Bernard W. Dan
President and
Chief Executive Officer

Chicago Board of Trade

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BY E-MAIL AND CERTIFIED MAIL

Ms. Jean A. Webb
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

COMMENT

Re: Self Regulation and Self Regulatory Organizations
70 F.R. 71090 (November 25, 2005)

Dear Ms. Webb:

The Board of Trade of the City of Chicago, Inc. ("CBOT®" or "Exchange") appreciates the opportunity to respond to the Commodity Futures Trading Commission's ("Commission") request for additional comments in connection with the Commission's ongoing review of self-regulation and self-regulatory organizations in the U.S. futures industry ("SRO Study").

Introduction

Recognizing the importance of futures industry self-regulation, and the Commission's obligation to foster and maintain market integrity, the Commission initiated its SRO Study in May 2003, in order to review the roles, responsibilities, and capabilities of SROs in the context of market changes. In June 2004, the Commission issued a Request for Comments that focused, among other things, on board composition, changing business models and ownership structures, and the organization and oversight of SROs' regulatory departments.[1] The CBOT filed a comment letter in response to the June 2004 Request on September 30, 2004, and would appreciate the Commission's consideration of those comments in conjunction with the additional comments contained in this letter. The Commission has issued its current Request for Comments in order to update its prior fact-finding on self-regulation and solicit any further comments in light of recent industry developments.

The Commission has also scheduled a Hearing on Self-Regulation and Self-Regulatory Organizations in the U.S. Futures Industry for February 15, 2006. On January 13, 2006, the CBOT filed a request to appear at the Hearing in order to express its views.

[1] In June 2004, the Commission also requested that each SRO complete a questionnaire regarding its governance structures, policies and procedures. The Exchange submitted its response to this questionnaire to the Commission on September 30, 2004.

141 W. Jackson Blvd.
Chicago, Illinois 60604-2994
312 435-3606
Fax: 312 347-4259

The CBOT continues to believe in the efficacy of the current system of self-regulation in the U.S. futures markets, under Commission oversight. The Exchange recognizes that questions have been raised whether conflicts of interest might arise, and whether the effectiveness of self-regulation might suffer, as a result of the conversion of futures markets into for-profit, publicly-owned companies.[2] However, a publicly-held futures exchange has strong incentives to ensure that its self regulatory function is not compromised by conflicts of interest – an exchange's integrity is critical to attracting customers and trading volume, the principal source of revenue for most futures exchanges. An exchange will only succeed in today's competitive business environment if it regulates itself in a manner that promotes market integrity and customer protection. Recognizing this, over the past several years we have devoted, and continue to devote, significant financial and technology resources to support and improve the CBOT's self-regulatory function. And the Exchange's experienced regulatory staff and disciplinary committees continue to maintain a strong track record with regard to the investigation of potential rule violations and the imposition of significant disciplinary penalties where they are warranted.

Notwithstanding the foregoing, the CBOT also recognizes that the methods and processes of futures industry self-regulation need to be periodically re-examined to ensure that they remain effective as business and governance models evolve. The Exchange has historically reviewed, and continues to review, its self-regulatory programs on an ongoing basis. Moreover, the Commission's Division of Market Oversight conducts periodic Rule Enforcement Reviews to ensure that exchanges are complying with the Core Principles set forth in the Commodity Futures Modernization Act of 2000 ("CFMA"). These internal and oversight reviews will reveal any specific weaknesses in particular self-regulatory programs, if they exist, so that necessary improvements can be made.

Furthermore, the Rule Enforcement Review function of the Commission continues to provide an important incentive for effective self-regulation by exchanges. Because the results of the rule enforcement review process are publicly available, adverse findings could affect an exchange's reputation for integrity. Against the backdrop of the competitive pressures in favor of effective self-regulation, there are legal and regulatory safeguards that already exist in the Commodity Exchange Act ("Act") and Commission Regulations. For example, Section 9(f) of the Act and Regulation 1.59(d) provide severe penalties for the improper use or disclosure of confidential information by exchange employees, board members, and committee members.

