



SWAPS & DERIVATIVES MARKET ASSOCIATION

November 26, 2010

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

Elizabeth M. Murphy, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington DC 20549-1090

Re: Comments from the Swaps & Derivatives Market Association on the CFTC Requirements for Derivatives Clearing Organizations, Designated Contract Markets, and Swap Execution Facilities Regarding the Mitigation of Conflicts of Interest. CFTC 17 CFR Parts 1, 37, 38, 39 and 40, RIN 3038-AD01 and the SEC Ownership Limitations and Governance Requirements for Security-based Swap Clearing Agencies, Security-Based Swap Execution Facilities, and National Exchanges with Respect to Security-Based Swaps under Regulation MC. SEC 17 CFR Part 242, Release No. 34-63107; File No. S7-27-10, RIN 3235-AK74

Dear Sir/Madam Secretaries,

The Swaps & Derivatives Market Association ("SDMA") appreciates the opportunity to comment on the Notice of Proposed Rulemaking regarding Section 726 (CFTC) and 765 (SEC) of the Dodd-Frank Act that pertains to the Mitigation of Conflicts of Interest for Derivatives Clearing Organizations ("DCOs"), Security-Based Swap Clearing Agencies, Designated Contract Markets ("DCMs"), Swap Execution Facilities ("SEFs") and Exchanges. The SDMA largely supports Title VII of the Dodd-Frank Act and commends the extensive hours of due diligence and follow-through by both chambers of Congress, regulators and staff to make the legislation an effective document.

The SDMA is a financial markets trade group of United States and internationally based broker-dealers, futures commission merchants and investment managers participating in all segments of the exchange-traded and over-the-counter derivative and securities markets. The SDMA was created as a nonprofit organization in January 2010 and today has over 20 member institutions representing all facets of derivatives execution and clearing.



The SDMA believes the Mitigation of the Conflicts of Interest sections of Title VII of the Dodd-Frank Act are vitally important; especially when referring to the swaps and derivatives marketplace chokepoints of Clearing Houses, DCMs, SEFs and Exchanges for the issues of:

- 1) Increased competition in execution and clearing on a mutually exclusive basis
- 2) Increased number of clearable types of swaps and derivatives; and
- 3) Objective and non-arbitrary IRS and CDS clearing member & participant requirements

The SDMA supports the CFTC and SEC proposals outlined below as they address the need for objective standards, open access and transparency in the OTC swaps and derivatives markets. We believe they are consistent with the core principles of the Dodd-Frank Act to help insure the successful addition of mutually exclusive execution-only broker/dealers and qualified clearing members and participants who will increase liquidity and diversify systemic risks.

The following outline lists the Regulatory Proposals as procured from the Federal Register in table format followed by the SDMA's recommendations.

I. Clearing Houses: Derivatives Clearing Organizations (DCOs)/Security-Based Swap Clearing Agencies

A. Voting Power: Direct & Indirect Limitation on Voting Equity Ownership & Exercise of Voting Rights

Regulatory Proposals	Individual Aggregate	Collective Aggregate
CFTC First Alternative	20% max by clearing member and/or enumerated entity and their related persons	40% collective max by all clearing members and/or enumerated entities and their related persons
CFTC Second Alternative	5% max by clearing member and/or enumerated entity and their related persons	None proposed because of 5% cap in the individual aggregate
SEC Voting Interest Alternative	20% max by clearing agency participant and its related persons.	40% collective max by all clearing agency participants and their related persons.
SEC Governance Focus Alternative	5% max by a clearing agency participant and its related persons	None proposed because of the 5% cap in the individual aggregate

Recommendation: The SDMA supports the CFTC's First Alternative proposal regarding Voting Power. This proposal not only addresses the issues most effectively but also allows for the inclusion of both clearing and non-clearing members and participants. The CFTC First Alternative establishes a diversified decision making foundation to insure more transparency and provides balanced procedures for the proper vetting of: 1) whether a swap contract is capable of being cleared; 2) the minimum criteria that an entity must meet in order to become a clearing member; and 3) whether a particular entity satisfies such criteria.

Current Clearing House voting structures are too focused and not truly representative of the market as a whole. Such a lack of diversification and concentrated governance provides for the risk that decisions are made on incomplete data that are not representative of the market. Because Clearing Houses now have the important central role of successful mitigation of OTC systemic risk, they must have more transparent, open, balanced, representative and independent governance structures.

