NOVIG

October 2, 2026	NOVIG PUBLIC COMMENT	RIN 3038-AF76

Conflicts and Affiliations

Affiliated market making and competitive liquidity

Docket No. CFTC-2026-1686

91 Fed. Reg. 50926 (August 6, 2026)

DRAFT 9.9

Comment of Novig on Conflicts and Affiliations

October 2, 2026

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

Re: Conflicts and Affiliations, RIN 3038-AF76, Docket No. CFTC-2026-1686

Dear Mr. Kirkpatrick:

Novig supports the Commission's proposed rules concerning conflicts and affiliations and recommends changes to their focus and implementation. Novig owns a designated contract market that lists event contracts, and we write from the perspective of an exchange whose participants depend on reliable liquidity across a large number of distinct and often short-lived markets.[1]

The proposal directs most of its attention to a speculative risk and comparatively little to a present one. Its affiliate-specific conditions rest on the possibility that an exchange will use its institutional powers to favor a market maker it controls. The Commission has supervised affiliated market making for decades without identifying a pattern of that conduct, and its own economic analysis describes a failure of the affiliate conditions as an unlikely event.[2] We support safeguards against that conduct, but the final rule should give greater attention to a problem that requires no prediction. An exchange's compensation and access decisions determine, every trading day, which firms can afford to quote and on what terms. The proposal's incentive-parity provision supplies the right starting point. The Commission's economic analysis concludes that requiring parity protects fair competition, attracts market makers, and improves price discovery and risk management, at limited cost.[3] Those benefits arise from the opportunity for qualified firms to compete on comparable terms, regardless of whether the firm receiving a benefit is an affiliate. The final rule should be built around that principle and extend it to exchange-supported liquidity arrangements generally.

We support enforceable protections against preferential execution, selective access to nonpublic information, discriminatory treatment in incentive programs, and regulatory decisions influenced by commercial interests, and we commend the Commission for recognizing the value of

---

[1] Conflicts and Affiliations, 91 Fed. Reg. 50926 (Aug. 6, 2026) (Proposal). Question numbers in Part III refer to the numbered requests for comment in the Proposal. Questions in the Commission's consideration of costs and benefits are numbered separately and are identified by the section of the economic analysis in which they appear.

[2] Proposal § VII.C(4)(h), 91 Fed. Reg. at 50982; see Part I.B, infra.

[3] Proposal § VII.C(4)(d), (h), 91 Fed. Reg. at 50978, 50982–83. The Commission estimates the direct costs of parity as limited, if any, and the associated loss of flexibility as de minimis. *Id.* § VII.C(4)(e), 91 Fed. Reg. at 50979.

affiliated liquidity through a standing market-maker exception.[4] The risk of affiliate favoritism should nonetheless be assessed in light of the exchange's own incentives. An exchange depends on participants' confidence that its markets are fair and that they can trade on competitive terms. Favoritism that damages that confidence impairs trading activity, deters liquidity providers, and diminishes the value of the exchange itself, and the common owner of an exchange and a trading affiliate has an interest in both businesses, not simply in the affiliate's return on the next trade. These incentives do not eliminate conflicts or excuse misconduct, and information barriers, impartial execution and access rules, effective surveillance, and independent regulatory decisions remain necessary. The Commission should establish why those protections are insufficient before imposing conditions that may reduce the liquidity available to participants.

The competitive problem the proposal largely leaves unaddressed is present wherever an exchange pays for liquidity. Participants benefit when multiple firms can commit capital, quote continuously, and compete on price, size, and reliability. A firm receiving benefits that other qualified market makers cannot obtain may be able to offer prices and depth its competitors cannot economically match, or may enjoy an advantage that discourages competitors from entering at all. The advantage need not involve an affiliate, preferential matching, or a transfer of confidential customer information. It can arise from an ordinary commercial agreement, and it operates on every quotation the disadvantaged firms decline to post. Commission staff issued an advisory in August 2026 because an increasing number of incentive-program filings, particularly for event contracts, contained procedural or substantive deficiencies that impeded staff's evaluation of program terms and core-principle compliance.[5] The terms on which exchanges compensate market makers are already a supervisory concern.

The proposal applies its parity principle to only one form of economic relationship. It treats common control as the principal marker of a conflicted liquidity arrangement, imposes on affiliated market makers a set of conditions that apply to no other liquidity provider, and requires parity only where an affiliate participates in an incentive program. Corporate affiliation is an incomplete measure of the economic relationship between an exchange and the firms that make its markets. An exchange can confer on a nominally independent firm an equity grant, a revenue share, a guaranteed payment, preferential connectivity, or exclusive access to a liquidity program, and each of those benefits can align the firm's interests with the exchange's and disadvantage its competitors as effectively as common ownership. The benefits the Commission attributes to parity do not depend on which firm would otherwise have been favored. A framework that restricts the affiliate while leaving those arrangements unexamined favors one business structure over another without making markets fairer.

The final rule should require full competitive parity among market makers. Every lawful liquidity-service benefit an exchange makes available to one provider should be available to every other provider prepared and able to satisfy equivalent, objectively defined obligations, whether or not either provider is affiliated and whether or not the exchange has an affiliate at all. Comparable treatment requires attention to the services actually supplied and to the complete economic package. Eligibility must provide a genuine opportunity for qualified firms to compete, without reserved places, numerical limits, slow approvals, constrained API capacity, or selectively administered technical requirements. Genuine capacity constraints and distinct

[4] Proposal § III.B, 91 Fed. Reg. at 50949–50.

[5] CFTC Press Release No. 9282-26 (Aug. 12, 2026); CFTC Letter No. 26-23 (Aug. 12, 2026).

services can be accommodated through transparent standards without protecting selected firms from competition.

We therefore recommend that the Commission extend the incentive-parity requirement of proposed § 38.852(b)(2) to every exchange-supported liquidity arrangement and to the complete package of financial and operational benefits, whether or not an affiliate participates; prohibit numerical and functional exclusion of qualified market makers; replace affiliation-based order subordination with neutral application of disclosed matching rules; preserve information barriers and independent regulatory oversight; and tailor verification, financial surveillance, and disclosure to identified risks. The Commission should use its existing authority under part 38 to obtain the market-making agreements and operational records needed to calibrate those requirements. If the Commission retains affiliate-specific conditions, it should at a minimum replace order subordination with neutral matching, require equivalent rather than asymmetric terms in proposed § 38.852(c)(1)(ii), extend paragraph (b)(2) to arrangements that are not filed as programs, and replace per-session acknowledgment with initial and material-change disclosure. Part I develops the economic and regulatory principles underlying these recommendations. Part II addresses inherent ownership interests, equity incentives, and concentrated ownership. Part III responds to the Commission's questions concerning self-regulation, financial surveillance, affiliated market participants and market making, governance, clearing, and compliance responsibility. We do not address the proposed FCM disclosure amendments.

I. First Principles

A. Risks, evidence, and regulatory alternatives

The Commission should first determine whether the risks it has chosen to address are the risks most consequential for market participants and the effective operation of regulated markets. The proposal concentrates on the possibility that an exchange might favor a market maker it controls, provide that firm with nonpublic information, or compromise its oversight because of the relationship. Those concerns warrant safeguards, but their probability and consequences should be established rather than inferred from common control. A focus on control also overlooks a broader and present source of harm: an exchange may provide selective economic or operational advantages to a market maker it does not control, leaving other qualified firms unable to compete on comparable terms. The resulting loss of competition affects spreads, depth, product coverage, and execution prices. The mechanisms of affiliate favoritism also differ from one another. Favoritism in matching or connectivity leaves a record in order messages, gateway logs, and capacity allocations; information leakage depends on which personnel and systems can reach restricted data; and compromised enforcement appears in alert dispositions, investigation files, and sanction decisions. The controls should respond to the conduct and market consequences identified rather than treating common control as sufficient reason for every proposed restriction.

Section 15(a) of the Commodity Exchange Act requires the Commission, before promulgating a regulation, to consider its costs and benefits in light of the protection of market participants and the public; the efficiency, competitiveness, and financial integrity of futures markets; price discovery; sound risk management practices; and other public interest considerations. Section 15(b) requires the Commission to take into consideration the public interest protected by the antitrust laws and to endeavor to take the least anticompetitive means of achieving the objectives

of the Act.[6] These provisions do not require the Commission to quantify every effect, and the D.C. Circuit has held that section 15(a) requires the Commission to consider costs and benefits rather than to perform any particular quantitative analysis.[7] The Commission must nevertheless consider reasonably foreseeable consequences, connect its decisions to the record, and address significant alternatives.[8] A rule that reassigns execution priority among market makers, imposes conditions on one class of liquidity provider, and influences which firms serve thin markets has consequences for competition that fall squarely within both provisions.

The proposal's antitrust discussion states that the Commission preliminarily identified no anticompetitive effects and, for that reason, identified no less anticompetitive means of achieving its objectives.[9] We respectfully disagree with that premise. Several proposed conditions operate directly on competition among liquidity providers. Order-priority subordination changes which firm receives an execution at a given price based on ownership rather than the timing or terms of its quotation. The market-maker condition permits terms less favorable to the affiliate than those offered to unaffiliated firms, while the parity provision protects unaffiliated firms against less favorable terms. The provisions permit unequal treatment; they do not require every exchange to impose unequal terms. The verification, financial surveillance, and per-session disclosure conditions also impose fixed costs on one form of liquidity provision. These provisions may or may not be justified, but they are not competitively neutral. The section 15(b) analysis should evaluate their effect on the number of firms quoting, displayed depth, spreads, and the range of contracts in which any firm is willing to quote, and compare them with less restrictive means of addressing the same risks.

The Commission's narrower focus also risks giving implicit regulatory acceptance to arrangements that exclude competing market makers merely because the favored firm is not controlled by the exchange. A rule directed at affiliate favoritism that leaves untouched a program awarding selected unaffiliated firms exclusive compensation, superior API capacity, or preferential onboarding would forgo, for every such program, the competitive benefits the Commission attributes to parity. Such conduct may already raise issues under the DCM core principles and impartial-access requirements, and the final rule should not be read to authorize it by omission. The final rule should address lawful market-making benefits across affiliated and unaffiliated relationships and distinguish comparable services from genuinely different obligations.

Part 38 gives the Commission the means to develop a complete record of these arrangements. Regulation 38.5(a) authorizes requests for information relating to a DCM's business, and Regulation 38.5(b) authorizes a request for a written demonstration of core-principle compliance supported by data, information, and documents.[10] The Commission should use that authority to

---

[6] Commodity Exchange Act (CEA) § 15(a)–(b), 7 U.S.C. 19(a)–(b).

[7] *Investment Company Institute v. CFTC*, 720 F.3d 370 (D.C. Cir. 2013).

[8] *Motor Vehicle Manufacturers Ass'n v. State Farm Mutual Automobile Insurance Co.*, 463 U.S. 29, 43 (1983).