The Commission has indicated that as it concludes its SRO Study, it will carefully consider the need for additional guidance with respect to the insulation of self-regulation from conflicts of interest and improper influence. The CBOT appreciates the

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[2] The common stock of Chicago Mercantile Exchange's holding company has been publicly-traded since December 2002, the common stock of the CBOT's holding company has been publicly-traded since October 2005, and the New York Mercantile Exchange ("NYMEX"), which demutualized in November 2000, is reportedly anticipating an initial public offering of its common stock later this year.

Commission's expressed commitment to industry self-regulation and flexible core principles under Commission oversight, which we believe continues to be the most efficient and effective regulatory structure. To the extent the Commission believes additional guidance is necessary to assist demutualized exchanges in complying with those Core Principles, we strongly believe that any such guidance should be non-prescriptive so that exchanges may continue to develop self-regulatory programs that best fit the unique circumstances of their markets.

The CBOT addresses the specific questions posed by the Commission below.

1. **Is the present system of self-regulation an effective regulatory model for the futures industry?**

Congress recognized the continuing efficacy of self-regulation in the U.S. futures industry, under the oversight of the Commission, when it adopted the CFMA. The CFMA, and the Commission through its implementing regulations, replaced "one-size-fits-all" federal regulation with the Core Principle approach, which has facilitated the evolution of SRO business models and fostered competition, without reducing the effectiveness of self-regulation.

The CBOT and the other larger exchanges have successfully conducted their self-regulatory activities for many years through regulatory departments within the exchanges. Some smaller exchanges have outsourced their self-regulatory functions to the National Futures Association. The Securities and Exchange Commission ("SEC") has suggested other possible approaches that the securities industry might consider, including a variety of models that might exist within or outside of the corporate structure of the securities exchanges.[3] Each of these models may have advantages and disadvantages within the context of a particular marketplace considering, among other things, the size of the market, the nature of its products, the method of trading (*e.g.*, electronic, open auction, or both), the size and expertise of the exchange's own current or prospective staff, and the relative costs. Each exchange is ultimately in the best position to determine for itself which model is most appropriate for its own market, under Commission oversight.

The Commission has a long history of effectively exercising its oversight responsibilities, in part, through its staff's performance of regular exchange Rule Enforcement Reviews. Since the passage of the CFMA, Commission staff has continued to conduct such reviews to ensure that Designated Contract Markets ("DCMs") remain in compliance with the Core Principles. Over the years, these reviews have resulted in ongoing, constructive dialogue between Commission staff and staff of the exchanges, which has served to enhance the effectiveness of exchange self-regulatory programs.

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[3] Concept Release Concerning Self-Regulation, 69 F.R. 71256 (December 8, 2004).

On August 25, 2005, the Commission's Division of Market Oversight released a report on its most recent Rule Enforcement Review of the CBOT's audit trail, trade practice surveillance, disciplinary, and dispute resolution programs for compliance with related Core Principles.[4] The Division found that the CBOT had adequate audit trail, trade practice surveillance, disciplinary, and alternative dispute resolution programs, and made no recommendations for improvement with respect to any of these programs. Indeed, the Commission recognized the results of the substantial investments the CBOT has made to enhance the accuracy and detail of its audit trail and to develop sophisticated electronic surveillance tools to support its trade practice programs.

On April 22, 2005, the CBOT completed its demutualization, converting the organization from a nonstock, not-for-profit company with members into a stock, for-profit holding company with stockholders, CBOT Holdings, Inc. ("CBOT Holdings"), and a nonstock, for-profit exchange subsidiary, the CBOT, with members. On October 24, 2005, CBOT Holdings completed an initial public offering of approximately 6% of its Class A common stock, which is listed on the New York Stock Exchange ("NYSE").

The fact that the CBOT has become a wholly-owned subsidiary of a for-profit, publicly-held company has not compromised the strength of the Exchange's commitment to self-regulation. The public record reflects that the CBOT has continued to vigorously investigate and prosecute potential rule violations and that the Exchange's disciplinary committees have continued to impose sanctions where appropriate. Additionally, the CBOT has continued, and will continue, to devote significant resources to the maintenance and enhancement of its self-regulatory capabilities.