The SDMA recognizes that Clearing Houses have significant responsibilities and would recommend against limitations on non-voting equity. Any waiver of voting limits as mentioned in the Federal Register once adopted is not recommended unless it can be proven that without them the following has been improved: 1) Governance, 2) Systemic Risk Mitigation, 3) Competition and 4) Fair and open access as evidenced by more executing-only broker/dealers and qualified clearing members/participants in addition to more products eligible for clearing.

B. Board of Directors and any Executive or Authoritative Arm Thereof

CFTC First and Second Alternatives	35% min Independent Directors with two total minimum being Independent Directors
SEC Voting Interest Alternative	35% min Independent Directors
SEC Governance Focus Alternative	51% min Independent Directors

Recommendation: The SDMA supports the CFTC's First and Second Alternative proposals. It is our understanding that the Commission has thoroughly vetted their proposals with the public in a recent rulemaking and is consistent with their core principles in designated contract markets (DCMs). Independent Directors play a valuable role but should not be charged with having a majority say on all matters of the Board's business. Specific matters are for separate committees with different compositions that are addressed below.

C. Risk Management Committee (and Subcommittee)

CFTC First and Second Alternatives	35% Independent Directors with sufficient clearing expertise, 10% Customers of clearing members unless delegated to the Risk Mgt. Subcommittee
SEC Voting Interest Alternative	35% min Independent Directors
SEC Governance Focus Alternative	51% min Independent Directors

Recommendation: The SDMA supports the SEC Governance Focus Alternative of min 51% Independent Directors, as it would insure more objectivity around the issues of membership, clearable swap contracts and the safety of the global financial system.

To date, clearing members and participants at interest rate and credit default swap Clearing Houses have been exclusively enumerated entities and thus have had an incentive to influence risk assessments pertinent to Risk Management Committee matters of: 1) whether a swap contract is capable of being cleared; 2) the appropriate membership criteria for a swap clearing member/participant; and 3) whether a particular entity meets such criteria. Being mindful of the necessity to avoid “strawmen” and the difficulty in finding strong independent personalities who are highly qualified especially in the areas of clearing to work with the Board, it certainly helps to have a majority of independent voices officially counted to provide balance at the very minimum. Such criteria should apply to the Risk Committee whether or not there is a Risk Management Subcommittee. Additionally, ideas and recommendations of clearing member and participant customers are certainly important but we believe their highest priority is, in fact it is their fiduciary duty, to keep initial margin rates low to increase the return profiles to their investors. The system is better off with higher margin rates with the cost-benefit inflection point the subject of a different paper.

D. Nominating Committee

CFTC First and Second Alternatives	51% min Independent Directors with an Independent Chair
SEC Voting Interest Alternative	51% Independent Directors
SEC Governance Focus Alternative	100% Independent Directors

Recommendation: The SDMA supports the CFTC First and Second Alternative proposals. The Nominating Committee identifies individuals qualified to serve on the Board of Directors and administers a process for

nomination to the Board. Making it a majority independent committee with an Independent Chair protects the integrity of the decision process by striking a balance between the inputs and concerns of all parties.

E. Disciplinary Panel

CFTC First and Second Alternatives	Minimum one Independent Director with an Independent Chair
SEC Voting Interest & Governance Focus Alternatives	Balanced with one Independent Director

Recommendation: The SDMA supports the CFTC First and Second Alternative proposals. The Disciplinary Panel's responsibilities are to conduct hearings, render decisions and impose sanctions on disciplinary matters. To maintain voting, financial and organizational impartiality it is imperative that Independent Directors are involved in a meaningful way.

II. Designated Contract Markets (DCMs)/Swap Execution Facilities (SEFs)/Exchanges**A. Voting Power: Direct & Indirect Limitation on Voting Equity Ownership & Exercise of Voting Rights**

Regulatory Proposal	Individual Aggregate	Collective Aggregate
CFTC	20% max by SEF/DCM member and/or enumerated entity and their related persons	None proposed to increase competition
SEC	20% max by SEF participant and/or Exchange member and their related persons	None proposed to increase competition

Recommendation: To promote competition in the newly formed SEF market as well as on DCMs and Exchanges from many different sources, the SDMA supports the CFTC proposal because it includes clearing and non-clearing members and participants.

Since SEFs, DCMs and Exchanges are charged with price discovery, trade execution and have self-regulatory obligations they effectively are a steward of public trust. Therefore, it is imperative to make sure these entities

are prioritizing self-regulatory responsibilities over commercial interests and providing direct and indirect access in a non-discriminatory manner.