[9] Proposal § VII.D, 91 Fed. Reg. at 50988.

[10] 17 C.F.R. § 38.5(a)–(b); see also CEA § 5(d)(2), (9), (12), (16), (19), 7 U.S.C. § 7(d)(2), (9), (12), (16), (19). Regulation 38.5(d) delegates the paragraph (b) compliance-demonstration authority to the Director of the Division of Market Oversight or the Director's designees.

obtain complete market-making agreements and the records needed to assess impartial access, competitive execution, fair and equitable trading, conflicts of interest, and restraints of trade. It should request submissions subject to applicable confidentiality protections and publish findings in a form that supports informed comment without improperly disclosing protected information. That process would not displace existing obligations to file and publish material incentive-program terms.

The inquiry should reach the entire arrangement rather than a list of affiliated firms or a comparison of posted rebates. It should include agreements and amendments, side letters and related instruments, cash and noncash compensation, guarantees, revenue participation, equity terms, expense reimbursements, exclusivity and renewal rights, quoting obligations, and performance records. It should also examine applications and denials, onboarding timelines, production access, API and message-rate allocations, testing and certification, technical support, and communications about new products and incentive changes. The Commission should compare written terms with benefits actually delivered, identify the services and risks for which each benefit compensates the provider, and evaluate competition and participant execution quality at the product level. Arrangements conducted through a parent or another affiliate should be included where they form part of the DCM's liquidity relationship.

That record would permit the Commission to ask the questions the proposal largely leaves unresolved. Can another qualified firm obtain the same economic package by undertaking comparable obligations? Are differences in compensation explained by product coverage, depth, uptime, risk, or distinct services? Do qualification standards or operational practices prevent otherwise capable firms from competing? What effect do exclusivity, limited enrollment, and renewal rights have on entry? How should finite incentive budgets, noncash awards, and genuinely indivisible services be treated? When does dependence on a liquidity provider compromise surveillance, discipline, or an outcome determination?

The Commission already has a competitive rationale for broader parity. Its economic analysis finds that parity will protect fair competition, improve competitiveness, trading efficiency, and price discovery, and attract unaffiliated market participants to make markets.[11] It also expects the proposed requirement to impose limited, if any, direct costs, based on its preliminary understanding that DCMs generally offer similar incentives to every market maker.[12] If that understanding is correct, extending parity to every liquidity arrangement should cost little. If it is not, the disparity the Commission identifies as harmful already exists in markets today. Either way, the benefits the Commission identifies do not depend on whether the firm that would otherwise receive preferential terms is affiliated. A broader standard reaching equity compensation, negotiated guarantees, operational support, and arrangements outside filed programs may require changes to valuation practices, contracts, systems, and budgets, and the Commission should assess those costs. They bear on how the broader standard is designed, not on whether the competitive rationale for parity extends to it. The part 38 record described above would allow the Commission to examine those costs, distinguish comparable obligations from genuinely different services, and accommodate real resource constraints.

[11] Proposal § VII.C(4)(d), (h), 91 Fed. Reg. at 50978, 50982–83.

[12] Proposal § VII.C(4)(e), 91 Fed. Reg. at 50979.

The Administration has also directed federal agencies to reduce unnecessary regulatory burdens and barriers to competition. Executive Order 14192, Unleashing Prosperity Through Deregulation, establishes a policy of reducing unnecessary regulatory burden and requires that the costs of new significant regulations be offset.[13] Executive Order 14215 extended OIRA review of significant regulatory actions to independent agencies, and the proposal reports OMB's determination that the proposed rule is not a significant regulatory action under section 3(f)(1) of Executive Order 12866 and therefore is not an Executive Order 14192 regulatory action.[14] Executive Order 14267, Reducing Anti-Competitive Regulatory Barriers, directs agencies to identify existing regulations that, among other things, create unnecessary barriers to entry for new market participants or limit competition between competitors.[15] That order operates as a review of existing rules rather than a constraint on this rulemaking, and none of these orders displaces the Commission's statutory obligations or creates rights enforceable by commenters. Executive Orders 12866 and 13563 likewise call for attention to regulatory costs and available alternatives. In determining whether to impose affiliation-based trading restrictions, the Commission should examine whether those restrictions would create unnecessary barriers to entry or distort competition.

An exchange does not ordinarily possess superior knowledge about whether the external event underlying an event contract will occur. The proposal should distinguish information about the underlying event, where the exchange ordinarily has no advantage, from information generated by operating the market: resting orders and their owners, customer identities and positions, the composition and historical performance of order flow from different customer channels, surveillance alerts and investigative files, pending listings and rule or fee changes, settlement determinations under review, and system information such as planned changes to matching logic or gateway capacity. The restrictions should address the particular information capable of misuse. Prohibiting a trading affiliate from accessing nonpublic customer orders and positions is straightforward and should be required. Aggregate statistics about the profitability of trading against particular customer channels may be more valuable to a market maker than any individual order; they should be withheld from trading firms or made available to all on equal terms. For upcoming listings and incentive changes, the Commission should permit the exchange to provide the same advance information to all qualified liquidity providers at the same time, under appropriate confidentiality and information-security protections. That approach prevents selective informational advantages without requiring the exchange to leave prospective providers uninformed until trading begins. The Commission should identify the information that an affiliated market maker might improperly obtain, what the supervisory record shows about its misuse, and why neutral distribution, access restrictions, logging, and surveillance would be insufficient before relying on conditions, such as order subordination, that do not regulate information flows.

---

[13] Exec. Order No. 14192, 90 Fed. Reg. 9065 (Feb. 6, 2025); Office of Management and Budget, Memorandum M-25-20, Guidance Implementing Section 3 of Executive Order 14192 (2025).

[14] Exec. Order No. 14215, 90 Fed. Reg. 10447 (Feb. 24, 2025); Proposal § VII.E, 91 Fed. Reg. at 50988. OMB guidance indicates that an action designated as significant at the final rule stage that imposes costs is subject to the offset requirement even if the proposal was not so designated. M-25-20, Q37.

[15] Exec. Order No. 14267, § 3(a), 90 Fed. Reg. 15629 (Apr. 15, 2025).

A categorical prohibition on advance discussions of prospective products with liquidity providers would work against the participants the proposal seeks to protect. Market makers need time to understand contract specifications and settlement sources, build pricing models, test connectivity, set risk limits, and commit personnel and capital. Without adequate preparation, a contract can open without reliable quotations, forcing participants to trade at worse prices or defer trading altogether. Equal advance notice of upcoming listings, supplied to all eligible liquidity providers on the same terms and without revealing confidential customer or regulatory information, addresses the legitimate information concern at substantially lower cost. To the extent the proposed restrictions might be interpreted to prevent such preparation, the Commission should make clear that neutral prelaunch coordination is permitted.

B. The Commission's experience with affiliated market makers

The proposal describes DCM relationships with affiliated market makers as "comparatively new." The Commission's own records demonstrate a much longer history. For most of the history of American futures markets, the principal exchanges were owned by their members, and those members included the floor traders who supplied much of the liquidity in their markets; the resulting conflicts, and those that followed demutualization, were addressed principally through governance and conduct requirements, including public directors, regulatory oversight committees, and conflicts procedures.[16] The Commission's 1997 Annual Report describes CME's establishment of GFX Corporation, a wholly owned subsidiary, to make markets in CME foreign-currency futures on Globex, together with audit-trail and recordkeeping protections, and CME's later annual reports describe GFX trading on Globex and offsetting its risk in the interbank market.[17] A 2013 rule enforcement review described Nadex's affiliated market maker, Market Risk Management, as the sole market maker and a counterparty to more than 99 percent of the exchange's trades during the review period. LedgerX's 2018 rulebook likewise identified LedgerPrime as a company under common parent ownership established to make markets in LedgerX products, subject to the same access criteria and without preferential pricing or an inherent execution-speed advantage. LedgerX was then a SEF; it received DCM designation in 2019, so that example supplies related experience with an affiliated liquidity arrangement rather than an additional pre-2019 DCM example. In its 2015 Regulation Automated Trading proposal, the Commission noted that its staff had historically required enhanced DCM surveillance when a DCM market maker was operated by an affiliate.[18]

---

[16] See Conflicts of Interest in Self-Regulation and Self-Regulatory Organizations, 72 Fed. Reg. 6936 (Feb. 14, 2007) (adopting acceptable practices for the DCM conflicts-of-interest core principle).

[17] See, e.g., CME Group Inc., Annual Report (Form 10-K), Item 1 (fiscal year 2009); Chicago Mercantile Exchange Holdings Inc., Annual Report (Form 10-K), Item 1 (fiscal year 2001).

[18] Proposal § I.F.iii, 91 Fed. Reg. at 50932. See also CFTC, 1997 Annual Report, Division of Trading and Markets, Exchange Rule Review (GFX); CFTC, Rule Enforcement Review of North American Derivatives Exchange (Nov. 2013), at 10; LedgerX LLC, Rulebook Rule 2.5 (Nov. 2018); Regulation Automated Trading, 80 Fed. Reg. 78,824, 78,883 n.555 (Dec. 17, 2015); CFTC, Rule Enforcement Review of North American Derivatives Exchange (July 28, 2017), at 11–12. CFTC Press Release No. 7945-19 (June 24, 2019) (LedgerX DCM designation; prior SEF registration in July 2017).

The Commission may regulate credible risks before they produce a violation, but decades of supervised experience are relevant to determining which risks warrant additional restrictions. The proposal does not identify, from that history, a demonstrated pattern of exchanges giving their affiliated market makers better execution, preferential access to information, or exemptions from exchange rules. There have been documented supervisory deficiencies, and they did not turn on ownership. In its 2017 review of Nadex, the Division of Market Oversight reported that the affiliated market maker was on one side of approximately 70 percent of trades and an unaffiliated market maker on one side of approximately 29 percent.[19] The exchange had closed 268 surveillance alerts concerning both firms without adequate investigation and had not published the material terms of its agreements with either firm, including terms permitting withdrawal before expiration, as Regulation 38.401 requires.[20] Those findings warrant effective investigation, disclosure, and independent oversight reaching affiliated and unaffiliated providers alike. They do not, without further analysis, establish that mandatory subordination or limits on the affiliate's trading are responsive remedies, and they illustrate that the transparency of liquidity arrangements is itself a supervisory concern. The Commission should examine its GFX, Nadex, LedgerX, and other supervisory records, describe any preferential treatment or customer harm it has identified, and explain why the controls developed over that history are inadequate. If that record shows little or no occurrence of the specific preferential conduct used to justify the proposal, that is material evidence in evaluating both the existence of the risk and the burden of the proposed remedy. By concentrating on that risk while leaving preferential arrangements with noncontrolled market makers largely unaddressed, the proposal would impose significant costs while leaving in place the impediments to competition that operate now.

