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COMMENT

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January 23, 2006

VIA ELECTRONIC DELIVERY

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

Re: Self-Regulation and Self-Regulatory Organizations

Dear Ms. Webb:

The Chicago Mercantile Exchange Inc. ("CME") welcomes the opportunity to comment upon the Commodity Futures Trading Commission's ("CFTC" or "Commission") ongoing review of self-regulatory organizations ("SROs"). CME invented financial futures contracts more than 30 years ago and is currently the largest and most diverse financial exchange in the United States and the largest derivatives clearing organization in the world. CME is also the largest demutualized and publicly-traded futures exchange in the United States.[1]

CME has a long history and strong track record in self-regulation. As one of the leading exchanges in the world, we believe that our market surveillance and financial supervision regulatory capabilities are part of the brand identity that we have created. In serving the marketplace, CME has stressed the quality and strength of its regulatory capabilities as an attraction to our products, markets and services. Market participants use our markets, in part, because they know we operate with high standards for market integrity and for supervision of trading activity and financial activity on the part of our member intermediaries.

As the Commission has requested, we have addressed each enumerated question individually, in the order that they appear in the release.

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[1] All of CME's outstanding shares are held by Chicago Mercantile Exchange Holdings Inc. ("CME Holdings"), a Delaware for-profit corporation. CME Holdings completed its initial public offering in December 2002 and its Class A common stock is listed on the New York Stock Exchange (the "NYSE") and The NASDAQ National Stock Market, Inc. ("NASDAQ"). The Board of Directors of CME Holdings and CME are comprised of the same individuals.

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

CME Response: CME believes that its model of self-regulation, in which a demutualized market center and regulatory function exist within the same entity, is effective and time-tested. Such a model represents the best model for the following reasons:

A. CME's Public Company Model Creates an Incentive to Regulate

CME's transition from a member owned exchange to a public company has created substantial additional incentives to operate a fair, financially sound and competitive marketplace. Reputation and competition are powerful motivating forces for ensuring proper behavior, especially in today's global environment where market participants have virtually immediate, around-the-clock access to a broad range of competing markets and products.

Moreover, publicly owned exchanges have a unique incentive to properly discharge their statutory self-regulatory responsibilities. Such exchanges operate in a transparent environment in which research analysts and institutional shareholders scrutinize management's business decisions and monitor the company's performance. Any failure to maintain and effectively implement prudential regulatory programs could cause analysts and shareholders to adopt a negative view of performance and stock prices would likely be adversely impacted. Indeed, the results of any materially adverse agency action involving the market would require disclosure to shareholders.

Ultimately, CME believes that our regulatory capabilities are part of the brand identity that we have created. The quality and strength of our regulatory capabilities provide market participants with the confidence to use our products, markets and services.

B. Commission Oversight Ensures Compliance

The Commodity Exchange Act (the "Act") and Commission regulations currently impose strict self-regulatory responsibilities on all SROs, which include the requirement that SROs enforce all of their rules and maintain continuing programs to ensure compliance with the Act, the Commission's regulations and the SRO's rules. The CFTC helps to ensure that exchanges satisfy their self-regulatory responsibilities through, among other things, periodic rule enforcement reviews that ferret out lax or deficient enforcement. In the event that an SRO fails to satisfy its obligations, the Commission is empowered to compel the SRO to fulfill its responsibilities, and may suspend or revoke the SRO's designation. We believe that these measures are appropriate and adequate to supervise and enforce an exchange's self-regulatory responsibilities.

C. Funding of the Self-Regulatory Function Is Not Diminished

CME has a strong incentive to adequately fund and ensure the integrity of its markets. CME has, in fact, continued to devote significant resources to self-regulation since going public.

Any notion that an established for-profit entity might attempt to attract order flow or increase its profits through lax self-regulation would be misplaced. In this respect, we note that Professor Craig Pirrong of the University of Houston has found that a for-profit SRO, as opposed to a not-for-profit SRO, would generally not have an incentive to attract volume or increase its profits through lax self-regulation.[2] According to Professor Pirrong, because "most of the attributes of exchange self-regulatory efforts have observable and often quantifiable impacts," the for-profit form creates a strong incentive to regulate intensely, while the not-for-profit form "is likely to have little impact on the intensity of exchange self-regulatory efforts."[3]

Operating as a for-profit company thus impels CME to further strengthen its brand through effective self-regulation.