It is important to point out that DCMs, SEFs, and Exchanges do not pose the same type of margin or systemic risk that Clearing Houses do. They are merely providing a trade execution platform that enables members, participants, investors, etc to increase pre-trade price transparency and post-trade operational efficiency. Issues arise when the management and/or owners of a these entities limit access and the scope of tradable products as well as abuse their voting power within a small group of players. The SDMA agrees with the Commissions that more independent directors on various important Boards do not justify more lenient limits on voting power and that they should be used in conjunction with one another to effectively have a checks and balances system within the organization. However, given the low barriers to entry relative to Clearing Houses, the voting power issues especially should not be an overriding concern.

B. Board of Directors and any Executive or Authoritative Arm Thereof

CFTC	35% min Independent Directors with min of 2 total Independent Directors
SEC	51% Independent Directors

Recommendation: The SDMA supports the CFTC proposal. Independent Directors play a valuable role but should not be charged with having a majority say on all matters of business. Specific matters are for separate committees that are addressed below.

C. Nominating Committee

CFTC	51% Independent Directors with an Independent Chair
SEC	100% Independent Directors

Recommendation: The SDMA supports the CFTC proposal. The Nominating Committee identifies individuals qualified to serve on the Board of Directors and administers a process for nomination to the Board. Making it majority independent with an Independent Chair protects the integrity of the decision making process by striking a balance between the inputs and concerns of management, investors, and qualified public directors.

D. Disciplinary Panel

CFTC	Min one Independent Director with an Independent Chair
SEC	Balanced with min one Independent Director

Recommendation: The SDMA supports the CFTC proposal. The Disciplinary Panel's responsibilities are to conduct hearings, render decisions and impose sanctions on disciplinary matters. To maintain voting, financial and organizational impartiality it is imperative that Independent Directors are involved in a meaningful way.

E. Regulatory Oversight Committee

CFTC	100% Independent Directors
SEC	100% Independent Directors

Recommendation: The SDMA supports the CFTC and SEC's proposals. The ROC oversees all facets of the regulatory program including proposals and adherence to rules and regulations. It's imperative that this committee remains 100% independent as it helps the Commissions carry out enforcement of the Act regarding fair and open access and the scope of products traded given that as few as five (5) major swap dealers or enumerated entities could effectively control 100% of a DCM, SEF or Exchange.

F. Participation or Membership Committee

CFTC	35% Independent Directors
SEC	None Required

Recommendation: The SDMA supports the SEC proposal. This committee determines the standards for initial and continuing membership, reviews appeals of staff denials of membership applications, and approves rules that would result in different classes of members receiving disparate access to the SEF. While certainly important, its functionality can be handled by the Regulatory Oversight Committee and/or delegated by the Board.



Conflicts of Interest Phase-in Implementation Period

The CFTC and SEC are proposing to permit a phase-in implementation period for rules pertaining to Conflicts of Interest of over 2 years or two regularly scheduled Board of Director's elections that would apply to existing Clearing Houses, DCMs, SEFs, Exchanges, or other organizations that officially want to register as a IRS and/or CDS Clearing House, DCM, SEF, or Exchange. However, all newly created IRS and CDS Clearing Houses, DCMs, SEFs, and Exchanges would have to comply immediately with the final rules. This proposal is anti-competitive and gives supreme advantage to all incumbent institutions. The SDMA recommends that to promote competition and a fair playing field that adherence to any Conflicts of Interest rules be equally applied.

The SDMA's recommendations set forth in this letter point to the necessity for the CFTC and SEC to jointly issue rules and regulations for Clearing Houses, DCMs, SEFs and Exchanges. Anything less will cause confusion and create loopholes; especially when trying to harmonize with international regulatory bodies.

Further information and support can be found in our Skirmish paper and comment letters from some of our members MF Global and New Edge:

- 1) http://www.newedge2009.com/images_newedgegroup/comment_letters/2010-1021_Access.pdf
- 2) <http://www.mfglobal.com>
- 3) http://www.thesdma.org/pdf/skirmish_paper_091610.pdf

We appreciate the opportunity to comment on these important issues and look forward to working with the Commissions to implement this important legislation. If you have any questions or need additional information please contact the Swaps & Derivatives Market Association at mhisler@thesdma.com or visit our website at www.thesdma.com.

Sincerely,

A handwritten signature in blue ink, appearing to read "Mike Hisler", is written over a faint, larger signature.

Mike Hisler

Co-Founder

The Swaps & Derivatives Market Association