

**MINUTES OF THE NINTH MEETING OF THE COMMODITY FUTURES TRADING  
COMMISSION'S MARKET RISK ADVISORY COMMITTEE  
JANUARY 31, 2018**

The Market Risk Advisory Committee (MRAC) convened for a public meeting on Wednesday, January 31, 2018, at 10:00 a.m., at the U.S. Commodity Futures Trading Commission's ("CFTC" or "Commission") Headquarters Conference Center, located at Three Lafayette Centre, 1155 21<sup>st</sup> St., NW, Washington, DC. The meeting consisted of four panels. Panel 1 discussed the statutory framework, regulatory process, and Commission authority with respect to the listing of new products through self-certification on CFTC-regulated designated contract markets (DCMs) and swap execution facilities (SEFs). Panel 2 discussed the Commission's authority, oversight tools in connection with the risk management and surveillance of new products, and the oversight of intermediaries who facilitate trading in such products. Panel 3 discussed the self-certification process from the perspective of DCMs and derivatives clearing organizations (DCOs), including product design, the governance process for listing and clearing new products, and post-launch oversight. Panel 4 discussed the regulatory, legal, and policy issues related to listing novel products.

**MRAC Members in Attendance**

Biswarup Chatterjee, Global Head of Electronic Trading & New Business Development, Credit Markets, Citigroup

Jason Cohen, Chief Executive Officer, NEX SEF Ltd

Thomas Coyle, Vice President and General Manager, Chicago and Illinois River Marketing

Kathleen M. Cronin, Senior Managing Director, General Counsel & Corporate Secretary, CME Group

Jerry Jeske, Group Chief Compliance Counsel- Mercuria Energy, Representing Commodity Markets Council

Sebastian Koeling, Chief Executive Officer- Optiver, Representing Futures Industry Association- Principal Traders Group

Glen Mackey, Chief Risk Officer, NRG Energy

Kevin McClear, Corporate Risk Officer, Intercontinental Exchange, Inc.

Dennis McLaughlin, Group Chief Risk Officer, LCH.Clearnet

Susan McLaughlin, Senior Vice President, Federal Reserve Bank of New York

Dale Michaels, Executive Vice President, Financial Risk Management, The Options Clearing Corporation

Richard Miller, Consultant, American Council of Life Insurers

Michael Modlock, Head of TriReduce North America, TriOptima

Angela Patel, Senior Vice President, Putnam Investments

Edward Pla, Managing Director, Head of Clearing and Execution, UBS Investment Bank, Representing Futures Industry Association

Marnie Rosenberg, Global Head of Clearing House Risk & Strategy, JP Morgan

Dr. Marcus Stanley, Policy Director, Americans for Financial Reform

Robert Steigerwald, Senior Policy Advisor, Financial Markets, Federal Reserve Bank of Chicago

Kristen Walters, Global Chief Operating Officer of Risk and Quantitative Analysis Group, BlackRock

Rana Yared, Managing Director, Goldman Sachs

Luke Zubrod, Director of Risk and Regulatory Advisory Services, Chatham Financial

Scott Zucker, Chief Administrative Officer, Tradeweb

**Invited Speakers and Panelists in Attendance**

Paul M. Architzel, Facilitator, WilmerHale LLP

Julie Winkler, Chief Commercial Officer, CME Group

Christopher Concannon, President and Chief Operating Officer, Cboe Futures Exchange, LLC

Trabue Bland, ICE Futures U.S., Inc., President

Albert S. Kyle, Charles E. Smith Chair Professor of Finance, University of Maryland Robert H. Smith School of Business

Kari S. Larsen, Counsel, Reed Smith LLP

**CFTC Commissioners and Staff in Attendance**

J. Christopher Giancarlo, Chairman

Rostin Behnam, MRAC Sponsor and Commissioner

Brian D. Quintenz, Commissioner

Alicia L. Lewis, MRAC Designated Federal Officer (DFO)