D. Combined Knowledge of Market and Regulation Creates Benefits

CME, as well as other exchanges, have built extensive and sophisticated regulatory systems and programs to ensure market integrity and financial safeguards for market users. CME has assembled some of the most talented regulatory, risk management and financial supervision experts in the world of trading. These employees oversee our market regulation department, financial audit area, risk management and clearing house departments and trading floor personnel. Importantly, our Market Regulation Department employees have an average of approximately eight years of departmental experience and 17 years of industry experience. Our Audit Department includes 17 employees who have Certified Public Accountant designations, and a management group whose employees average 13.5 years of departmental experience. The quality of our overall regulatory system depends heavily on the integration of these separate functions and on the manner in which these staff members are able to coordinate closely their activities and information sharing. Unbundling any part of this extensive and intertwined system will damage the protections afforded to the industry and market participants.

In times of a market crisis, these staff members work together as a tightly knit team that is responsive to CME's needs to ensure market integrity and financial safeguards. Emergency situations demand the highest level of coordination.

A prime example of an emergency situation involves the recent bankruptcy filing by Refco, Inc., the parent company of Refco, LLC ("Refco"), a large clearing member of CME. As a result of the alleged fraudulent activities of its chief executive officer, Refco Inc. was forced to seek bankruptcy court protection through a Chapter 11 filing. While Refco Inc. was in bankruptcy, its Refco subsidiary continued to operate as a clearing member in good standing at CME.

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[2] *See* Craig Pirrong, A Theory of Financial Exchange Organization, 43 J. of Law & Econ. (2000); Craig Pirrong, Electronic Exchanges are Inevitable and Beneficial, 22 Regulation (1999).

[3] Letter of Craig Pirrong, Professor of Finance and Director of the Global Energy Management Institute, Bauer College of Business of the University of Houston, to Jean A Webb, Secretary, Commodity Futures Trading Commission (Sep. 13, 2004).

During the several weeks that Refco continued to operate after its parent company was in bankruptcy, CME, as the designated SRO for Refco, brought together in-house experts from various CME departments to work with the industry and the CFTC in an effort to monitor the trading activity of Refco and to analyze and discuss the future of Refco. In addition, in the event that a worst case scenario arose involving Refco, CME explored, discussed and developed a comprehensive contingency plan for a large clearing member default if a sale to another party did not occur and Refco was forced into bankruptcy.

According to many sources within the industry, CME and its staff were instrumental in managing the Refco situation to a positive result. CME auditors, who have worked with Refco for years and were intimately familiar with Refco's operations, were on-site at Refco the day after Refco, Inc.'s financial problems were made public. The on-site auditors coordinated with the CME audit staff in Chicago as well as the CME clearing house staff and market regulation, membership and legal staff to monitor and assess the ever-changing Refco situation. Information was provided immediately by CME staff to the entire industry, allowing money flows to and from Refco to continue and allowing the clearing member to stay in business while its parent was in bankruptcy. If the information had not been provided by CME staff to the rest of the industry, daily movement of funds to and from Refco would likely have stopped and many of the approximately 24,000 customers would have had their trading accounts and funds placed in jeopardy.

CME's long-standing familiarity with Refco, the trust and personal relationships that have been built over the years between CME staff and Refco staff, and the ability to have Audit, Clearing House, Market Regulation and Surveillance, Membership and Legal staff all in close proximity and on-hand immediately sharing the same information, allowed a potential crisis to be resolved in a positive manner for Refco's customers and the futures industry. CME's development of sophisticated regulatory, margining and auditing systems over the years came into play during the Refco situation. CME's ability to use its systems and analyze the resulting data in an immediate response to Refco, assisted in information flowing to the industry and the clearing member staying in business until a sale to a third-party could be arranged.

As the Refco matter demonstrates, CME has a strong incentive to regulate vigorously and monitor its member firms in order to maintain a robust industry and, through its combined market and regulation model, CME has shown that it is unequivocally equipped to address such emergencies. To alter such a model in the face of the Refco success could risk the integrity of the industry.