The CBOT believes that the present system of self-regulation is an effective regulatory model for all of the reasons discussed herein, and in the Exchange's September 30, 2004 comment letter filed with the Commission. Both Congress and the Commission have recognized that regulatory services may be effectively performed by exchanges themselves or by a third party regulatory services provider. Section 5(b)(6) of the Act; Appendix B to Part 38 of the Commission's Regulations. This flexibility should be retained, so that each exchange may determine the most appropriate and effective approach to perform its self-regulatory functions.

2. **As the futures industry adapts to increased competition, new ownership structures, and for-profit business models, what conflicts of interest could arise between:**

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[4] The review focused on Core Principles 10 (Trade Information) and 17 (Recordkeeping), which relate to an exchange's audit trail program for the recording and safe storage of trade information in a manner that enables prevention of customer and market abuses and enforcement of exchange rules; Core Principles 2 (Compliance with Rules) and 12 (Protection of Market Participants), which relate to an exchange's program for enforcing its rules, conducting disciplinary proceedings, and protecting market participants from abusive practices; and Core Principle 13 (Dispute Resolution), which relates to an exchange's alternative dispute resolution program for market participants.

(i) An SRO's self-regulatory responsibilities and the interests of its members, shareholders, and other stakeholders; and

(ii) An SRO's self-regulatory responsibilities and its commercial interests?

It would be incorrect to assume that an SRO's self-regulatory responsibilities, its commercial interests, and/or the interests of its members, shareholders, and other stakeholders will necessarily conflict with one another under a for-profit business model. The Exchange's enhancements to its audit trail for both electronic and open auction trades over the past two years provide prime examples of the convergence of regulatory, business and member and shareholder interests.

With the CBOT's transition to its new e-cbot® electronic trading platform in 2004, the Exchange delivered substantially improved speed, reliability and functionality to its customers and simultaneously developed its e-SMART system, which provided a significantly enhanced electronic audit trail and sophisticated new surveillance capabilities. Similarly, in 2005, the Exchange implemented the Denali system[5], which was designed to increase operational efficiency, facilitate near real-time risk management and reduce processing costs in the open auction environment. The Exchange's customers receive better service through the reduction of the turnaround time for accepting orders and recording, confirming and submitting trades for clearing purposes, and the consequent reduction in outtrades and errors. At the same time, corollary regulatory systems were developed based on the data generated within the Denali system to build a more accurate and comprehensive open auction audit trail that supports the trade practice surveillance conducted by the Exchange's regulatory staff. These initiatives clearly demonstrate how an SRO's commercial and self-regulatory interests often complement each other and simultaneously advance the interests of the Exchange's customers, members, and shareholders, and its self-regulatory function.

The commercial interests of a publicly traded, for-profit exchange are served by its diligent fulfillment of its self-regulatory responsibilities. We do not believe an exchange could succeed in attracting volume without an effective self-regulatory function. To the contrary, it is good business to maintain the integrity of the exchange. Potential participants are drawn to a market that treats them fairly, and on which they obtain prices determined by the fundamentals of the particular commodities and the liquidity of the market. The Exchange is not aware of any instances where an exchange that has become a publicly-owned entity has altered its self-regulatory behavior in a manner that adversely affected customers or other market participants.

The Exchange discussed its conflict of interest procedures in detail in its September 30, 2004 letter, as supplemented by this letter. The CBOT continues to believe that these

[5] The Denali system is a near real time electronic trade matching, endorsement and confirmation system for open auction trades executed through the electronic order routing system or wireless hand held technology.

procedures are more than adequate to address any conflicts of interest that might arise under its current publicly-traded, for-profit business structure.

3. **Given the ongoing industry changes cited above, please describe how self-regulation can continue to operate effectively. What measures have SROs taken thus far, and what additional measures are needed, to ensure fair, vigorous, and effective self-regulation by competitive, publicly-traded, for-profit SROs?**

A publicly-traded futures exchange has both an enhanced responsibility and a strong business motivation to ensure that its markets are regulated effectively in a manner that minimizes conflicts of interest. Self-regulation has continued to operate effectively subsequent to the demutualization and/or public offerings of the major U.S. futures exchanges or their holding companies, as the Commission's Division of Market Oversight has recognized in its recent Rule Enforcement Reviews. Nevertheless, SROs should and do continue to monitor the effectiveness of their self-regulatory programs on an ongoing basis, and make improvements where warranted or desirable, even in the absence of any noted shortcomings. The CBOT has taken a number of measures to ensure fair, vigorous, and effective self-regulation during the past several years, as described, in part, in response to Question 2 above.