Brian Bussey, Director, Division of Clearing and Risk (DCR)

Daniel J. Davis, General Counsel, Office of the General Counsel (OGC)

William Heitner, Acting Deputy Director, Division of Clearing and Risk (DCR)

Matthew Kulkin, Director, Division of Swap Dealer and Intermediary Oversight (DSIO)

James McDonald, Director, Division of Enforcement (DOE)

Amir Zaidi, Director, Division of Market Oversight (DMO)

**I. Opening Remarks**

Ms. Alicia L. Lewis, MRAC DFO and Acting Chair of the Committee, called the meeting to order, gave welcoming remarks, and introduced Chairman J. Christopher Giancarlo, Commissioner Brian D. Quintenz, and Commissioner Rostin Behnam, who all gave welcoming remarks. Chairman Giancarlo, in his remarks, stated that MRAC would be discussing the product self-certification process under Part 40 of the Commission's regulations. He added that the product self-certification framework gives DCMs the ability to design and certify new products, but does not provide for public input. However, he noted that those entities using the self-certification process will be asked to disclose steps to gather such input. In addition, the Chairman asked Commission staff to take a closer look at DCO governance rules regarding clearing of new virtual currency products, and formulate recommendations for possible further action regarding those rules.

Commissioner Quintenz agreed with Chairman Giancarlo's views on self-certification of new financial products. He emphasized that regulators cannot remove all financial risk from the markets. However, he noted that following self-certification, CFTC staff performs daily surveillance, new rule reviews, and regularly performs market-wide and clearinghouse-level stress tests. Commissioner Quintenz added that the Commission continually monitors risks assumed by Futures Commission Merchants' (FCMs) positions, and is always receptive to hearing the public's concerns.

Commissioner Behnam thanked all for attending and noted the timeliness of the meeting following the introduction of two Bitcoin futures contracts. He further stated that it is critical that the CFTC: (1) engage with industry in addressing risk regarding new products, (2) provide legal and regulatory certainty to the market, (3) educate the general public, and (4) question and challenge the status quo in the market and within the Commission.

Commissioner Behnam noted the criticism the CFTC received for not holding public hearings prior to the self-certification of Bitcoin futures. He commended CFTC staff for then developing a heightened review standard—within the limits of the self-certification standard—in response to the criticism. Commissioner Behnam noted that this review was conducted to determine whether the Bitcoin futures products comply with an exchange’s obligations under the CEA core principles, CFTC regulations, and related guidance. The Commissioner stated that the need for the heightened review, demonstrated that the Commission must reconsider its historical regulatory approach to new products, which may require a more formal process. He also stated that self-certification is a unique process that has served market participants, the CFTC, and the general public very well, and that any action above and beyond that must be subject to Commission action in a transparent forum.

## **II. Panel I: Overview of Self-Certification for Products**

Mr. Paul Architzel, the meeting facilitator, gave opening remarks, and introduced the three panel members—Mr. Daniel J. Davis, Mr. Amir Zaidi, and Mr. Brian Bussey.

Mr. Davis described the history of the product approval process leading up to, and including, self-certification, which was introduced by the Commodity Futures Modernization Act of 2000 (CFMA). Mr. Davis stated that prior to the year 2000; every product had to be submitted to the Commission for action, but that the CFMA changed the standard for product review and for rule review, most notably adding time limitations for completion of the review. Mr. Zaidi stated that DMO focuses its review on compliance with Core Principles 3 (Manipulation), 4 (Monitoring), and 5 (Information). He also commented that DMO’s mandate does not allow for daily determinations of the underlying markets viability, but that it does seek to assure that new products are not readily susceptible to manipulation. Mr. Bussey discussed the significance of a firm being designated as a “Systemically Importance Derivatives Clearing Organization” (SIDCO), under Regulation 40.10, stating that only two DCOs currently have the designation—CME and ICE Clear Credit.