The relevant costs are not confined to compliance budgets. A condition that reduces any firm's willingness to quote imposes costs on participants through wider spreads, thinner depth, fewer contracts with reliable two-sided markets, and more expensive hedging. Those costs are diffuse, and they are borne by the people the rule is meant to protect. A rule that improves the execution opportunities of unaffiliated market makers can benefit participants if it induces better competing quotations, but that benefit is an empirical proposition rather than a necessary consequence. The Commission should therefore measure the effect of its proposed conditions on execution prices, displayed depth, available products, and access to liquidity, rather than on the allocation of executions among market makers alone.

C. Event-contract valuation and expandable supply

An event contract provides a payment determined by a specified event or outcome under published settlement terms. A binary contract pays a stated amount, commonly $1, if an event occurs and zero otherwise. A scalar contract instead pays an amount determined by where an observed outcome falls within a specified range. For either structure, the expected settlement payout, rather than the number of people wishing to hold the contract, provides an anchor for valuation. In the binary case, a trader assessing a 33 percent probability of a $1 payout calculates an expected payout of 33 cents. A trader valuing a scalar contract instead weights the possible settlement amounts by their assessed probabilities. The price at which either trader is willing to transact also reflects costs of collateral, risk preferences, hedging value, and confidence in the underlying assessment. A binary Yes contract bought for 35 cents when its expected payout is 33

[19] Nadex Review at 16.

[20] *Id.* at 4, 10–12.

cents has an expected loss of 2 cents before costs; holding until resolution or attracting additional traders with the same belief does not change that arithmetic. None of these propositions depends on settlement being all-or-nothing.

Event contracts also permit offsetting positions to be created without a fixed inventory of outstanding contracts. In a fully collateralized binary example, a Yes position bought at 33 cents and the complementary No position bought at 67 cents together fund the $1 terminal payment, and additional matched pairs can be created as participants take opposing positions and provide the required collateral. In a scalar contract, the two sides of a properly structured matched position likewise bear offsetting exposures under the contract's settlement formula, although collateral requirements depend on the payout terms and risk framework. The amount outstanding results from trading, subject to position limits and the availability of opposing risk-bearing capacity. An ordinary share, by contrast, is a claim on a business whose quantity changes through issuance and repurchases, and secondary trading transfers existing shares. A cryptoasset whose supply is set by protocol is similar in this respect: ordinary trading transfers tokens while new supply follows the protocol. Other derivatives also allow opposing positions to expand, so this feature is not unique to event contracts. Event contracts combine it with an identifiable contingent payout that constrains valuation, whether binary or scalar.

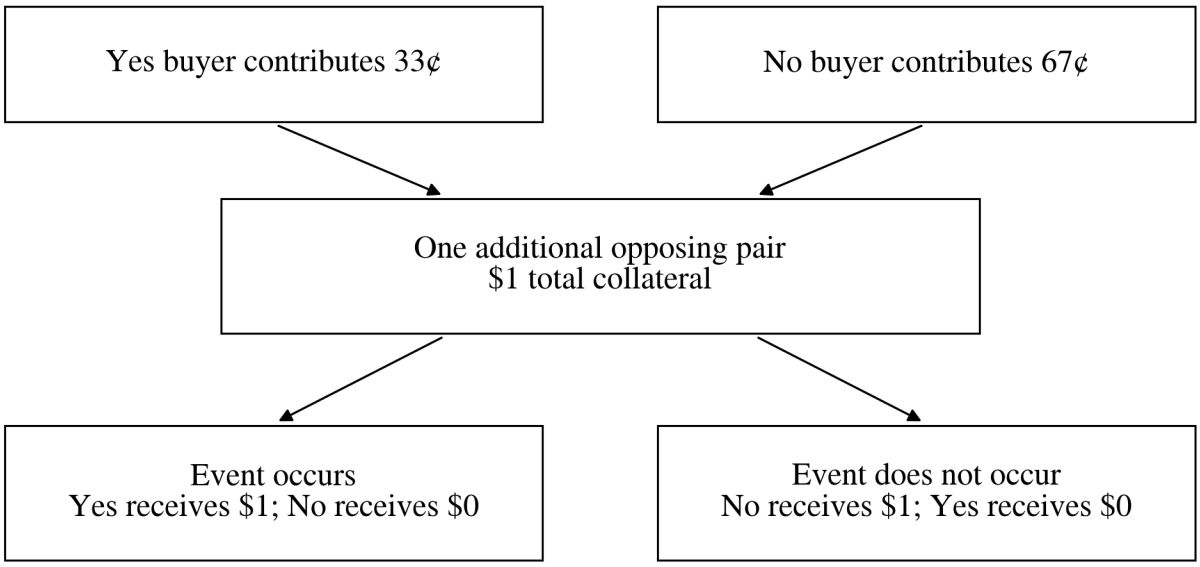


Figure 1. Expandable contract supply. Additional opposing pairs can be created at the same prices when participants supply collateral. Illustrative mechanics before fees; contract terms and position limits apply.

In an asset with positive net supply, an increase in the number of investors who wish to hold it must be met from an existing stock of shares or tokens, and when short selling is costly or constrained, prices can come to reflect the views of the most optimistic holders.[21] In an event contract, a participant who believes the price is too high can express that view by buying No on the same terms on which another participant buys Yes, and new arrivals who share the prevailing

[21] Edward M. Miller, Risk, Uncertainty, and Divergence of Opinion, 32 J. Fin. 1151 (1977).

assessment can be accommodated by creating new positions at the prevailing price. If a market grows from three participants to a million while the distribution of beliefs, wealth, and risk tolerance across the two sides remains unchanged, open interest can grow while the price does not move. Participation does move prices when it changes that distribution, for example where new participants hold systematically different beliefs, cluster on one side, or face different financing constraints, and order imbalances can move execution prices without any change in an individual trader's assessment. Even so, event-contract prices are disciplined by the expected payout and by the availability of capital willing to take either side, rather than by competition for a scarce inventory.

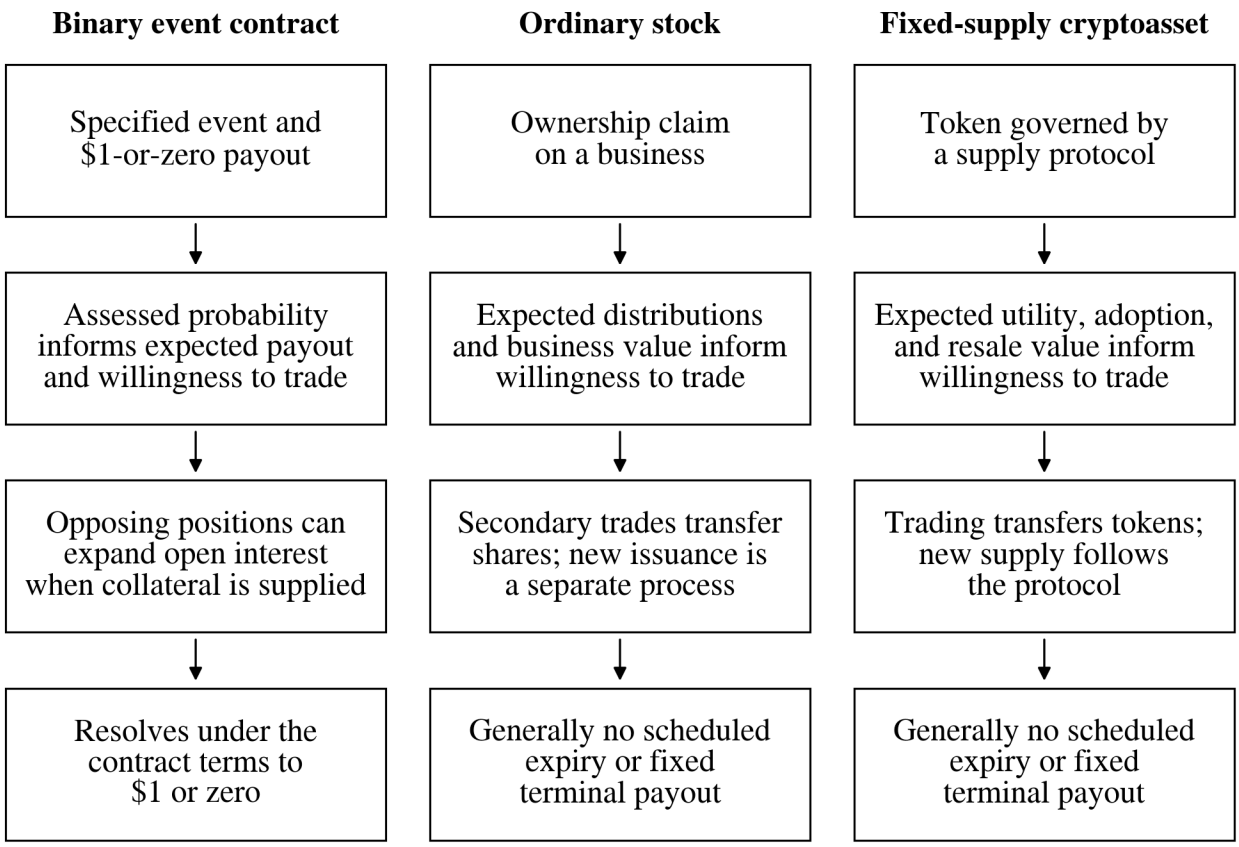


Figure 2. Valuation, supply, and resolution. Simplified comparison of a binary event contract, an ordinary stock, and a cryptoasset whose supply is set by protocol. All three involve valuation and trading preferences; they differ in how supply responds to trading and in whether a fixed terminal payout exists.

The prediction-market literature supports this account, with qualifications. Wolfers and Zitzewitz show that prices correspond closely to mean beliefs under plausible assumptions about the distribution of beliefs and risk preferences, while Manski showed that when risk-neutral traders face budget constraints the price can instead correspond to a quantile of the belief distribution

and need not equal the mean.[22] Beygelzimer, Langford, and Pennock show that when traders bet according to the Kelly criterion, the market price is a wealth-weighted average of their beliefs.[23] Empirical work on the favorite-longshot bias documents systematic differences between prices and outcome frequencies that reflect risk preferences or the misperception of small probabilities.[24] These results support treating prices as an aggregation of beliefs weighted by capital and risk tolerance, and they caution against treating any price as an unbiased probability. Each places at the center of the analysis the capital that is willing to bear risk on either side, which is the function a market maker performs.

Market quality in event contracts depends heavily on the capital available to take the other side of a trade at competitive prices. An exchange can attract many customers who want the same exposure and still offer poor execution if few firms will hold the offsetting risk. A market maker supplies that capacity so that a customer need not wait for another customer seeking the opposite exposure to arrive at the same moment. The economic structure also affects the risks associated with market making. A market maker supporting a token with a fixed float or a thinly traded stock may influence the price of a scarce asset in ways that benefit an affiliated issuer or holder. An affiliate quoting an event contract cannot change the contract's terminal payout, which depends on the event and the settlement terms, although its willingness and ability to absorb risk can materially affect execution prices and depth. It can also trade abusively, engage in wash trades, or misuse information obtained through the exchange. The Commission should assess those risks against the contract's economic characteristics and select controls that address the conduct involved.