By transitioning to a publicly-traded, for-profit structure, organizations, including futures exchanges, are required to focus on corporate governance and related matters, which improves the performance of a variety of functions, including self-regulation. At the CBOT, we have implemented an educational program, with the assistance of outside experts, for our Board of Directors, Board committees and management to review for them in detail governance-related topics, including SEC and NYSE corporate governance requirements, SEC reporting and internal control requirements, and fiduciary duties under state corporate law. We have also implemented policies and systems to ensure compliance with these requirements, which has strengthened governance and controls throughout our organization.

For example, the Board of Directors of CBOT Holdings has adopted a comprehensive Code of Business Conduct and Ethics that applies to directors, officers and employees of CBOT Holdings and of the Exchange. This Code is posted on the Exchange's website at http://www.cbot.com/cbot/pub/page/0,3181,2021,00.html and, among other things, prohibits Exchange employees from having any business, employment, or financial relationship with a member, member firm, or any other entity, which involves the trading of any CBOT products. The Exchange has also adopted an Employee Investment Policy, which is specifically designed to restrict investments by employees or their family members that may create a conflict of interest, or the appearance of a conflict of interest, and which prohibits employees generally from trading directly or indirectly in futures or options traded on the Exchange or in their underlying commodities.

The Code of Business Conduct and Ethics contains a "whistle blower" provision which prohibits directors, officers or other employees from taking retaliatory action against an employee because he or she has in good faith reported a suspected improper action regarding the Exchange's accounting, internal accounting controls, or auditing functions, any non-accounting/financial laws or regulations, or the Code of Business Conduct and Ethics itself or related Exchange policies. All CBOT employees have been given a confidential telephone number and web site where they can report suspected improper actions relating to accounting, internal accounting controls, or auditing. Any such complaints would be communicated confidentially to the Audit Committee of CBOT Holdings' Board of Directors, which consists solely of independent directors (as defined by both the SEC and the NYSE).

At the CBOT, there is a clear separation between the regulatory staff and the business staff. The Office of Investigations and Audits ("OIA") is headed by two Vice Presidents, one who oversees Financial Surveillance and Audits, and the other who is responsible for Investigations, Market Surveillance, and Regulatory Reporting.

In February 2005, the CBOT's Board of Directors adopted a formal OIA Confidentiality Policy and corresponding amendments to its regulations. This Policy clearly defines and codifies the Exchange's policies to ensure that Confidential Information[6] obtained by OIA for regulatory purposes may not be disclosed to any other Exchange employees or other persons for any purposes that do not relate to regulation or risk management. The Policy is posted on the Exchange's website at http://www.cbot.com/cbot/pub/page/0,3181,1204,00.html, and all OIA employees and any OIA consultants are required to sign it, to indicate their understanding and agreement to abide by its requirements. Similarly, Exchange Regulation 170.02 (a) provides that:

> [a]ll information obtained by [OIA] regarding the market position of an identified individual or firm or the financial condition of an identified individual or firm, which has been submitted to, or obtained by, the Exchange for regulatory purposes, shall be considered confidential, and [with limited exceptions set forth in paragraph (b)], shall be disclosed only to authorized employees and committees of the Exchange or its Clearing Services Provider for regulatory or risk management purposes, ...

4. What is the appropriate composition of SROs' boards of directors to ensure the fairness and effectiveness of their self-regulatory programs?

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[6] Confidential Information is specifically defined to include market positions of identified individuals or firms obtained from large trader reports; non-public financial records and reports relating to identified individuals or firms, obtained or generated in connection with financial examinations or financial surveillance; and source documents for trades, account documents and non-public financial information obtained, and reports generated, in connection with routine market and trade surveillance or investigations of possible rule violations.

5. Should SROs' boards include independent directors, and, if so, what level of representation should they have? What factors are relevant to determining a director's independence?