E. International Acceptance Demonstrates Model's Success

The demutualized, publicly-traded exchange model is internationally accepted. As a publicly-traded exchange, CME is not alone in effectively combining its market center and self-regulatory functions. Internationally, for example, demutualized exchanges such as Euronext, N.V. (through its various markets), the Singapore Exchange (SGX), OMX (through its Stockholmsborsen market), and the London Stock Exchange (LSE), all employ a model that generally combines the market center function with the self-regulatory function. The broad acceptance of such a model, combined with the absence of any demonstrable failures, provides

strong evidence that the model effectively permits demutualized exchanges to satisfy their self-regulatory obligations.

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

   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?**

CME Response: In the context of a demutualized, publicly-traded exchange, CME does not believe that conflicts of interest are inherent or likely to arise between the self-regulatory function and the interests of members, shareholders, stakeholders or profits. To the contrary, for the reasons discussed above, CME believes that a demutualized, publicly-traded exchange has a strong incentive to obviate conflicts of interest and ensure that markets are fair and credible.

Moreover, by taking affirmative steps to reduce the potential for conflicts, such as increasing the representation of independent members on our board of directors and disciplinary committees and chartering a board-level Market Regulation Oversight Committee ("MROC"), comprised of non-industry directors, to oversee the self-regulatory function, CME has consistently demonstrated an unparalleled commitment to a marketplace free of conflicts.

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

CME Response: We believe that the continued movement toward demutualization will continue to drive more effective self-regulation, in that exchanges will have a stronger incentive to ensure market integrity.

With respect to measures that SROs have taken to ensure effective self-regulation, CME has been at the forefront to ensure that self-regulation is fair, vigorous and effective. For example, in April, 2004, CME became the first futures exchange to appoint a board-level MROC devoted to self-regulatory oversight. MROC, which operates independent of management and the Board of Directors and has access to outside counsel, is charged with reporting to the full Board of Directors on an annual basis concerning the independence of CME's regulatory functions from CME's business operations, the independence of CME management and regulatory personnel from improper influence by industry directors regarding regulatory matters, and CME's compliance with its statutory self-regulatory responsibilities. MROC's charter helps to ensure that the self-regulatory function is fair and free of conflicts of interest. (MROC's specific responsibilities are discussed in response to Question 6 below.)

CME has also strengthened its disciplinary process—and mitigated any perceived conflicts—by increasing the representation of independent members on its chief disciplinary committees—the Business Conduct Committee ("BCC") and Probable Cause Committee ("PCC"). As discussed more fully in response to Question 8, these committees now include substantial non-member representation to ensure that such independent members have significant input in disciplinary proceedings.

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

CME Response: CME does not believe that there is a "one-size-fits-all" approach with respect to composition requirements for effective self-regulation. At CME, we strive to ensure the fairness and effectiveness of self-regulation through a combination of governance initiatives, which include taking steps to ensure that our Board operates independently of management by having at least a majority of independent directors and providing additional assurances that our SRO functions are being administered on a fair and consistent basis through the independent oversight of MROC. In addition, we believe that it is important to have significant non-industry representation on the Board because such directors add important perspectives, such as public company and financial expertise and unqualified neutrality on issues that might impact various classes of our market users. CME's Board is currently comprised of seven non-industry directors (out of 14 directors nominated by the Board).

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?

CME Response: CME believes that boards of directors should be comprised of at least a majority of independent directors. CME has both advocated and implemented such a position, which is consistent with accepted corporate governance "best practices" regarding board composition.

CME does not, however, believe that there is a bright-line definition of "independence" that can ensure that a board functions effectively and independently. We do recognize that the inclusion of directors with no other relationships to the industry on the boards of SROs is important to mitigate any perceived conflicts of interest. However, we also believe that directors who are members or end-users of an exchange organization have an invaluable understanding of the business and can provide useful perspectives on significant risks and competitive advantages. Indeed, the inclusion of exchange members on CME's Board has been essential in transforming CME from a century-old mutual organization to a thriving publicly-traded company and from a largely floor-based open outcry business to one of the largest electronic trading platforms in the world. We would be concerned about the adoption of any bright-line standard that would automatically prohibit a board from finding a member of an exchange organization to be independent regardless of the particular facts and circumstances his or her relationship with the exchange. Such a requirement would prohibit all members from serving on key board committees and would result in exchanges losing the benefit of their insight without

the benefit of any analysis as to whether the use of our markets actually impairs a particular director's independence.