The exchange's role in determining contract outcomes presents an additional conflict that warrants specific safeguards. The exchange often administers the determination of whether the underlying event occurred, particularly where the outcome is ambiguous or the source of the data revises it. Any trading firm that holds positions through resolution, affiliated or not, has an interest in that determination. The appropriate response is to require that outcome determinations follow pre-specified contract terms, be made by personnel insulated from every trading firm, be documented, and be reviewed by the regulatory oversight committee where the exchange exercises discretion. That requirement should apply whenever a firm with a material position or a significant commercial relationship with the exchange stands to gain from the determination.

D. Market making and the benefits of affiliation

Market makers provide executable quotations across event-contract markets. They commit capital, maintain forecasting and pricing models, integrate external data, build and operate trading systems, and manage the risk of the positions they accumulate. A displayed quotation is an offer to trade, not an entitlement to profit. A market maker quoting a 32-cent bid and a 34-cent offer has not earned two cents. Whether its trades are profitable depends on which side

---

[22] Justin Wolfers & Eric Zitzewitz, Interpreting Prediction Market Prices as Probabilities (Fed. Reserve Bank of S.F. Working Paper No. 2006-11, 2006); Charles F. Manski, Interpreting the Predictions of Prediction Markets, 91 Econ. Letters 425 (2006).

[23] Alina Beygelzimer, John Langford & David M. Pennock, Learning Performance of Prediction Markets with Kelly Bettors (2012), arXiv:1201.6655.

[24] Erik Snowberg & Justin Wolfers, Explaining the Favorite-Long Shot Bias: Is it Risk-Love or Misperceptions?, 118 J. Pol. Econ. 723 (2010).

executes, whether the counterparty knew something the market maker did not, how the event develops while the position is held, and whether the position can be offset. The market-microstructure literature identifies the components of the spread that compensate for these risks: the cost of trading against better-informed counterparties, the cost of carrying unwanted inventory, and the fixed costs of maintaining a presence in the market.[25]

Each of these costs is pronounced in event contracts. Information about many events arrives in discrete jumps, through an announcement, a data release, a score, or a ruling, so a resting quotation can become stale instantly, and the counterparty most eager to trade against it is often the one who has already seen the news. A binary payoff concentrates that risk near resolution, when the price can move from near certainty in one direction to certainty in the other. Commission staff reviewing an exchange listing binary contracts in 2017 described market-maker agreements that permitted market makers to withdraw quotations in the final minutes before a contract expired.[26] Inventory risk is also distinctive. A market maker that quotes both sides of a contract on which customers predominantly want one side accumulates the other side as a consequence of meeting its obligation, and that exposure may be impossible to hedge in any other instrument.

The economics of exchanges that list many distinct and short-lived contracts compound the problem. Each new contract can require contract-specific data, model development and validation, exposure limits, and monitoring, and the opportunity to recover that investment ends when the contract resolves. Because the investment precedes any evidence of trading demand, an independent firm evaluating a new or small contract weighs a certain cost against an uncertain and often modest return. Even a successful exchange may therefore have many contracts that no independent firm can justify quoting continuously on trading revenue alone, and that condition need not disappear as the exchange matures. A contract on a less popular event is not less legitimate because fewer people want to trade it, and a participant who needs to hedge an exposure in such a contract is poorly served by a rule premised on the expectation that independent liquidity will eventually arrive.

Competing market makers bring different valuations and risk limits to the same contracts. They add capacity and compete for executions through price, size, and reliability, while a sole provider faces less pressure to narrow its spread. Several genuinely competing providers are generally preferable to one, and one responsible provider is preferable to an empty book. More quoting firms do not mechanically produce more accurate prices, because firms may use similar models and share the same errors, but competition gives participants more opportunities to transact against different assessments and constrains execution costs. The Commission should give all qualified firms an opportunity to compete on the same terms without imposing ownership-based disadvantages that discourage liquidity provision.

---

[25] Lawrence R. Glosten & Paul R. Milgrom, Bid, Ask and Transaction Prices in a Specialist Market with Heterogeneously Informed Traders, 14 J. Fin. Econ. 71 (1985); Thomas Ho & Hans R. Stoll, Optimal Dealer Pricing Under Transactions and Return Uncertainty, 9 J. Fin. Econ. 47 (1981); Albert S. Kyle, Continuous Auctions and Insider Trading, 53 Econometrica 1315 (1985).

[26] CFTC Division of Market Oversight, Trade Practice Rule Enforcement Review of North American Derivatives Exchange 12, 16–17 (July 28, 2017) (Nadex Review).

An affiliated market maker can have an economic incentive to support liquidity beyond the return on its own trading account. An independent market maker decides whether to quote a contract by comparing the expected trading profit with the cost of quoting it. An affiliate faces the same calculation but can also account for the value that reliable liquidity creates for the exchange. Participants who find executable prices in the contracts they want are more likely to trade again, to trade other contracts, and to bring others to the venue. Economic research describes the reinforcing relationship between trading participation and liquidity: more reliable liquidity attracts additional participants, and that participation can in turn support more liquidity.[27] A firm that captures part of the value of a market with greater participation and reliable liquidity through its ownership interest in the exchange will rationally invest more in reaching it than a firm that captures only its own trading profit. The proposal identifies this coordination problem as the reason for its standing market-maker exception.[28]

Studies of designated market-maker arrangements, including contracts under which listed companies pay firms to provide liquidity, have found improvements in liquidity, particularly for less actively traded securities. Theoretical work also explains why paying for liquidity can create value when its benefits extend beyond the parties to individual trades.[29] An exchange stands in a similar position with respect to its own markets. It bears the consequences of illiquidity across its entire business, and it can rationally support liquidity in contracts whose trading revenue would not attract an outside firm. An affiliate is one means of providing that support. A contract with an outside firm is another.

Participants benefit from that additional incentive when it produces executable quotations in markets independent firms would otherwise decline to serve. A participant in a newly listed contract needs a usable market before the contract has accumulated the volume that would justify independent investment, and a participant in a persistently small market may need that support indefinitely. The exchange's long-term success depends on attracting and retaining participants with useful products and competitive trading conditions. An affiliate whose owners share in that success has a reason to quote reliably in contracts that are unprofitable to serve in isolation, to maintain quotations through periods when an independent firm would withdraw, and to avoid conduct that would drive participants away. The alignment does not depend on the affiliate earning superior trading returns or receiving preferential treatment. It depends on the affiliate's owners valuing the exchange's reputation and growth.

The alignment of incentives should inform the Commission's assessment without becoming a claim that private incentives guarantee participant welfare. An exchange and its affiliate can benefit from reliable liquidity and participant trust while still making decisions that disadvantage competing providers. They may also face short-term incentives inconsistent with their longer-term interests. The relevant regulatory question is which conduct the record shows, how it affects participants, and whether impartial access, information protection, surveillance, and

[27] Marco Pagano, Trading Volume and Asset Liquidity, 104 Q.J. Econ. 255 (1989).

[28] Proposal § III.B, 91 Fed. Reg. at 50949–50.

[29] Kumar Venkataraman & Andrew C. Waisburd, The Value of the Designated Market Maker, 42 J. Fin. & Quantitative Analysis 735 (2007); Amber Anand, Carsten Tanggaard & Daniel G. Weaver, Paying for Market Quality, 44 J. Fin. & Quantitative Analysis 1427 (2009); Hendrik Bessembinder, Jia Hao & Kuncheng Zheng, Market Making Contracts, Firm Value, and the IPO Decision, 70 J. Fin. 1997 (2015).

independent oversight address it. The value of affiliated liquidity is a reason to preserve it under effective safeguards and to measure the cost of restrictions, rather than assume that the interests of an affiliated provider are necessarily adverse to those of the exchange's participants.

Exchanges already recognize this value when they pay independent firms for liquidity. When an exchange pays an outside market maker a monthly fee, a share of revenue, or an equity award in exchange for quoting commitments, it compensates that firm for the same broader value: liquidity that helps the venue operate and grow beyond the return available on any single trade. The regulatory treatment of that value should not become fundamentally different solely because the incentive is held through common ownership rather than through a commercial agreement.

E. Full parity among market makers

Common control is an incomplete proxy for the circumstances in which unequal market-making arrangements harm competition and market participants. The competitive concern arises when an exchange gives one liquidity provider benefits, access, or privileges that similarly situated firms cannot obtain, regardless of which firm the exchange controls. A market maker may receive equity or equity-linked compensation, a share of transaction revenue, guaranteed or minimum payments, rebates, fee concessions, superior connectivity, exclusive program eligibility, or preferential access to order flow without giving the exchange any power to direct its management. Such arrangements may permit the selected firm to quote on terms its competitors cannot match, discourage entry, and ultimately affect the prices and liquidity available to participants. The final rule should reach materially preferential economic and operational arrangements and apply parity and independent-oversight protections to them. Control remains a useful trigger for safeguards addressed to management influence and information access, but it cannot be the test for whether an exchange's treatment of market makers is competitively neutral.

The proposal adopts a control-based definition of affiliation. In explaining the parallel definition of affiliate FCM, the Commission reasons that commercial alignment, information flow, and reporting-line pressure turn on the ability to direct management and policies rather than on any particular equity stake.[30] Control is an administrable trigger for safeguards addressing the exercise of that power. It is not the only way information can be shared or commercial pressure can arise. A significant contractual relationship may produce those risks without control, just as noncontrolling equity compensation or revenue participation may create competitive advantages. The Commission should preserve the control definition for affiliate-specific requirements while examining material economic relationships and preferential treatment on their own terms.

A framework that imposes special restrictions on formal affiliates while overlooking economically comparable relationships with nominally independent firms invites substitution rather than protection. If affiliated market making becomes uneconomic, an exchange that still needs liquidity will purchase it from an outside firm through minimum guarantees, revenue participation, equity, or exclusivity. Those arrangements can preserve liquidity, but they can also create dependence on a single commercial counterparty whose threatened withdrawal could pressure the exchange's commercial and disciplinary decisions, and they can deter a second provider from entering. The Commission should not assume that replacing common ownership with a contract improves either independence or competition.

[30] Proposal § II.A.iv, 91 Fed. Reg. at 50935.

The Commission's action concerning FTX and Alameda Research illustrates the consequences of selective trading privileges. The complaint alleged that FTX created features in its code that gave Alameda an essentially unlimited line of credit, faster execution, and an exemption from the platform's auto-liquidation process.[31] Those allegations involve both preferential execution and extraordinary credit and risk-management accommodations. The latter raise regulatory concerns regardless of whether similar accommodations could be offered to other firms; equal availability does not make an otherwise impermissible practice lawful. An exchange must comply with applicable collateral, credit, and risk-management requirements independently of any parity obligation. The relevant principle for this proposal is that an exchange should not confer selective execution, information, or operational advantages on a favored trading firm, whether that firm is an affiliate or an independent commercial counterparty.