An SRO may have a fair and effective self-regulatory program under a number of different governance structures. The CBOT believes that an SRO board should generally include SRO members or market participants, and directors who are defined as non-member directors, public directors, or independent directors. However, the specific composition of the board of directors which will meet the needs of, and be most effective for, carrying out the self-regulatory programs of any particular SRO will depend on many factors, including the nature of the market and its participants, whether the SRO is mutually owned or demutualized, and whether it has public shareholders and is thus subject to the requirements of the market where it is listed. In all circumstances, however, the CBOT believes that industry experience and knowledge is essential in carrying out the functions of an SRO board.

SROs whose shares are listed on the NYSE or other securities markets are subject to the relevant listing standards, which impose particular board composition requirements and define "independent directors." For example, the NYSE's listing standards require that listed companies must have a majority of independent directors, and provide that a director may only be considered independent if the board of directors affirmatively determines that such director has no "material relationship" with the listed company. In particular, the listing standards identify certain employment, compensation, or other financial relationships with the listed company that would not permit a director to be considered independent. Section 303A.02 of the NYSE Listed Company Manual. The NYSE's listing standards do not preclude a finding that a director that is a member and/or a shareholder of an SRO is independent. Section 303A.02(a) explicitly states that "[h]owever, as the concern is independence from management, the [New York Stock] Exchange does not view ownership of even a significant amount of stock, by itself, as a bar to an independence finding."[7] The CBOT is in compliance with these standards. The CBOT also evaluates the effectiveness of its Board and Board committees and its corporate governance policies on an ongoing basis.

The CBOT believes that the flexibility included in existing stock exchange listing standards is valuable in allowing SROs to achieve the best blend of expertise and independence. The board of directors of a major futures exchange like the CBOT, with sophisticated electronic trading and order routing systems, diverse product offerings, and global operations, must possess a broad range of skills and business experience. When the CBOT Holdings' Nominating Committee considers potential Board candidates, it seeks to ensure that the best mix of skills and backgrounds is represented, and to ensure

[7] Any suggestion that a member of an exchange should not be considered independent because the member may be subject to disciplinary powers of exchange management and staff is mooted by the types of checks and balances discussed in response to Question 8. At the CBOT, exchange staff does not currently serve on disciplinary committees or impose disciplinary penalties.

that the Exchange will be able to meet both its business and regulatory needs, while minimizing potential conflicts of interest. In particular, it is essential that the board of directors of a futures exchange have significant futures industry experience, including an in-depth understanding of the business, financial, technology and regulatory aspects of firms that handle customer and proprietary futures business.

6. **Should self-regulation be overseen by an independent entity within an SRO?**

   (i) **If so, what functions and authority should be vested in such an entity?**

   (ii) **At least two futures exchanges have implemented board-level regulatory oversight committees ("ROCs") to oversee their regulatory functions in an advisory capacity. Commenters are invited to address any strengths or weaknesses in this approach.**

As the Commission has noted, certain futures exchanges have created board-level regulatory oversight committees ("ROCs"), composed solely of independent, non-member directors to oversee their regulatory functions in an advisory capacity.

The CBOT believes that an SRO should provide for the review of its regulatory functions on an ongoing basis. The creation of an ROC made up of a majority of, or solely of, independent directors, however defined, is one possible means of fulfilling these responsibilities, but it is not necessarily the only effective approach. Currently, the manner in which a particular SRO determines and reviews its regulatory budget, makes decisions regarding personnel and compensation of regulatory staff, and ensures the effectiveness of its compliance and disciplinary programs is determined by the SRO, subject to the CFTC's oversight.

For example, the CBOT has had a Regulatory Compliance Committee for more than fifteen years. This Committee currently consists of three independent directors (as defined by NYSE listing standards), as well as the chairmen of each of the Exchange's disciplinary committees and its Arbitration and Membership Committees. The CBOT's Regulatory Compliance Committee determines certain compliance policies, reviews related proposed rule changes, and makes appropriate recommendations to the Board of Directors. The Committee has been effective in fulfilling these roles because of the expertise of its members and the wealth of experience represented in administering the Exchange's disciplinary and other regulatory processes.