As set forth in our categorical standards of independence (available at www.cme.com), we believe that as long as a director satisfies the independence requirements of the NYSE and NASDAQ listing standards and our categorical independence standards relating to affiliations with charitable organizations, consulting services and share ownership, his or her independence will not automatically be impaired based on membership status so long as their transactions as members are made in the ordinary course of business on terms consistent with those prevailing at the time for corresponding transactions by similarly situated, unrelated third parties.

Furthermore, CME believes that it should be the responsibility of the board to determine whether, based on all the facts and circumstances, including the level of trading activity and influence of the particular member, as to whether he or she is independent of the exchange. State corporation laws generally require a board to exercise its business judgment to act in what it reasonably believes to be in the best interests of the company and its shareholders regardless of a director's status as a member of the organization. Directors must fulfill their responsibilities in a manner that is consistent with their fiduciary duty to their owners, in compliance with all applicable laws and regulations. We believe that rather than a blanket independence standard regarding membership, a comprehensive conflicts of interest policy is more appropriate to address any potential conflicts of interest that may arise due to an individual's trading activities. For example, CME keeps records as to the trading activities of its directors, if a matter is presented to the Board that could have a significant impact on a director's trading, that director is expected to recuse him or herself from the matter. (The foregoing procedures are set forth in more detail in the Company's Director Independence and Conflict of Interest Policy available at www.cme.com.)

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.

CME Response: CME does not believe that the self-regulatory function should be overseen by an independent entity within the SRO. Such a model is beset by several flaws:

First, if the board of an independent entity reports to the parent board of the company, conflicts—to the extent that they exist—would likely continue to persist because the regulatory function and the market center function would ultimately report to the same board of directors. Such an independent entity model would thus not improve upon any perceived conflicts of interest concerns.

Second, formally separating the regulatory function from the market center function could harm self-regulatory efforts because the separation could reduce the familiarity of the regulators with market practices. Such a forced division of expertise would hamper, rather than help, regulatory personnel in attempting to understand and regulate the market.

Third, in transferring the regulatory function to a separate entity, any synergy between the market center and the regulatory function could be jeopardized. In particular, as exchanges seek to innovate, their regulatory systems might not be as well designed for effective surveillance because the regulators may not have had the opportunity to provide input into the development and implementation of the technology.

Finally, requiring the establishment and maintenance of a separate entity would add an additional layer of bureaucracy to the organization, which would increase costs without any corollary benefit.

Rather than experiment with a proven model, we believe that the appropriate mechanism to ensure fair and effective self-regulation is through a regulatory oversight committee ("ROC"). At CME, the ROC (also referred to as the MROC) is comprised solely of non-industry directors and is charged with the following significant responsibilities:

- to review the scope of and make recommendations with respect to the responsibilities, budget and staffing of the Market Regulation Department and the Audit Department with the goal that each department is able to fulfill its self-regulatory responsibilities.

- to oversee the performance of the Market Regulation Department and Audit Department with the goal that each department is able to implement its self-regulatory responsibilities independent of any improper interference or conflict of interest that may arise as a result of a member of CME serving on the Board or participating in the implementation of CME's self-regulatory functions.

- to review the annual performance evaluations and compensation determinations and any termination decisions made by senior management of CME with respect to the Managing Director, Regulatory Affairs, and the Director, Audit Department, with the goal that such determinations or decisions are not designed to influence improperly the independent exercise of their self-regulatory responsibilities.

- to review CME's compliance with its self-regulatory responsibilities as prescribed by statute and the rules and regulations promulgated thereunder.

- to review changes (or proposed changes, as appropriate) to Exchange rules to the extent that such rules are likely to impact significantly the self-regulatory functions of the Exchange.

We believe that the MROC represents an aggressive and appropriate step towards independence in self-regulation. Importantly, the formation of the MROC represents a best-

practice model for exchange self-regulation, and we encourage the Commission to recognize, and other futures exchanges to follow, our lead.

