struck an appropriate balance between (i) the need to minimize conflicts of interest in DCM decision-making processes with (ii) the need for expertise and efficiency in such processes. Such rationale would appear to apply to SEF and DCO Boards of Directors as well.")

[30] 89 Fed. Reg. at 19667.

[31] 89 Fed. Reg. at 19667.

[32] 89 Fed. Reg. at 19667.

E. Public Director Definition – Proposed § 37.1201(b)(12)

The current "public director" definition found in DCM Core Principle 16 Acceptable Practices provides for the DCM's board of directors to determine, on the record, that the director has no "material relationship" with the DCM,[33] and contains a list of *per se* material relationships (the "bright-line disqualifiers") that disqualify service as a public director, including where "such director, or a firm in which the director is an officer, director, or partner, receives more than $100,000 in aggregate annual payments[34] for legal, accounting, or consulting services from the DCM, or an affiliate of the DCM."[35]

The Proposed Rule, if adopted, would codify, with modifications, this existing DCM Core Principle 16 Acceptable Practices "public director" definition for both SEFs and DCMs. Specifically, it would apply the bright-line disqualifier related to public director compensation to SEFs where a director receives more than $100,000 in aggregate annual payments for any purpose from the SEF or an affiliate of the SEF (removing the reference "for legal, accounting, or consulting services").[36] The Commission noted in the NPRM that "eliminating 'legal, accounting, or consulting service' from the bright-line disqualifier that applies to payments in excess of $100,000 is necessary, as the provision of other services could also be 'material' for purposes of establishing whether an individual qualifies as a public director."[37]

The WMBAA does not believe the Commission should automatically assume that a director has a "material relationship" with a SEF if that director or a firm in which the director is an officer, director, or partner, received a specific amount of money from the SEF or the SEF's affiliate. Some experienced people and firms may command tens of thousands of dollars or more for providing software or technical administrative services, for example, and we do not believe that a director should be assumed to have a material relationship with a company for providing such services. We believe the "overarching materiality test" set forth in the existing DCM Core Principle 16, as applied to SEFs in the Proposed Rule § 37.1201(b)(13), is sufficiently broad enough to capture situations where a material relationship exists, regardless of the size or purpose of such a payment.

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[33] Part 38, Appendix B, Core Principle 16 Acceptable Practices (b)(2)(i).

[34] As noted in the NPRM, compensation for services as a director of the DCM or as a director of an affiliate of the DCM does not count toward the $100,000 payment limit, nor does deferred compensation for services prior to becoming a director, so long as such compensation is in no way contingent, conditioned, or revocable.

[35] Part 38, Appendix B, Core Principle 16 Acceptable Practices (b)(2)(ii).

[36] The Proposed Rule specifies that "compensation for services as a director of the swap execution facility or as a director of an affiliate of the swap execution facility does not count toward the $100,000 payment limit, nor does deferred compensation for services rendered prior to becoming a director of the swap execution facility, so long as such compensation is in no way contingent, conditioned, or revocable." Proposed Rule § 37.1201(b)(13)(i)(D).

[37] 89 Fed. Reg. at 19669.

In the NPRM, the Commission asked if it should "continue to permit public directors to serve on the board of directors of a SEF's or DCM's affiliate?" As noted above, the Commission recognizes that SEF boards of directors "need to have individuals … with sufficient background and expertise to support the SEF's … market functions" as well as "individuals with sufficient independent perspectives" on the board.[38] WMBAA believes that permitting directors to serve on the board of directors of a SEF who also sit on the board of directors of a SEF's affiliate can positively impact both of these elements, and should continue to be allowed under CFTC Rules.