Exchanges should remain free to compensate market makers through equity, revenue sharing, cash payments, and other incentives. Market makers provide a service, and an exchange may rationally pay more for reliable liquidity than the firm could earn from trading alone. The Commission should require exchanges to make every such benefit available to each market maker prepared and able to satisfy equivalent, objectively defined obligations, regardless of affiliation, while separately prohibiting unlawful accommodations and arrangements that exclude otherwise qualified competitors. The principle applies to financial benefits, including cash compensation, rebates, fee reductions and waivers, minimum or guaranteed payments, revenue sharing, equity and equity-linked awards, and reimbursement of expenses. It applies equally to operational benefits, including API access and message-rate allowances, connectivity, technical and onboarding support, test environments and certification, access to market data that may lawfully be shared, and the opportunity to participate in liquidity programs at all. It should govern every exchange-supported liquidity arrangement, whether or not an affiliate participates and whether or not the exchange has an affiliate.

The Commission's own economic analysis makes the case for that extension. It concludes that requiring incentive parity will protect against the harm to fair competition and enhance trust in market integrity; will improve competitiveness, leading to better trading efficiency and improved price discovery; will attract unaffiliated market participants to be active in making markets, fostering liquidity and price discovery; will improve price discovery by increasing the information embedded in prices through better trading participation; and will support sound risk management by increasing liquidity.[32] Every one of those benefits flows from the mechanism of parity: qualified firms compete for the same compensation on the same terms, and more of them choose to quote. None depends on whether the firm that would otherwise have been favored is an affiliate. A program that awards a guaranteed payment or an equity grant to one unaffiliated firm and excludes its competitors causes the same harm to fair competition, discourages the same market makers, and degrades the same price discovery that the Commission attributes to an affiliate-only arrangement. The Commission describes paragraph (b)(2) as closing the channel through which an exchange could advantage its affiliate. The same channel remains open for every favored firm that is not an affiliate. As proposed, the provision secures the benefits the Commission has identified only on exchanges that have an affiliate principal trading firm, only for programs that include it, and only for programs filed under part 40.

---

[31] CFTC Press Release No. 8638-22 (Dec. 13, 2022); CFTC Press Release No. 8644-22 (Dec. 21, 2022); Complaint, *CFTC v. Bankman-Fried*, No. 1:22-cv-10503 (S.D.N.Y. filed Dec. 13, 2022).

[32] Proposal § VII.C(4)(d), (h), 91 Fed. Reg. at 50978, 50982–83.

Commission Regulation 38.151(b) already requires a DCM to provide impartial access to its markets and services, through access criteria that are impartial, transparent, and applied in a nondiscriminatory manner and comparable fee structures for participants receiving equal access or services. Core Principle 19 prohibits a DCM, unless necessary or appropriate to achieve the purposes of the Act, from adopting rules or taking actions that result in an unreasonable restraint of trade or impose a material anticompetitive burden on trading. The Commission has stated that a DCM's market maker and trading incentive programs are rules within its oversight authority, and Commission staff has required a DCM to publish the material terms of its market-maker agreements under Regulation 38.401.[33] The proposal's incentive-parity provision applies these principles to programs in which an affiliate participates. They apply with equal force when the favored firm is unaffiliated. An exchange that confers a material liquidity benefit on one firm outside a published program, or on terms unavailable to its competitors, raises the same concern under Regulation 38.151(b) and Core Principle 19 whether or not the firm is an affiliate.

The Division's August 2026 incentive-program advisory confirms that these are present concerns. Staff issued it in response to an increasing number of deficient incentive-program filings, particularly for event contracts, and it emphasizes complete filings, objective eligibility, uniform incentives for participants meeting the criteria, and attention to selective financial and nonfinancial benefits.[34] The advisory is informational and creates no new obligations. It also contemplates disclosure and review of enrollment limits; it does not establish the general prohibition on numerical gating proposed here. The Commission should use the filings and the additional records it obtains to determine where existing requirements are sufficient and where the final rule should impose clearer or stronger protections.

Parity does not require identical compensation for different services, and the number of contracts alone does not establish comparability. Relevant obligations include product coverage and duration, depth, maximum spreads, uptime, exposure through announcements or resolution, inventory risk, and the capital and technical resources needed to perform. A firm quoting ten thin contracts may undertake a different service from one quoting a heavily traded contract, and a provider furnishing distinct development work may supply something beyond liquidity. The exchange should identify the service purchased and use transparent, objective criteria to explain differences in compensation. Every firm capable of undertaking comparable obligations should have a genuine opportunity to qualify for the corresponding benefit. Criteria designed around a preselected firm, or unrelated investment requirements used to reserve a tier, should not defeat that opportunity.

Equity and other noncash benefits require particular care. An equity award or revenue share for liquidity services can reproduce much of the economic alignment associated with common ownership, and a selectively available award can determine which firms are able to compete. A bare assertion that a cash rebate is equivalent to an equity grant should not suffice. Part II

---

[33] 17 C.F.R. 38.151(b); CEA § 5(d)(19), 7 U.S.C. 7(d)(19); Provisions Common to Registered Entities, 76 Fed. Reg. 44776, 44778 (July 27, 2011); 17 C.F.R. 38.401; Nadex Review at 11–12.

[34] CFTC Division of Market Oversight, Staff Advisory on Self-Certification of Incentive Programs for Prediction Markets, CFTC Letter No. 26-23, at 1, 3, 6–7, 11 (Aug. 12, 2026) (informational status, complete filings, impartial access and financial incentives, and disclosure of enrollment limits); CFTC Press Release No. 9282-26 (Aug. 12, 2026).

addresses how comparability should be measured and how equity compensation should be distinguished from ownership acquired for other reasons.

The Commission should prohibit exchanges from limiting participation in a market-making program to a selected number of firms where additional firms can meet the published obligations. A program restricted to one or two designated providers is not open on equal terms because its compensation is uniform within the selected group. Nor is a program open if the exchange may reject qualified applicants in its discretion, stops admitting participants once preferred firms have joined, admits new firms only during a brief window of which favored firms had advance notice, or grants an incumbent exclusivity or a right of first refusal over a competitor's participation. In each case, the exchange selects which firms receive a commercial advantage instead of permitting qualified firms to compete for it.

The same requirement must apply to the exchange's operational decisions, because firms can be excluded without an express limitation in the program rules. An exchange may leave a program open on paper while processing some applications in days and others in months; issuing production credentials, trading permissions, or market-data entitlements promptly for some firms and slowly for others; allocating API message rates, order-entry sessions, or throttle limits more generously to some firms without any basis in their proposed activity; offering test environments, certification slots, and engineering support on different terms; imposing certification or connectivity requirements disproportionate to any operational need; applying eligibility standards inconsistently; or informing preferred firms of new programs, listings, or changes to incentive terms before others. A firm subject to those obstacles may never become capable of meeting obligations that are facially neutral. Because these practices rarely appear in published rules, a parity requirement that examines only the text of a program will not reach them. It must be enforced through records of what the exchange actually did, including application and onboarding timelines, access and capacity decisions, support provided, communications about program changes, and the payments and other benefits actually conferred.

Exchanges have legitimate technical, financial, security, and operational requirements, and a parity rule should preserve them. An exchange may require minimum financial resources, demonstrated operational competence, connectivity and conformance testing, risk controls, market-abuse controls, and enforceable quoting commitments, and it may require more of a firm seeking higher benefits or broader product coverage. Those requirements should be objective, proportionate to the obligation and the risk, published, consistently administered, and genuinely connected to operational needs. They should not serve as a pretext for excluding otherwise qualified competitors. A firm denied participation, suspended, or terminated should receive a timely written explanation and an opportunity for review by personnel independent of the exchange's commercial functions.

Genuine capacity constraints can be accommodated without permitting arbitrary or indefinite gating. Matching engines and gateways have finite capacity, and an exchange may reasonably limit message rates, sessions, or physical connectivity to protect system integrity. Where a constraint is real, the exchange should document it, allocate the constrained resource through a published and nondiscriminatory method, reassess the allocation, and take reasonable steps to expand capacity. The limit should apply to the resource actually constrained; a limit on gateway sessions does not justify a limit on the firms eligible for rebates. Finite incentive budgets and specialized services require separate analysis. An ordinary incentive budget should be allocated by transparent criteria rather than treated as a sufficient reason to select favored firms. A

genuinely distinct or indivisible service may require competitive procurement instead of an indefinitely open rebate schedule. The Commission should examine whether such services can be divided, offered in proportionate tiers, or procured through open qualification, and what safeguards are necessary if they cannot. Describing a market-making arrangement as specialized should not exempt its liquidity benefits from parity or its selection process from review.

Commercial dependence on the exchange can heighten these conflicts. A firm expecting the renewal of an equity award or continued revenue participation may hesitate to challenge an exchange's decisions, and an exchange that depends on one firm's quotations may hesitate to discipline it. Transparent terms, open qualification, and independent review reduce reliance on informal relationships and allow competing firms to discipline the terms of the liquidity service through their own participation. A comprehensive parity obligation would also limit an exchange's ability to direct preferential benefits to its affiliate. An exchange that cannot confer a benefit on its affiliate without offering the same benefit to every qualified competitor has little ability to use its liquidity programs to favor the affiliate.

Dependence on a sole provider also warrants an operational response even where its terms are open and its conduct is proper. The exchange should monitor quotation coverage, spreads, depth, outages, inventory concentration, and the effect of the provider's withdrawal, with independent regulatory review and appropriate escalation. Product-level comparisons should be used where meaningful comparators exist, and the exchange should document contingency plans for interruptions. The Commission should examine which measures distinguish necessary liquidity support from dependence that impairs competition or oversight. It should not require a second provider to exist, or remove the first before an alternative is available, merely to satisfy a numerical conception of competition.

F. Competitive execution and the core principles

Core Principle 9 requires a DCM to provide a competitive, open, and efficient market and mechanism for executing transactions that protects the price discovery process of trading in its centralized market. Core Principle 2 requires impartial access, Core Principle 12 requires rules that protect participants from abusive practices and promote fair and equitable trading, Core Principle 16 requires rules that minimize and resolve conflicts of interest in the exchange's decision-making, and Core Principle 19 prohibits unreasonable restraints of trade and material anticompetitive burdens.[35] These requirements call for open access, impartial regulatory oversight, and execution rules that support competition among trading firms. They do not direct that any class of participant receive a guaranteed share of executions. Market quality is measured by the prices, depth, and reliability available to participants, and the identity of the firm on the other side of a particular trade is not itself a measure of that quality.