Mr. Architzel asked the panel for more information on the formal versus the informal approval process. Mr. Bussey described the informal process that includes stress and liquidity testing, and on-site examinations, which are done every year for SIDCOs. Mr. Zaidi also commented on the self-certification process.

Questions and comments came from the committee members. Mr. Biswarup Chatterjee, Ms. Marnie Rosenberg, and Ms. Kristen Walters asked how protections for new products are assured, the process for allowing for public comment (and when public comment is mandatory), and when it’s necessary to move from an informal to a formal process for approval of a new product like Bitcoin, requiring Commission review. Ms. Kathleen Cronin commented that the

informal review process has worked and that a formal process would impose more burdens on industry staff. Both Mr. Davis and Mr. Bussey explained when a more formal review process is appropriate. Mr. Zaidi stated that a formal review process is not being considered, but that the Commission does examine a product's susceptible to manipulation.

Mr. Architzel asked for a description of the review process that the Commission uses prior to a new product being launched under Section 5c(c). Mr. Davis explained the process. Dr. Marcus Stanley asked about the Commission's use of its regulation 40.10 authority, and about manipulation. Mr. Bussey stated that regulation 40.10 use is not the standard. Mr. Zaidi responded that an examination of market settlement should occur before changing review standards. Others emphasized that market protections are in place to address any potential risks.

### **III. Panel II: New Products from a Risk Perspective**

The second panel involved a discussion of the Commission's authority and oversight in connection with the risk management and surveillance of new products, and consisted of Mr. Bussey, Mr. William Heitner, Mr. Matthew Kulkin, and Mr. James McDonald. Mr. Bussey described the pre- and post-launch review process, the importance of on-site examinations, and the process covering SIDCOs. He explained that the focus for pre-launch discussion is on margin, risk surveillance, and compliance with core principles.

Mr. Heitner described the surveillance process within DCR covering new product margin reviews, and risk management. He stated that DCR tests product benchmarks, monitors product performance, and margin adequacy. For Bitcoin, Mr. Heitner stated that the Commission examines risks and stress tests, and that, so far, risks associated with Bitcoin have been relatively small compared to other products. Mr. Kulkin commented that DSIO is tasked with assuring compliance with Commission rules regarding segregation of customer funds, noting that staff works with the National Futures Association and CME to assure that new contracts comply with Commission rules. Mr. McDonald commented that surveillance activity has been moved into DOE, allowing DOE to enforce market integrity, provide a quick response to various forms of misconduct, and maintain an open line of communication with the exchanges.

Mr. Architzel asked the panel to explain the value of the pre-launch versus the post-launch review process. Mr. Bussey emphasized that there is a continuous process of product review and monitoring. Next, in response to a question about monitoring the spot market, Mr. McDonald stated that DOE looks for fraud and manipulation by doing surveillance.

Questions were raised about examining risks associated with new products, and margin models in regards to volatility. Mr. Bussey responded that, with regard to Bitcoin, the Commission looked at margin data submitted by the CME, and was confident with the level of margin erosion prior to the CME's launch of Bitcoin. Ms. Cronin commented that the CME was very conservative in setting the margin requirements for Bitcoin. In response to a question regarding FCMs' assessing the risks of new products, Mr. Kulkin stated that the Commission continuously dialogues with FCMs to assure that FCMs are engaged with their customers.

### **IV. Panel III: Futures Exchanges and New Products**

The third panel consisted of a discussion of the self-certification process from the perspective of DCMs and DCOs. The panel speakers were Ms. Julie Winkler, Mr. Christopher Concannon, Mr. Trabue Bland, and Mr. Dale Michaels. Ms. Winkler described the product launch process from the perspective of the CME and explained its interactions with market participants and risk management of a product. She stated that a product must meet CFTC core principles and explained the process to accomplish that goal. Mr. Michaels described OCC's risk management process for new or novel products, which involves stress testing and default management.

Mr. Architzel asked the panel to describe how the exchanges gather public (client/FCMs) input on new products. Mr. Concannon commented regarding his firm- CBOE, that public input occurs because his company is publically traded. Ms. Winkler stated that the CME received client input on Bitcoin for over two years prior to launch. Mr. Bland stated that without customer interest, a product is not listed.