7. The parent companies of some SRO's 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?

CME Response: Directors are required to oversee the company for the benefit of its shareholders. In taking action on behalf of the company, directors should be free from conflicts of interests to ensure that transactions are fair to the corporation and are made on an arms length basis. CME has taken steps to ensure that its Board acts independently by, among other things, complying with the independence standards of the NYSE and NASDAQ and instituting its Director Independence and Conflict of Interest Policy.

We believe that all corporations, including DCMs, would benefit from these policies. For example, the listing standards that apply to publicly traded companies are designed to raise the bar for corporate accountability by increasing the independence of the board of directors and its committees. Under the requirements, at least a majority of the directors must be free from material relationships with the company and certain of its committees must be comprised solely of independent directors. We believe that having a majority of independent directors and independent board committees provides additional assurance that a board will act independently of management and free from conflicts of interest.

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?

CME Response: CME believes that SRO disciplinary committees should have independent, non-SRO committee members. In this respect, CME has pioneered changes to the structure of its disciplinary committees. For example, non-members were added to CME hearing panels in 1990 and the degree of influence of non-members has been consistently expanded—most recently in 2004, when CME increased the proportion of independent panelists on its disciplinary committees.

Presently, CME's Probable Cause Committee (the "PCC"), which is the committee responsible for the issuance of charges involving allegations of trade practice violations, is composed of three non-members and four members, plus a non-voting member chairman. CME's Business Conduct Committee (the "BCC"), which is the committee that is responsible for

resolving such charges, is composed of two non-members and three members, plus a non-voting member chairman.

We believe that it is important that the level of representation for independent members is consistent across all types of disciplinary cases. While some exchanges use non-member panelists in the disciplinary process only when a case appears to involve customer harm, CME believes that independent, non-industry panelists are a useful component in *all* types of disciplinary cases before the PCC and BCC.

We further believe that ensuring that a disciplinary committee has the requisite level of expertise is best accomplished by encouraging members and users of an exchange's products to participate in the disciplinary process. Such individuals not only understand the nature and jargon of the futures business, but possess first-hand knowledge of the often complex and technical workings of the business. The result of such participation is that case resolutions are commensurate and responsive to the charges brought. In each non-summary proceeding, CME includes at least one broker, one local trader and one firm (*e.g.*, FCM) representative, thus ensuring a multitude of market perspectives. Based upon our feedback with the community that we serve, the level of market expertise is appropriate.

Moreover, impartiality is best accomplished by requiring SRO disciplinary committee members to abstain from participating in a disciplinary matter if there is a perceived or actual conflict of interest or the member has engaged in an *ex parte* communication concerning the merits of the matter. Importantly, CME Rules 416 (Conflicts of Interest) and 417 (Prohibited Communications), make it clear that CME will not tolerate violations of these important precepts.

Lastly, we do not believe that the CFTC should mandate a reporting requirement with respect to disciplinary committees. At least in the case of CME, an adequate oversight structure currently exists. The BCC and PCC chairmen, as well as the heads of the Market Regulation Department and Audit Department, have unfettered, *ex parte* access to the MROC to discuss any issue, including a potential conflict or concern. Moreover, at least once per year, the MROC meets with the BCC and PCC chairmen (and the heads of the Market Regulation Department and Audit Department), without CME staff or management present, to examine any potential conflict or concern, as well as to discuss the strengths and weaknesses of the disciplinary program. Finally, to the extent that a party to a disciplinary proceeding believes that it has been aggrieved by an inappropriate committee decision, the party is accorded ample recourse, which includes the right to appeal the decision to a hearing panel of the Board of Directors with respect to any decision that imposes a fine greater than $10,000 or a suspension greater than five business days, as well as recourse to the CFTC and federal court. Such a structure ensures independence with respect to the BCC's and PCC's role in the self-regulatory 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?

CME Response: As a public company, CME is subject to the disclosure and reporting requirements of the Securities Act of 1933, Securities Exchange Act of 1934 and the rules and

regulations promulgated thereunder by the SEC. In addition, CME is subject to the disclosure requirements of the NYSE and NASDAQ, which require CME to make publicly available on its website numerous corporate governance documents and provide annual certifications regarding its compliance with the listing standards.