Order priority is particularly important in event contracts. Contracts on most exchanges trade in one-cent increments on a contract worth at most one dollar, and in active contracts the spread is frequently a single tick. When the spread cannot narrow further, liquidity providers compete through queue position and displayed size rather than through price, and the value of time

[35] CEA § 5(d)(2), (9), (12), (16), (19), 7 U.S.C. 7(d)(2), (9), (12), (16), (19); 17 C.F.R. 38.150, 38.500, 38.650, 38.850.

priority rises accordingly.[36] Time priority rewards the firm that commits liquidity first and exposes it longest, and in a tick-constrained market it is one of the principal margins on which market makers compete. A rule that removes that reward for one class of firm alters competition at the margin where it is most active.

Core Principle 9's requirements for open, competitive, and efficient execution provide the appropriate standard for assessing the proposed affiliation-based subordination requirement. A rule that prevents the exchange from giving its affiliate faster access, better information, or preferential treatment in matching protects competition, and the proposal rightly requires it. A rule that requires the exchange to give every other participant preference over the affiliate at the same price, regardless of when each order arrived, replaces one departure from neutrality with another. Whether that replacement improves price discovery depends on whether it draws more competing quotations into the market than it drives out, which is a question of evidence. The Commission's economic analysis attributes improved price discovery to parity precisely because parity brings more firms into the market on equal terms.[37] Neutral execution rules serve that end. Ownership-based priority works against it for one class of firm. The Commission should evaluate each condition by its effect on competition in price, depth, and execution quality, rather than by its effect on the share of executions received by a firm with a particular ownership structure.

II. Equity Interests, Parity, and Control

Common control can give an affiliated market maker an economic interest in the exchange that an independent market maker does not share. Where the exchange and trading firm are held by the same parent, profits or losses from either business may affect the value of the parent's investment. The affiliate can therefore justify quotations based in part on the benefits that trading activity generates for the exchange. An unaffiliated firm ordinarily cannot capture that residual value without acquiring an ownership interest or negotiating a separate commercial arrangement. This is one reason affiliated market making can support contracts that would otherwise lack liquidity, and it also means that parity cannot be achieved by pretending the affiliate and independent firms have identical financial incentives.

The existence of a common parent does not itself mean that the exchange has granted its affiliate an additional trading benefit. Nor would parity require the exchange to distribute equity to every market maker, compel existing owners to dilute their holdings, or pay independent firms for the entire value of the affiliate's preexisting ownership relationship. Such a requirement would eliminate the incentive alignment discussed in Part I without ensuring better execution for market participants. The regulatory obligation should instead govern the advantages the exchange can confer through its market operations and through compensation for liquidity services. Matching priority, market data, connectivity, onboarding, access to contracts, rebates, guarantees, and equity awards made in exchange for quoting obligations are subject to rules ensuring impartial treatment and genuinely open opportunities for all qualified firms.

---

[36] See Chen Yao & Mao Ye, Why Trading Speed Matters: A Tale of Queue Rationing Under Price Controls, 31 Rev. Fin. Stud. 2157 (2018).

[37] Proposal § VII.C(4)(h), 91 Fed. Reg. at 50983.

Equity compensation creates a harder parity question than a published per-contract rebate. The value of an award depends on valuation, vesting, dilution, transfer restrictions, governance rights, and other terms. An exchange may not be able to replicate a grant with an identical number of shares after its value or capital structure has changed. A qualified competing firm should be able to obtain the same compensation for comparable services or a comparably valued alternative under a documented methodology. The assessment should use the value and conditions when each service commitment and award are made, without conferring a right to historical appreciation on a later entrant. The Commission should examine valuation practices and disclose its proposed standard for comment. Comparability should cover the complete economic package, rather than one nominal grant or rebate in isolation.

The opportunity must also be real. An exchange could formally offer the same equity incentive to every applicant while conditioning eligibility on a minimum purchase, investment size, capitalization, or volume commitment that is unnecessary for the liquidity being purchased. For example, a requirement that a participant commit a very large amount of capital to acquire equity might reserve a supposedly open incentive program for the largest institutional firms, even where smaller firms can provide meaningful quotations in the relevant products. An exchange should be permitted to require sufficient financial resources and risk-bearing capacity to perform the promised services. But those requirements should bear a reasonable relationship to the actual obligations. Where services can be provided at different scales, proportionate tiers and comparable benefits should permit qualifying firms to compete without having to make an unrelated investment in the exchange.

Equity acquired by purchasing shares, including shares available in public markets, should be analyzed separately from equity granted by an exchange in return for market making. An ordinary secondary-market purchase on terms that the exchange does not control is not itself an exchange-provided liquidity incentive, and equal treatment does not entitle competing firms to receive comparable shares. Accumulated ownership can nonetheless change the relationship. A firm that purchases a sufficiently influential interest, whether directly or through a parent or related holders, may acquire the power to direct or cause the direction of the exchange's management and policies. At that point the Commission's proposed control definition can treat the firm as an affiliate, even without an express agreement designating it one.

Ordinary capital investment should likewise be distinguished from compensation for liquidity services. A parent may capitalize its trading subsidiary, and an investor may acquire newly issued equity for a bona fide contribution of capital at risk. Neither transaction, by itself, requires the exchange to furnish the same capital or ownership interest to every competitor. The Commission should examine whether an investment also includes quoting commitments, discounted equity, guarantees, reimbursements, or other consideration tied to liquidity provision. The distinction should turn on the transaction’s substance and documented terms. An exchange should not be able to place liquidity compensation in an investment agreement or route it through its parent to avoid parity.

No particular ownership percentage supplies a complete answer. Voting power, board designation or removal rights, veto rights, shareholder agreements, coordinated holdings, convertible instruments, and contractual powers can establish or contribute to control. Conversely, a substantial passive investment without those rights may not confer control under the proposed definition. The exchange should review the relevant rights and aggregated interests when ownership or governance arrangements change materially, document its analysis, and disclose

circumstances that create a significant commercial conflict. A noncontrolling investment that does not satisfy the definition of affiliation should still be covered by the requirements governing material economic relationships, open incentives, and impartial market access. Ownership acquired through the market must not become an opportunity to avoid the conflicts protections when practical control has been obtained.

These distinctions permit the Commission to preserve the value of affiliated liquidity while preventing exchanges from awarding selected providers a commercial advantage that competitors cannot obtain. Parity applies to exchange-provided opportunities and to the performance obligations attached to them; control determines when affiliate-specific governance obligations apply; and material economic relationships short of control receive tailored conflicts review. That is the parity the Commission's economic analysis credits with protecting fair competition, attracting market makers, and improving price discovery, applied to every benefit the exchange controls rather than only to those offered to an affiliate. The Commission should make clear that an incumbent affiliate's ownership interest is not itself a justification for favorable trading treatment, just as the mere existence of that interest is not a reason to prevent the affiliate from competing under impartial rules.

III. Responses to the Commission's Questions

Questions 8 through 21

The Commission should preserve meaningful choice of designated self-regulatory organization (DSRO). An FCM should not be compelled to depend on a regulator whose commercial affiliate competes with it where another qualified SRO can perform the same examination function. The proposed election provides a useful protection against that conflict, but limiting the alternative to a registered futures association does not establish a competitive framework. The proposal notes that NFA is the only registered futures association. The Commission should permit an FCM to elect another qualified SRO of which it is a member, subject to common examination standards, demonstrated capacity, independence from the FCM being examined, and Commission oversight.[38]

Self-regulation has value because it brings industry knowledge and experience to supervision and permits regulatory methods to respond to changing businesses and market conditions. Where regulated firms have no meaningful choice, the self-regulator faces less pressure to explain its decisions, improve its processes, or distinguish necessary protections from administrative preferences. It can acquire the rigidity of a centralized regulator without the competitive discipline that should make private provision responsive. The Commission should examine whether its designation and election rules preserve the benefits of self-regulation or unnecessarily concentrate supervisory authority in a single institution. The objective should be effective supervision under enforceable standards, with qualified alternatives able to compete on expertise, responsiveness, and efficient administration.

The securities-market discussion offers a relevant comparison. In its 2004 Concept Release Concerning Self-Regulation, the SEC examined competing member regulators and the risk that a universal regulator could become unresponsive because of its size, scope, and lack of

[38] Proposal § I.A, 91 Fed. Reg. at 50927 n.3; id. § II.A.vii, 91 Fed. Reg. at 50939–40 (Questions 8–21).

competition. The subsequent consolidation of NASD and NYSE member regulation into FINRA was justified in part by reducing duplicative examinations and conflicting rules. Those considerations support coordination and common standards; they do not establish that the absence of meaningful alternatives is always preferable. The Commission should consider that experience and explain which features of futures supervision justify a different balance between efficiency, accountability, and choice.[39]

Meaningful choice must not become an opportunity to avoid supervision. A transfer should preserve examination history, open findings, remediation obligations, access to records, and accountability for pending matters. Common examination standards and Commission oversight should prevent competition through weaker enforcement, while information sharing and coordinated assignments should prevent gaps or duplicative examinations. Transition periods, staffing arrangements, and minimum tenure should be justified by the work needed to maintain continuity, rather than used to make an election impracticable. Any phase-in should follow transparent criteria, and its duration should reflect the receiving organization's actual capacity and the risks of the firms affected.

Questions 22 through 29

We support financial surveillance proportionate to the risks of the business being supervised. Intraday position and financial-resource monitoring serves a different function from periodic DSRO examinations, and the safeguards should reflect that distinction. Replacing "continuously" with "throughout the day" appropriately permits the frequency and intensity of monitoring to reflect changing exposures, rather than imply that every business requires the same uninterrupted process. Relevant considerations include leverage, customer-fund custody, credit exposures, concentration, liquidity needs, settlement obligations, and operational dependencies. Fully collateralized trading narrows credit exposure but does not eliminate liquidity, operational, settlement, or governance risk.[40]

Affiliation identifies a conflict that must be managed; it does not determine the appropriate surveillance method by itself. The Commission should preserve the principles-based approach to a DCM's in-house surveillance of an affiliate FCM, requiring effective information controls, independent judgment, documented resolution of conflicts, and escalation that commercial personnel cannot obstruct. The exchange should be able to demonstrate those results through controls suited to its systems and organizational structure. Separate offices or a prescribed reporting arrangement should not substitute for evidence that the people performing surveillance have the authority, information, and independence to act. Guidance can illustrate acceptable methods without foreclosing equivalent protections.

Mandatory outsourcing should require a showing that effective internal controls cannot address the identified risk. A third-party provider introduces its own costs, capacity constraints, information-security needs, and coordination requirements, particularly where action must occur

---

[39] SEC, Concept Release Concerning Self-Regulation, Exchange Act Release No. 34-50700, 69 Fed. Reg. 71256 (Dec. 8, 2004), §§ V.D–E; Erik R. Sirri, Director, Division of Market Regulation, SEC, Testimony Concerning Consolidation of NASD with the Member Firm Regulatory Functions of the NYSE: Working Towards Improved Regulation (May 17, 2007).