The senior regulatory officers of an exchange have particular expertise to make knowledgeable recommendations regarding their staffing and budgetary needs. Whether they make their recommendations to an independent ROC, which in turn makes recommendations to the board, or whether they make their recommendations directly to the board, or to the board through the exchange's chief executive officer, the board of directors will ultimately need to allocate funds to its regulatory function in a manner that

will serve the complementary purposes of ensuring compliance with Core Principles and enhancing its business reputation.

7. **The parent companies of some SROs are subject to the listing standards of the securities exchanges on which they are traded. Are such listing standards relevant to self-regulation and to conflicts of interest within DCMs?**

The Exchange's parent company is subject to the NYSE's listing standards. The CBOT believes that these listing standards not only serve to enhance the governance of the Exchange, but also help to ensure that the CBOT fulfills its self-regulatory obligations in an effective, transparent manner, which serves to minimize potential conflicts of interest in the performance of those obligations.

CBOT Holdings and the Exchange have identical Boards of Directors, which consist of a majority of independent directors, as defined in the listing standards of the NYSE, and as described in response to Questions 4 and 5 above. CBOT Holdings also complies with the NYSE listing standards that require that listed companies have audit, nominating/corporate governance and compensation committees that are composed solely of independent board members and that fulfill certain defined functions. Sections 303A.04 through 303A.07 of the NYSE Listed Company Manual.

CBOT Holdings also has adopted a Code of Business Conduct and Ethics, which is applicable to the CBOT, as described in the response to Question 3 above. In accordance with NYSE Listing Standards, CBOT Holdings' Code of Business Conduct and Ethics addresses a variety of important governance matters, including conflicts of interest, the improper use of corporate opportunities, confidentiality, fair dealing, protection and proper use of company assets, compliance with laws, rules and regulations, and the reporting of any illegal or unethical behavior. Section 303A.10 of the NYSE Listed Company Manual.

The NYSE's listing standards also require that listed companies adopt and disclose corporate governance guidelines regarding, among other things, director qualification standards, director responsibilities, director compensation, and annual board performance evaluations, and CBOT Holdings has done so. Section 303A.09 of the NYSE Listed Company Manual.

Although these listing standards may have been designed to protect the interests of the shareholders of public companies generally, they also serve to strengthen the governance of listed exchanges, minimize potential conflicts of interest in the self-regulatory process and protect the Exchange's customers.

8. **What is the appropriate composition of SROs' disciplinary committees to ensure both expertise and impartiality in decision-making?**

(i) **Should a majority of committee members be independent? Should the composition of SROs' disciplinary committees reflect the diversity of the constituency? Should similar safeguards apply to other key committees and if so, which committees?**

(ii) **Should SRO disciplinary committees report to the board of directors, an independent internal body, or an outside body?**

DCMs are subject to the Act's Designation Criteria 3 and 6, and Core Principles 2 and 12, which all address requirements that such exchanges enforce their rules and/or maintain effective disciplinary procedures. Sections 5(b)(3), 5(b)(6), 5(d)(2) and 5(d)(12) of the Act. None of these Designation Criteria or Core Principles requires that an exchange fulfill its disciplinary responsibilities through a committee mechanism, nor do they mandate how any such committees should be structured.

The CBOT believes that any SRO that enforces its rules through disciplinary committees should have flexibility to determine how such committees should be constituted so as to ensure expertise and impartiality. There is not necessarily a single structure that will fulfill these goals. An SRO's determination of the appropriate composition of any particular disciplinary committee may depend on the nature of the matters handled by that committee.

In order to ensure sufficient expertise, the CBOT's Financial Compliance Committee is made up of "qualified individuals, whether members or non-member employees of member firms." CBOT Rule 551.00. This provision permits individuals who have knowledge of futures-related accounting requirements and practices of member firms to serve on this committee, whether or not they hold their firms' memberships in their own names. By contrast, persons who are not, or have not been, recently employed in the futures industry would not have the specialized knowledge necessary to contribute meaningfully to the deliberations or decisions of the Financial Compliance Committee.