F. Nominating Committee and Diverse Representation – Proposed § 37.1205

Proposed Rule § 37.1205 requires a SEF's nominating committee be comprised of at least 51 percent public directors "to enhance the transparency of the board of directors."[39]

The WMBAA is not supportive of a requirement for SEF nominating committees to be composed of at least 51 percent public directors. The Commission's stated aims of including this high threshold are to "limit the influence of non-public directors that are already involved in the governance and management of a SEF … and to help ensure a broader pool of candidates for consideration, in turn promoting diversity and independent perspectives in the governing bodies of SEFs."[40]

We believe such a requirement is unnecessarily burdensome, uneconomical, and could lead to unintended consequences with respect to the effective operation and appropriate SRO function of SEFs. For example, under the Proposed Rule, if a SEF board of directors is composed of five directors (which is common in the experience of WMBAA-member SEF entities), at least two of those directors must be public directors to satisfy the 35 percent public director requirement. A nominating committee, to meet the requirement to have at least 51 percent public directors, would need to have at least three committee members, at least two of which would be public directors, leaving just one non-public director for such nominating committee. In WMBAA's view, this could lead to nominating committees considering candidates without the benefit of specific business knowledge related to the SEF that is brought to committee deliberations by non-public directors. The WMBAA also knows of no reason why the public director requirement for the nominating committee should be higher than the requirement for the board of directors itself. Further, we believe that SEFs, as they currently operate, adequately consider diverse pools of candidates and independent perspectives for their boards of directors, and imposing such an onerous requirement on SEF nominating committees is therefore an unnecessary burden.

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[38] 89 Fed. Reg. at 19667.

[39] *Id.* at 19666.

[40] *Id.* at 19670.

G. Regulatory Oversight Committee – Proposed § 37.1206

Proposed Rule § 37.1206(a) requires a SEF to establish a ROC and that it be comprised solely of public directors "to protect the integrity of the market regulation function of SEFs."[41] Under Proposed Rule § 37.1206(f), the ROC "must have processes related to the conducting of meetings, including" that it "must not permit any individuals with actual or potential conflicts of interest to attend any discussions or deliberations in its meetings that relate to the [SEF's] market regulation functions."

In its discussion of this proposal, the Commission observes that "some DCMs have limited individuals other than ROC members or DCM staff performing market regulation functions from attending the ROC meetings, while others have allowed DCM executives and non-ROC members of the board of directors to attend" and that in the Commission's view, the "former practice is preferable as the latter practice invites to ROC meetings the very conflicts of interest that the establishment of a ROC is intended to address."[42] The Commission also states that it "recognizes … that there may be limited circumstances in which it would be appropriate for individuals outside of the ROC—including business executives or employees whose interest may conflict in certain respects with the ROC's market regulation functions—to attend portions of ROC meetings."

The WMBAA is generally supportive of the CFTC's proposal that SEFs establish a ROC. However, we believe that in the context of this proposed requirement, Proposed Rule § 37.1206(f)(1)(ii) is wholly unnecessary and could serve to work against the Commission's goals by creating information barriers restricting the ROC from functioning successfully.

While we understand the view that individuals "with actual or potential conflicts of interest" be restricted from acting as decision-makers or voting on issues within the purview of the ROC, Commission regulations should not be so inflexible as to hamstring the ROC from effectively doing its work. Disallowing such individuals from being "present, in any capacity, during discussions of the SEF's … market regulation functions, such as surveillance, investigation, or enforcement work" could indeed create such a dynamic.[43] The ROC (particularly if comprised entirely of public directors, as proposed) could regularly face situations where it would benefit from hearing from such individuals in the context of their discussions or deliberations about a particular issue. CFTC regulations should not be so overly restrictive so as to result in situations where the ROC cannot perform its responsibilities effectively due to incomplete information.

Specifically, in response to the Commission's question "should business executives and employees working outside of the SEF's or DCM's market regulation functions be permitted to attend even portions of ROC meetings that relate to their business? Or should ROC meetings be strictly limited to ROC members and employees who perform work related to the SEF's or DCM's

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[41] *Id.* at 19666.

[42] *Id.* at 19671.

[43] *Id.* at 19672.

market regulation functions?" The WMBAA strongly believes that the Proposed Rule is far too overreaching in its restrictions and requirements and the Commission should craft the rule to give the ROC sufficient independence in determining appropriate processes and meeting attendance, in alignment with the CFTC's overall principles-based approach.