Mr. Architzel then asked if there is a role for the Commission to provide input regarding the structure and method for stakeholder validation of new products before they are submitted to the Commission, under the self-certification process. Mr. Concannon stated that the CFTC provides feedback during review under the self-certification process.

Mr. Architzel asked the panel to discuss press reports that suggested that perhaps certain types of contracts should be subject to a separate clearing fund, and whether it's being considered. Mr. Michaels stated that his company decided that a single clearing fund was best after examining the volatility of the product. Ms. Winkler stated that, for the CME, currently, the base margin being collected for Bitcoin futures is covering the risk.

Next, Mr. Architzel asked, in regards to futures, whether there were any novel contracts that should be split out into a separate guarantee fund. Panel members commented that contract specifics would need to be examined to make that determination. Ms. Winkler stated that there is daily surveillance for Bitcoin futures.

Mr. Glen Mackey asked how do the companies think about cryptocurrencies where the underlying market is unregulated and other commodities where the underlying marker is regulated. Mr. Concannon responded that that issue was discussed with the CFTC and that they have information sharing agreements with the various crypto markets. Mr. Chatterjee asked the panel to explain the basis for the adverse reaction to self-certification of Bitcoin. Panel members responded that, to address such issues, stakeholders need to be involved in forums that address the issue; that industry should proactively explore some of the unintended consequences of such products; and that markets have to be prepared for digitization.

Mr. Edward Pla asked the panel to discuss what the various exchanges think about the adequacy and the diversity of their clearing member set, and whether they can support it in a crisis. Members responded that default member testing procedures are a key part of their contracts, and that any clearing member can reject a trade, including Bitcoin, from any other firm.

Chairman Giancarlo departed the meeting before the start of Panel IV. He offered closing remarks, praising the work of his fellow Commissioners and Commission staff. The Chairman also offered appreciation for the dialogue offered by the advisory panel and participants.

#### **V. Policy & Regulatory Approach for Novel Products**

The last panel discussed the regulatory, legal, and policy issues related to listing novel products. The panel speakers were Mr. Albert Kyle, Mr. Pla, and Ms. Kari Larsen. Mr. Kyle discussed how difficult it is to determine who ultimately owns Bitcoins, and that the fundamentals of supply and demand aren't present. Mr. Pla stated that the launch of Bitcoins would have benefitted from more two-way dialogue from the clearing firms. Ms. Larsen commented that novel products can present novel issues, and that differences between the key players should be resolved.

Mr. Architzel asked if the current self-certification process is appropriate for new and novel contracts, and whether heightened review is necessary. Panel members responded that volatility may be an indication of poor liquidity; however, one panel member expressed the view that a lot of the products are volatile, which is why there are futures contracts on those products. Other panel members questioned if the CFTC would have the capability and expertise to resolve problems resulting from a new, novel product; others questioned how such a product would be defined and whether such new products should be examined through the same risk perspectives as the exchanges.

Finally, Mr. Architzel asked the group to comment on what is an optimal process for an SRO processing new products, and the optimal process for CFTC oversight for new products both pre- and post-launch. Panel members responded that member input is important; that receiving feedback from customers is important; and that the CFTC needs to be aware that open interest may not reflect what is happening in the market.

#### **VI. Closing remarks**

Commissioner Quintenz thanked the attendees for participating, stating that the Commission is seeing in the market now digital commodities being created on a daily basis. Commissioner Behnam stated that self-certification is a big issue, but that it has worked well and that he hopes it continues. He also added that, although there is room for improvement, good products have been launched and that the Commission needs to be sure that the core principles are followed.

Ms. Lewis adjourned the meeting at 3:55pm.

I hereby certify that the foregoing minutes are accurate.

  
Alicia L. Lewis  
Acting Chair and Designated Federal Officer

11/17/18  
Date