Disciplinary committees that include representatives of the various categories of members who appear before them have the experience necessary to determine whether violations have occurred and their consequences, and impose appropriate penalties. For example, brokers, traders and FCM representatives who are familiar with trading practices and recordkeeping requirements are in a unique position to quickly recognize how a broker may have mishandled a customer order and how his actions may be revealed by his trade documentation. Moreover, other brokers and exchange members want to ensure that there is appropriate discipline to correct abusive behavior and maintain the integrity of the exchange in a manner that will benefit all market participants.

The Exchange's conflict of interest regulation (Regulation 188.04) generally prohibits an individual from serving on a disciplinary panel that is considering a matter involving a person with whom the individual has a family, employment, or direct and substantial

financial relationship. In addition, CBOT disciplinary committee members routinely recuse themselves from their committees' deliberations not only when specifically required by this conflict of interest regulation but also in other circumstances where they think that there might be an appearance of possible bias. Furthermore, under CBOT Regulation 165.01, respondents are entitled to exercise one peremptory challenge (for no reason) to the presence of a member of an Exchange disciplinary committee impaneled to hear the matter and unlimited challenges for cause. The CBOT's experience with its disciplinary committees, no matter what the composition, has been that they take their responsibilities very seriously and strive to be as objective in possible in examining the evidence presented. In addition, the Exchange's disciplinary committees regularly seek to impose penalties that are consistent with other penalties imposed in similar cases.

The Commission has also requested comment with respect to whether SRO disciplinary committees should report to the board of directors, an independent internal body, or an outside body. There are numerous checks and balances built in to the disciplinary process at U.S. futures exchanges. At the CBOT, preliminary charges are issued by the respective disciplinary committees, depending on the nature of the violations alleged. In all adjudicated cases, except those involving potential minor penalties, disciplinary hearings are conducted by the Exchange's Hearing Committee. Disciplinary findings and sanctions imposed by any of these committees may be appealed to the CBOT's Appellate Committee. Finally, the Exchange's Board of Directors may exercise its discretionary authority to review a disciplinary case. After a respondent in a disciplinary proceeding has exhausted his appeal rights within the Exchange, and the Board has either reviewed the matter or chosen not to review the matter, the respondent may appeal an adverse decision to the Commission itself, and ultimately to the U.S. Court of Appeals. The CBOT believes that this process, which potentially involves six separate bodies, provides significant protection to individuals who are charged with violations of Exchange rules against any bias or conflict of interest that might possibly exist in the decision-making process.

9. **What information should SROs make available to the public to increase transparency (*e.g.*, governance, compensation structure, regulatory programs and other related matters)? Are the disclosure requirements applicable to publicly traded companies adequate for SROs?**

SROs should have flexibility in determining what additional information they will make available to the public with respect to its governance, compensation structure and regulatory programs, in addition to that which is already required by existing law and the disclosure requirements applicable to publicly-traded companies.

There are a number of SEC disclosure requirements that are applicable to shareholder-owned companies, and thus are applicable to the largest U.S. futures exchanges, including information regarding the compensation of directors and the extent of their

stock ownership, as well as certain business relationships.[8] For example, in the registration statements that CBOT Holdings filed with the SEC in connection with its offering of its Class A shares to CBOT members in the first phase of the Exchange's demutualization, and its subsequent initial public offering, detailed biographical information was provided about each Board member, his/her affiliation, membership status, length of service and committee membership. More extensive biographical information about the Exchange's Board members is available on the CBOT's website at http://www.cbot.com/cbot/pub/page/0,3181,946,00.html.

In addition, as described above in the response to Question 7, the NYSE's listing standards require that listed companies adopt and disclose detailed corporate governance guidelines. The CBOT's Corporate Governance Guidelines can be found at http://www.cbot.com/cbot/pub/page/0,3181,1118,00.html.

The names of the Exchange's disciplinary committee members are also available to the public, upon request. Other information posted on the CBOT's website includes the Exchange's Rules and Regulations (http://www.cbot.com/cbot/pub/page/0,3181,931,00.html), regulatory notices, biographical sketches of the Exchange's senior management (http://www.cbot.com/cbot/pub/page/0,3181,947,00.html), and the most recent annual report, including certified financial statements (http://www.cbot.com/cbot/pub/page/0,3181,2183,00.html).