In accordance with the foregoing rules and as a matter of best practice, CME makes widespread disclosures to its shareholders and the general public. For example, CME files financial reports on an annual and quarterly basis with the SEC. It also has created a corporate governance section on its website that contains CME's key corporate governance documents, including its Director Independence and Conflict of Interest Policy, Corporate Governance Principles for its Board of Directors, categorical standards of independence, charters and memberships of its Board standing committees, and biographies for each of its directors, including their relationships with the exchange. This high level of disclosure goes far beyond that of any non-public SRO, and CME welcomes such transparency.

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

CME Response: CME believes that the same general conflict of interest standards that apply to other organizations should apply to DCOs. For example, CME employees, whether in the Clearing House Division, the Audit Department, the Market Regulation Department or the Business Development Division are expected to dedicate their best efforts to CME and avoid any conflicts with the interests of CME. As such, in order to maintain the highest degree of integrity in the conduct of our business and to maintain independent judgment, all CME employees and directors are required to avoid any activity or personal interest that creates or appears to create a conflict between an employee's interests and the interests of CME. We believe that such a premise should apply to all types of organizations. CME specific standards are embodied in our Code of Conduct, which applies to all employees and requires annual disclosures of all conflicts through a questionnaire and certification process. Moreover, because CME is conscious of its responsibilities to avoid conflicts, the Market Regulation Department and Audit Department have adopted a compliance policy that stresses the importance of protecting the confidential information that member firms provide to CME as part of CME's oversight responsibilities. The confidentiality policy is available at www.cme.com.

CME further believes that the conflicts of interest standards that apply to the disciplinary committees, such as CME's BCC and PCC, should also apply to clearing house risk committees. The CME Clearing House Risk Oversight Committee is a risk-management oversight committee that has ancillary disciplinary authority. The committee is comprised of 11 members, which include: 1) five broker-dealer/FCMs (*i.e.*, Morgan Stanley, J.P. Morgan, Goldman Sachs, Bear Stearns, O'Connor); 2) one FCM-only firm; 3) one settlement banker; 4) three floor members; and 5) one CBOT member firm representative (in connection with CME's agreement to provide clearing services to the CBOT). Because clearing firms own a significant amount of the collateral available to the CME Clearing House, we believe that their interests should be principally represented on the committee. Importantly, the CME conflict of interest rules applicable to the BCC and PCC—CME Rules 416 (Conflicts of Interest) and 417 (Prohibited Communications)—also apply to the Clearing House Risk Oversight Committee to ensure that conflicts do not impair the process.

Finally, the MROC oversees the activities of the Clearing House Division and helps to ensure that CME protects market users from being harmed by potential conflicts of interest by clearing members, individual exchange members and other market participants involved in exchange regulatory and disciplinary processes. Indeed, the credibility of the futures markets depends upon the avoidance of even the appearance of such conflicts, and the MROC takes an important step in that direction.

We thus believe that conflicts of interest measures are appropriate for DCOs, and that CME's conflicts avoidance measures represents a best practice model.

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.

CME Response: CME believes that third-party regulatory service providers, such as the NFA, should be subject to the same governance standards as other SROs. To exempt such providers from comparable regulation not only would encourage regulatory arbitrage, as new contract markets shop for the low cost (and concomitantly low quality) provider, but invite disparate qualities of regulation. Ultimately, such an approach would serve to commoditize the self-regulatory function and thereby damage the credibility of the futures industry.

In addition, virtually any third-party regulatory service provider is likely to be subject to its own conflicts of interest. For example, a majority of the NFA's Board of Directors is comprised of futures industry participants, many of whom are employed by intermediaries that have a significant financial stake in the outcome of regulatory developments and investigations. In a similar fashion, the Futures Industry Association's Board of Directors, which supports the NFA's role as a provider of regulatory services, is comprised primarily of representatives of large intermediaries. Not a single futures exchange is represented on the FIA board. Respondents to disciplinary proceedings, however, generally are intermediaries or employees and agents of intermediaries. The CFTC should thus mindful of such an inherent conflict of interest and seek to ensure that strong conflict avoidance standards apply to all third-party regulatory service providers.

Conclusion

Thank you for the opportunity to comment upon the Commission's study. If you have any questions or comments, please do not hesitate to contact me or Matthew F. Kluchenek, Director and Associate General Counsel, at (312) 338-2861.

Respectfully submitted,

Craig S. Donohue

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