H. Disciplinary Panel Composition – Proposed § 37.1207

Currently, CFTC Rule § 1.64(c) applies to SEFs and requires each major disciplinary committee or hearing panel to include: (1) at least one member who is not a member of the SEF; and (2) sufficient different membership interests so as to ensure fairness and to prevent special treatment or preference for any person in the conduct of a committee's or the panel's responsibility. The WMBAA believes that the current structural requirements for such panels are sufficient and have functioned well for SEFs, and Proposed Rule § 37.1207 is unduly prescriptive; SEFs should be permitted to establish the composition and procedures of disciplinary panels flexibly in line with current regulations.

I. Staffing and Investigations – Proposed Changes to § 37.203

Proposed Rule § 37.203 would require a SEF to "establish and maintain sufficient staff and resources to effectively perform market regulation functions" and to monitor on an annual basis the size and workload of its staff and ensure its resources and determine staff effectively perform market regulation functions at appropriate levels, determined in light of enumerated factors, including "trading volume increases, the number of new products or contracts to be listed for trading, any new responsibilities to be assigned to staff, any responsibilities that staff have at affiliated entities, the results of any internal review demonstrating that work is not completed in an effective or timely manner, any conflicts of interest that prevent staff from working on certain matters, and any other factors suggesting the need for increased staff and resources."[44]

The WMBAA agrees that establishing and maintaining appropriate procedures that require staff responsible for market regulation functions to conduct investigations of possible rule violations, and ensuring these market regulation staff are properly resourced, are important ways SEFs support the operation of a well-regulated market and enable SEFs to appropriately engage in self-regulatory activities.

We believe that the Proposed Rule, however, is an unnecessary overreach and is unduly prescriptive in light of the current approach to these responsibilities SEFs currently engage in. In particular, we are concerned about Proposed Rule § 37.203(d), which proposes to include in the list of factors that a SEF should consider in determining the appropriate level of resources and staff any responsibilities that staff have at affiliated entities.

[44] *Id.* at 19676.

SEF Core Principle 13 currently requires that SEFs "have adequate financial, operational, and managerial resources to discharge each responsibility of the swap execution facility."[45] In furtherance of this core principle, SEFs already monitor the size and workload of market regulation staff to determine appropriate resource adequacy and make adjustments as needed. This is further supported by the duties undertaken by the SEF CCO pursuant to CFTC Rule 37.1501.[46] For many years, SEFs have effectively undertaken their duties related to compliance and "market regulation" functions without prescriptive dictates regarding the balancing of staff workload between affiliates. To the extent that the responsibilities that staff may have at affiliated entities could pose an issue to ensuring adequate resources set aside for compliance functions, the SEF CCO would already be responsible for raising such an issue to the SEF's governance bodies as appropriate. Further, to the extent that the Commission adopts a requirement that SEFs must establish a ROC (as proposed, comprised of entirely public directors) it would also have oversight in this regard. Imposing this prescriptive obligation onto SEFs may unduly result in increased costs for SEFs and a decrease in the sophistication and market intelligence brought by staff to the SEF under current cost sharing models between SEFs and their affiliates.

In the WMBAA's view, the NPRM does not provide adequate reasoning for the inclusion of the affiliated entity requirement as a necessary element of the Proposed Rule,[47] and the Proposed Rule is unnecessarily duplicative and prescriptive when considered in the context of the existing regulatory requirements and responsibilities applicable to the SEF and the SEF CCO.

J. Transfer of Equity Interest – Commission regulations § 37.5(c)

Proposed Rule § 37.5(c) requires SEFs to file with the CFTC notification of transactions involving the transfer of at least 10 percent of the equity interest in the SEF, a threshold well below the current 50 percent threshold and in conformance with existing CFTC regulations for DCMs and DCOs. It further specifies that "a change in the ownership or corporate or organizational structure of a [SEF] that results in the failure of the [SEF] to comply with any provision of the Act, or any regulation or order of the Commission thereunder … shall be cause for the suspension of the registration of the [SEF] or the revocation of registration as a SEF, in accordance with the

[45] 17 C.F.R. § 37.1300.