[40] Proposal § II.B.iii–vii, 91 Fed. Reg. at 50941–44 (intraday surveillance, principles-based conflicts procedures, and Questions 22–29).

intraday. The Commission should compare those consequences with demonstrably independent internal supervision, distinguish existing costs from incremental changes, and retain the DCM's responsibility for the function. It should obtain the relevant controls, service arrangements, and implementation information directly rather than presume that one organizational model is necessary for every affiliated structure. Additional binding procedures should be supported by the supervisory record and a reasoned assessment of less burdensome means of achieving equivalent protection.

Questions 30, 31, and 42

The affiliate-specific conditions should continue to rest on control. Control is administrable, it tracks the ability to direct the exchange's personnel and systems, and it is the right trigger for information barriers, governance safeguards, and the market-maker conditions that address those risks. The DCM definition should expressly include affiliate introducing brokers, as the SEF definition does, while the functional catchall continues to reach equivalent arrangements regardless of label. Control should not, however, be the only relationship the rule examines. Equity accumulated through market purchases should be assessed together with voting arrangements, governance rights, contractual rights, and other indicia of the ability to direct management and policies; a noncontrolling stake may also create material economic alignment that calls for conflicts review without automatically becoming control. Partial ownership interests that fall short of control, revenue participation, equity awards, minimum payments, and exclusivity arrangements can create commercial alignment and competitive advantage without conferring any power to direct the exchange.

The Commission should define a significant liquidity counterparty by reference to a material economic or contractual relationship with the DCM, rather than by trading volume alone. The definition should address material equity or equity-linked interests in the exchange or its parent, whether obtained through a grant or purchase; revenue participation; individually negotiated guarantees or financial accommodations; and exclusive or preferential rights that create meaningful economic alignment. Receipt of incentives under a genuinely open program on the same terms as other qualified firms should not, standing alone, trigger that designation. A large trading share may justify concentration surveillance without establishing a special commercial relationship. The Commission should use the agreements it obtains under Regulation 38.5 to set materiality standards that distinguish ordinary liquidity compensation from relationships warranting enhanced conflicts review. That review should include independent disciplinary decisions, appropriate recusals, and controls on nonpublic information. The trading restrictions in proposed § 38.852(c) should not automatically extend to such firms merely because a commercial relationship exists. Control remains the appropriate trigger for requirements specifically directed at the power to manage an affiliate's personnel and systems.

The published regulatory text also warrants two technical corrections. Proposed § 38.852(a) defines an affiliate market participant through a trading-activity condition followed by a reserved paragraph (ii), omitting the control condition expressly described in the preamble. In addition, proposed § 38.852(b)(1) establishes procedures for affiliate market participants generally, but its five enumerated minimum requirements refer only to affiliate futures commission merchants.[41] The Commission should reconcile those provisions and preserve the distinction between binding requirements and acceptable practices.

[41] Compare Proposal § III.A.iv, with proposed 17 C.F.R. 38.852(a)–(b)(1).

A parity obligation should not depend on the existence of an affiliate principal trading firm. If a DCM provides a material liquidity benefit to any market maker, the corresponding opportunity should be open to every qualified provider undertaking comparable obligations. The inquiry should reach direct payments and noncash benefits, including equity, revenue participation, reimbursement, data and infrastructure concessions, and operational assistance. The final rule should address numerical limits and effective exclusion through onboarding, technical approvals, API capacity, support, or qualification standards unrelated to the services sought, while preserving necessary financial, technical, and performance conditions. The Commission's own economic analysis credits parity with protecting fair competition, attracting market makers, and improving price discovery, and none of those benefits depends on whether the favored firm is an affiliate. Its estimate of de minimis cost concerns the narrower proposed requirement; broader parity needs its own assessment of contractual, valuation, operational, and budget effects. The Commission should not finalize an affiliate-only parity rule as though the competitive concern were confined to affiliates.

Questions 32 through 35 and 39

We support binding requirements for effective information protection, impartial access, documented conflict resolution, and independent regulatory oversight. Exchanges should be able to demonstrate compliance through controls suited to their systems and risk profiles. Separate credentials, role-based permissions, segregation of sensitive data, access logging, and periodic testing are more directly relevant to information leakage than whether two teams occupy different offices. The proposed text appears to require physical separation and prohibit shared personnel other than administrative staff, while the preamble describes a principles-based approach supported by acceptable practices. The final rule should reconcile that tension by requiring protection of restricted customer and regulatory information and independence in regulatory decisions, with physical and organizational separation treated as acceptable practices that equivalent controls may satisfy. It should also expressly permit neutral distribution of eligible prelisting and program information under the safeguards discussed in Part I. Physical separation should not excuse inadequate digital controls, and its absence should not condemn effective ones.

Legal and compliance functions should be evaluated by responsibility and access rather than by title. Personnel who investigate trading by an affiliate or a significant liquidity counterparty, review surveillance alerts, decide disciplinary matters, make outcome determinations, or handle confidential customer positions should be insulated from the trading business. Shared legal work on an unrelated employment or corporate matter does not create the same risk. Function-specific restrictions, access controls, recusal, and independent escalation can address the distinction. No shared role should permit a trading firm to direct, obstruct, or obtain confidential information about its own regulatory review.

Public disclosures should identify the relationship, describe material liquidity incentives and relevant execution rules, and explain the applicable protections in plain terms. They should describe the actual arrangement rather than merely announce that an affiliate exists, and the Commission should protect confidential customer information and legitimately proprietary details when specifying their content.

Questions 37 and 38

The benefits of affiliated liquidity include sustained investment in new products, liquidity in less active contracts, committed risk-bearing capacity, and quotations that remain in place when independent firms would withdraw. Those benefits can persist after an exchange becomes established. They should be measured through quotation coverage, displayed depth, time at the best price, execution costs, and participant access to markets, rather than through aggregate trading volume alone.

The Commission should not assume that every exchange already implements every proposed practice because some employ broadly similar safeguards. Incremental cost depends on existing architecture and on the precise requirement adopted. Its part 38 request should seek a structured comparison of current controls and proposed changes, distinguish fixed from recurring costs, and examine effects on new entrants.

The inquiry should address whether DCM market-making programs are open to additional qualified entrants in practice. An inventory of formal affiliate relationships cannot show whether economically significant preferences exist. The Commission should review part 40 filings alongside complete agreements, benefits actually delivered, application denials, onboarding intervals, API allocations, related payments, and the firms receiving benefits at each tier. Its 2017 Nadex review, which found that material agreement terms governing nearly all trading on that exchange had not been published, shows that such an inquiry can identify matters a rulebook does not reveal.[42]

Questions 36, 40, 41, and 43

The Commission should retain a standing avenue for affiliated liquidity provision and should not adopt an absolute prohibition. The proposal frames affiliated principal trading as prohibited unless the affiliate qualifies for the market-maker exception, and the conditions of the exception will therefore determine whether affiliated market making remains viable. The exception should be workable for continually introduced contracts and for markets that remain small. Eligibility should not expire because a venue or product reaches a specified age, and a high affiliate share of volume should prompt examination of market conditions rather than an automatic withdrawal of liquidity. We support the Commission's preliminary decision not to propose a volume or value cap. A cap does not establish that a substitute provider exists, and where the affiliate is the only firm quoting, limiting its participation leaves orders without a counterparty.

Retail participation warrants understandable disclosure and effective protection against abusive execution and misuse of information. It does not establish that reducing available liquidity improves customer outcomes, and retail participants are often the participants most exposed to wide spreads in thin markets. The core prohibitions on preferential information and discriminatory exchange access should apply wherever the relevant conduct occurs, including on SEFs, but requirements built around a DCM central limit order book should not be transplanted to request-for-quote or other SEF execution methods without an analysis of how those methods work.

Our position concerns bona fide liquidity provision and the inventory management needed to support it. We do not seek an exception for unrelated proprietary strategies. Any distinction

[42] Nadex Review at 11–12.

should turn on documented activity and risk management, and it should be clear enough that ordinary market-making inventory is not reclassified after the fact as prohibited speculation. Any definition of bona fide market making should also operate together with open qualification. An exchange should not be able to define product coverage or technical standards so as to allocate a program to one favored firm when others could provide comparable liquidity, although it should retain room to design product-specific obligations that correspond to the risks and needs of each contract.

Question 44 and the market-making conditions

Product-specific agreements reviewed under part 40 are preferable to uniform federal spread, size, or uptime parameters. Agreements should identify required coverage, minimum depth where appropriate, maximum spreads, performance measures, exceptions, and the consequences of nonperformance, and their criteria should be objective and comparable across similarly situated providers. The proposal would require an affiliate market maker to maintain continuous two-sided quotations in each product in which it undertakes a market-making obligation, during the trading hours specified in its market-making agreement. That obligation should be accompanied by clearly defined treatment of scheduled announcements, trading halts, technical failures, and the period immediately before resolution, as the agreements Commission staff reviewed on Nadex provided.[43] An obligation that cannot be suspended when the information environment changes will either be breached or be priced into wider quotations at all times.

The condition in proposed § 38.852(c)(1)(ii) requiring that the affiliate's program be on terms no less favorable to the exchange than those offered to unaffiliated members should be replaced with a requirement of equivalent terms. As written, the condition permits an exchange to impose heavier obligations on its affiliate than on any competitor while paragraph (b)(2) prevents it from offering the affiliate anything more favorable. Equivalent obligations and equivalent benefits, available to every qualified provider, are what parity requires.

The Commission considered and did not propose a requirement that an affiliate end each trading period flat or within a net-position threshold, and we agree with that judgment. Two-sided quotations do not produce balanced executions. If participants predominantly buy one side, the market maker accumulates the other while performing its obligation, and a requirement that the exposure disappear at an arbitrary time can force costly offsetting trades or cause the provider to reduce its quotations before the deadline, particularly in contracts that resolve outside ordinary hours. The final rule should provide that inventory acquired in meeting quoting obligations, positions taken to reduce or hedge that inventory, and positions held through resolution consistent with documented risk limits are positions taken in connection with the obligation to maintain two-sided quotations. Supervisors can test that standard against contemporaneous quoting records, risk limits, and trading data, while a net position alone does not establish an unrelated directional strategy. Where a firm holds positions through resolution, the outcome-determination safeguards described in Part I should apply.

Questions 45 and 46

The Commission should replace mandatory affiliate subordination with a requirement that the exchange apply its disclosed matching rules to the affiliate's orders on the same terms as to every

[43] Nadex Review at 12, 16–17.

other participant's, with no priority, preference, or latency advantage. Under proposed § 38.852(c)(1)(i), the exchange's matching system would fill the bid or offer of any unaffiliated member before the affiliate's at the same price, without regard to time priority, so that the affiliate is filled last at every price level.[44]

Consider an affiliate offering 100 contracts at 34 cents, followed by an unaffiliated firm offering 100 contracts at the same price. Under price-time priority, an incoming buyer of 100 contracts would execute against the earlier offer. Under the proposal, the later offer executes first. The buyer pays 34 cents in either case, and the unaffiliated firm obtains the execution without improving the price or offering more size.