The Exchange publicizes its final disciplinary actions by entering the information into the BASIC system, the National Futures Association's ("NFA") internet-accessible database, which serves as a central repository of information about disciplinary actions taken by all U.S. futures exchanges, the NFA, and the Commission.

An exchange may choose to publicly disclose certain information about its regulatory programs. The Commission itself also provides detailed general information about futures exchanges' regulatory programs to the public when it publishes its Rule Enforcement Review reports on its website. Any more specific information about surveillance programs is likely to be confidential, and public disclosure, which would necessarily include disclosure to persons who might become the subjects of relevant investigations, could compromise the effectiveness of those programs.

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[8] The SEC voted on January 17, 2006, to publish for comment proposed rules that would update and expand the disclosure requirements for executive and director compensation, related party transactions, director independence and other corporate governance matters, and security ownership of officers and directors, with respect to proxy statements, annual reports and registration statements.

10. What conflicts of interest standards, if any, should apply specifically to DCOs, both stand-alone DCOs and those integrated within DCMs?

The primary self-regulatory goal of a Derivatives Clearing Organization ("DCO") is to preserve the financial integrity of the clearing house, in part through ensuring the financial integrity of its clearing members. The Core Principles applicable to DCOs address, among other things, financial resources, participant and product eligibility, risk management, settlement procedures, treatment of funds and default rules and procedures. Section 5b(c)(2) of the Act. DCOs are also subject to a Core Principle regarding rule enforcement, and the Commission has stated in its Appendix A to Part 39 of its Rules (Application Guidance and Compliance with Core Principles) that DCOs should have "[a]rrangements and resources for the effective monitoring of compliance with rules relating to clearing practices and financial surveillance" as well as for the effective enforcement of such rules. The Core Principles applicable to DCOs do not specifically address conflicts of interest. DCOs should retain the flexibility to design those conflict of interest standards that they deem necessary in light of the fact that their primary reason for existence is to serve as the central counterparty in connection with futures and options transactions, and that their primary tool is effective risk management.

11. What conflict of interest standards, if any, should be applicable to third-party regulatory service providers, including registered futures associations, to ensure fair, vigorous, and effective self-regulation on their part?

At the time when Congress amended the Act to replace a rules-based approach with a Core Principle approach to the regulation of futures exchanges, it retained the detailed provisions of Section 17 of the Act that govern registered futures associations. Section17 addresses, among other things, board and disciplinary committee composition. Neither Section 17 of the Act, nor the Commission's Part 170 Regulations, specifically addresses conflicts of interest in the decision-making of a registered futures association. However, the CBOT believes that registered futures associations that are functioning as SROs (or any Commission-approved third-party regulatory service providers)[9] should be subject to no less onerous standards than those that the Commission applies to exchange SROs.

Conclusion

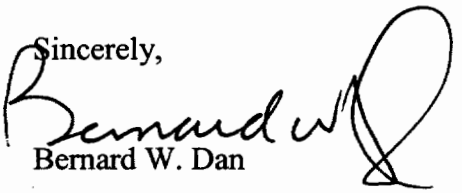
The Commission has demonstrated its continuing ability to effectively exercise its oversight responsibilities as market structures have evolved and competition has increased. While the Exchange does not believe that there is evidence that the emergence of publicly-owned exchanges over the past several years has raised any significant issues with respect to board composition and decision-making or the impartiality of exchange

[9] If the Commission were to consider permitting third parties other than registered futures associations or other registered exchanges to perform regulatory services, such a proposal should be the subject of a separate publication in the Federal Register and request for comments, and the CBOT is not addressing the permissibility of such an arrangement in this letter.

disciplinary processes, we recognize the importance of continuously evaluating our industry's evolution to ensure that our self-regulatory programs remain effective and appropriate. We appreciate the opportunity to participate in the ongoing dialogue between the Commission and the industry in an attempt to identify best practices with regard to the self-regulatory process.

If you have any questions about these comments, please feel free to call Anne Polaski, Assistant General Counsel, at (312) 435-3757.

Sincerely,



Bernard W. Dan