[46] *See* 17 C.F.R. § 37.1501(d)(3) (requiring, as an element of the annual compliance report, "a description of the financial, managerial, and operational resources set aside for compliance with the Act and applicable Commission regulations.").

[47] The only discussion of this element of the requirement, even in passing, is in the cost-benefit analysis of the Proposed Rule, where the Commission suggests that "[t]his amendment is beneficial because it will help ensure sufficiency of SEF staff responsible for performing market regulation functions and identify in a timely way any potential conflicts of interest relating to market regulations staff, particularly regarding a SEF's or DCM's affiliates." 89 Fed. Reg. at 19697.

procedures provided in sections 5e and 6(b) of the Act, including notice and a hearing on the record."[48]

The WMBAA is very concerned that the Commission is proposing to promulgate, in the context of these Proposed Rules, a rule which would enable the Commission to suspend or revoke a SEF's registration without sufficient and demonstrable reasonableness for such proposal and without ensuring that due process is afforded to SEFs prior to any Commission suspension or revocation action. Moreover, as noted by Commissioner Pham in her statement, "the rules are clearly overbroad because the CFTC could revoke registration due to changes 'in the ownership or corporate or organizational structure'" of a SEF, which "could include simple changes in headcount and other staffing reorganizations, making it all too easy for the CFTC to manufacture a reason to revoke registration."[49]

We urge the Commission to remove this provision in its entirety. First, we urge the Commission to consider the markets in which SEFs operate, where competition and liquidity could be significantly negatively impacted should a SEF's registration be suspended or revoked without due consideration of the market impact of such a decision and absent the ability of the SEF to correct any identified issues in the course of business. Further, there are substantial mechanisms already extant enabling the CFTC to ensure that SEFs have appropriate ownership structures and governance and comply with regulatory requirements. The CFTC has the power to conduct investigations[50] and sanction violations of the CEA. Section 5e of the CEA also authorizes the CFTC to suspend or revoke the designation of a contract market, SEF, or DCO based on a failure or refusal to comply with any of the provisions of the CEA, CFTC regulations, or CFTC orders.[51] Adding this rule, as proposed, is duplicative of powers already available to the CFTC in its oversight of SEFs and represents a dangerous overreach of the Commission's ability to suspend or revoke a SEF's registration without due process.

III. Conclusion

The WMBAA supports the CFTC's goal to improve the governance and decision-making processes and reduce conflicts of interest of SROs, including SEFs, and appreciates the Commission's ongoing commitment to provide guidance to its registrants. However, we urge the CFTC to consider carefully the ways in which promulgating unduly prescriptive and highly

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[48] Proposed Rule § 37.5(c)(6).

[49] *See* 89 Fed. Reg. at 19725-26 (Statement of Commissioner Caroline D. Pham).

[50] *See* CFTC Division of Enforcement, Enforcement Manual (May 20, 2020) (noting that "The statutory authority for the Division to conduct investigations into potential violations of the CEA or the Regulations is found in Sections 6(c)(5), 8(a)(1), and 12(f) of the CEA, 7 U.S.C. §§ 9, 15, 12(a)(1), 16(f). The authority to conduct investigations is delegated to the Director of the Division of Enforcement under Part 11 of the Regulations, 17 C.F.R. pt. 11."), *available at* https://www.cftc.gov/sites/default/files/2021-05/EnforcementManual.pdf.

[51] 7 U.S.C. § 7b.

technical requirements may hinder the very processes and operations of SEFs that underpin the core principles set forth in the CEA and lead to potential uncertainty and confusion for SEFs and the markets they serve. We urge the CFTC to reconsider the new, complicated, and highly specific elements of the Proposed Rule that, as described herein, are not supported by an articulated need, or, in the alternative, to simplify the Proposed Rule to more closely reflect the Commission's longstanding principles-based approach in alignment with the statutory framework of the CEA.

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The WMBAA appreciates the CFTC's efforts in seeking public input on the Proposal. We thank the CFTC staff for its willingness to consider our opinions and welcome the opportunity to discuss these issues further.

Sincerely,

William Shields
Wholesale Markets Brokers' Association, Americas