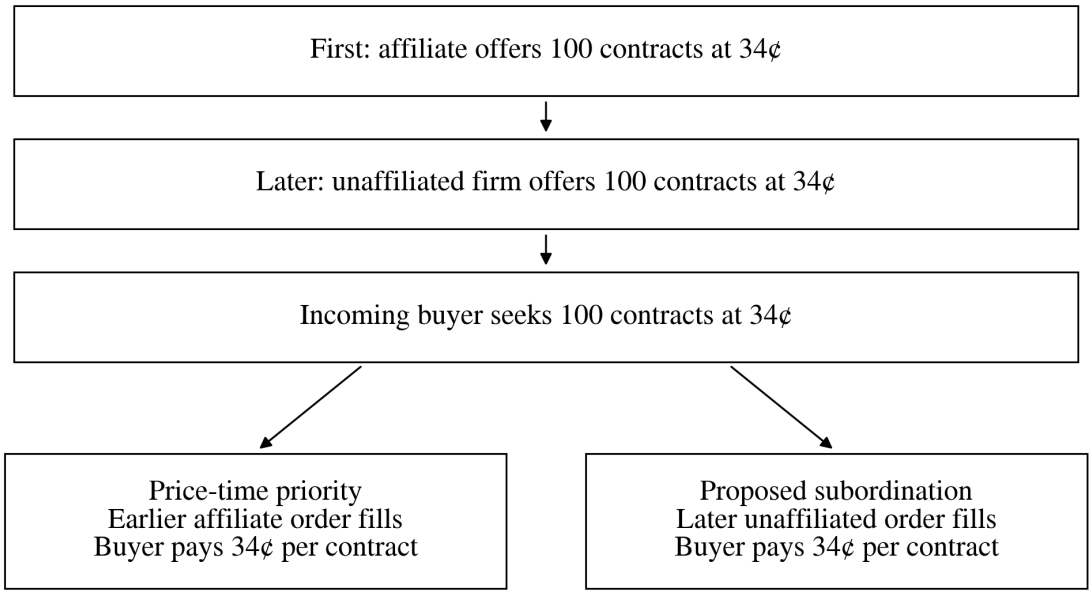


Figure 3. Same-price execution under price-time priority and proposed affiliate subordination. The immediate price to the buyer is unchanged. Any broader effect depends on how the rule changes entry, quotations, and the mix of executions each firm receives.

The preamble describes subordination as a self-adjusting limit: the affiliate supplies liquidity when no one else is present and recedes as others arrive. The economic analysis recognizes the cost that description leaves out, namely that unaffiliated market makers can trade with uninformed participants ahead of the affiliate and leave it to trade against informed ones. A firm at the back of the queue at a price level is filled only when incoming orders exhaust the liquidity ahead of it, and those are disproportionately the larger and better-informed orders that move the price through the level. Small orders from uninformed participants, which compensate a market maker for the risk of the informed ones, are absorbed by the orders ahead. Research on the value of queue position shows that position in the queue is economically significant and that orders at the back are more exposed to adverse selection.[45] Subordination can therefore alter the mix of orders the affiliate receives while leaving its quoting obligation in place, and the affiliate may

[44] Proposed 17 C.F.R. 38.852(c)(1)(i); Proposal § III.B.iii, 91 Fed. Reg. at 50951.

[45] See Ciamac C. Moallemi & Kai Yuan, A Model for Queue Position Valuation in a Limit Order Book (Columbia Business School working paper); Yao & Ye, *supra*.

respond by quoting less size, widening its prices, or declining to support products where it expects intermittent competition. A firm that receives priority merely by joining an existing price also has less reason to improve that price. None of these responses is inevitable, but the proposal does not establish that the entry benefit exceeds the cost to displayed liquidity.

Precedent for requiring certain trading firms to yield priority does exist. Section 11(a) of the Securities Exchange Act and Rule 11a1-1(T) have long required exchange members trading for their own accounts under certain exemptions to yield priority, parity, and precedence to orders of non-members at the same price.[46] That rule rested on the time-and-place advantages that membership conferred on the trading floor, and it applied to every member that enjoyed those advantages, not to firms selected by ownership. It supports regulating an identified functional advantage on equal terms across all firms that possess it, which is the approach we recommend. Where the proposal's information barriers, access controls, and surveillance prevent the affiliate from obtaining any advantage in information or access, the functional rationale for making it yield is absent.

If the Commission concludes that resting customer orders deserve protection at the same price, it can provide that protection without reference to ownership. Several U.S. options exchanges give priority at the same price to orders of public customers over orders of professional participants, and they apply that priority to all market makers alike.[47] A DCM could adopt a disclosed rule under which the orders of participants not acting as liquidity providers are filled before those of any liquidity provider at the same price, affiliated or not. That rule would protect customers in the way the Commission intends while preserving competition among market makers on equal terms.

Affiliation-based priority may be technically feasible but still requires changes to order classification, account controls, testing, audit trails, and failure handling, and a pro rata system would require its own allocation analysis. The rule should prohibit selective privileges under whatever algorithm the exchange uses without mandating a single allocation method or inviting circumvention through account labels. Request-for-quote and block-trade methods do not contain a queue comparable to a central limit order book, and equal invitation criteria, simultaneous access to relevant information, disclosed response windows, and neutral selection rules are more relevant in those settings.

A disclosed and uniformly applied matching algorithm, supported by surveillance, information barriers, and a prohibition on selective exchange assistance, addresses the central concern that an exchange could favor its affiliate through its institutional powers. Combined with comprehensive parity, it also prevents the exchange from favoring the affiliate, or any other firm, through the incentive programs and operational benefits that surround the matching engine. The Commission should address preferential compensation, connectivity, and support directly rather than attempting to offset those advantages through different matching priority for affiliates.

---

[46] 15 U.S.C. 78k(a)(1)(G); 17 C.F.R. 240.11a1-1(T).

[47] See, e.g., Nasdaq ISE, LLC Rules, Options 3, Section 10(c)(1)(A) (Priority Customer orders take priority over non-Priority Customer interest at the same price).

Question 47

The Commission should permit exchanges to combine enforceable access parity, information barriers, independently accountable surveillance, objective liquidity agreements, and periodic testing. The exchange's regulatory function should have the authority and resources to investigate affiliates and significant liquidity counterparties, with direct escalation to the regulatory oversight committee. Separate profit-and-loss measurement and compensation based on a trading team's results can improve accountability and help distinguish liquidity services from unbounded subsidies, although they do not eliminate the parent's interest in the exchange's growth or replace information controls. Separately managed affiliated desks can contribute different models and independently determined quotations, but multiple desks under a common parent are not independent competitors and should not substitute for open access by outside firms. A mandatory minimum number of affiliate desks would multiply fixed costs; the arrangement should be permitted where useful rather than required.

Questions 48 and 49

The Commission should protect the financial resources a DCM must maintain under Core Principle 21 and require clear documentation of affiliate funding. An affiliated market maker should not be permitted to draw on resources the DCM needs to discharge its obligations or to receive collateral or financial accommodations unavailable to other firms under objective criteria, and transactions and support arrangements within the group should be documented and reviewable. Complete economic independence between entities financed by a common parent is neither achievable nor necessary; funding provenance, legal segregation, transfer restrictions, and the availability of resources for regulatory obligations can be examined, but the counterfactual source of every dollar in a corporate group cannot.

Financial surveillance should fit the activity. The proposal would require surveillance of the affiliate as if it were an FCM, other than requirements applicable to customers. A principal trading firm that holds no customer funds does not create the custody and segregation risks that FCM requirements address. A tailored standard should examine collateral, liquidity, concentrated exposures, funding arrangements, and operational continuity, accounting for whether the contracts are fully collateralized. Full collateralization narrows trading-credit exposure but does not eliminate liquidity, operational, settlement, or governance risk.

Questions 50 and 51

We support meaningful independent verification of information barriers, access parity, liquidity agreements, and regulatory treatment. The Commission should specify the objectives and minimum evidence while avoiding duplication of surveillance the exchange already performs. The preamble contemplates the existing Regulation 38.606 regulatory-service-provider framework, under which providers are registered futures associations or registered entities, although the proposed certification text does not expressly incorporate that definition.[48] The final rule should state who may perform the review and how proprietary records will be protected. Where another trading venue performs it, access to sensitive order-message data requires particular safeguards. The Commission should also consider independent accounting, audit, and compliance firms meeting defined competence and independence standards, and establish

[48] 17 C.F.R. § 38.606; Proposal § III.B.iii, 91 Fed. Reg. at 50952 (contemplating the established regulatory-service-provider framework for annual independent verification).

whether sufficient reviewer capacity exists before making certification a condition of continued trading. Independence should encompass ownership, commercial relationships, reporting lines, compensation, and the ability to report deficiencies without interference. Verification should cover parity obligations for all liquidity programs, not only those involving the affiliate.

An annual review can provide a regular assessment, supplemented by notification and targeted review after material incidents or system changes. The certification should identify its scope, testing, exceptions, and remediation, and it should not imply that the reviewer guarantees the absence of undetected violations. The consequences of a lapse should depend on its nature. Material misuse of information or preferential execution can justify immediate suspension of the affected activity. A delayed certification or remediable administrative defect should not require disorderly liquidation of properly collateralized positions, and the rule should distinguish new risk-taking from supervised risk reduction, specify who authorizes remediation and resumption, and preserve settlement obligations.

Questions 52 through 54

We favor prominent disclosure before a customer first trades on the venue, renewed notice when the arrangement materially changes, and a persistent, readily accessible statement of the affiliate relationship and material trading conditions within the trading interface. Product-specific notice can supplement that approach where an arrangement creates a material distinction a customer would otherwise miss. Requiring an affirmative acknowledgment before every trading session imposes repeated interruption without evidence that customers gain understanding. The Commission should evaluate comprehension and salience rather than equate the number of acknowledgments with the quality of disclosure. A customer who has already read an unchanged notice learns nothing new by clicking it again, and repeated prompts tend to train customers to dismiss disclosures, including ones that matter.

Delivery obligations should follow the access path. The exchange should deliver disclosures through its own interface, and an intermediary or interface operator should deliver them where it controls the customer interaction, with the exchange responsible for approved content, distribution arrangements, and reasonable verification. The rule should address API access, multiple interfaces, and recordkeeping without requiring duplicative notices for the same interaction. If disclosure is a protection worth requiring, the same disclosure of material liquidity arrangements should be required where a significant unaffiliated liquidity counterparty receives benefits beyond the generally applicable fee schedule.

Question 55

The Commission should use Regulation 38.5 to obtain product-level evidence of liquidity-provider participation, agreements and quoting obligations, compensation and funding, access decisions, current controls, and expected implementation costs. That request should cover affiliated and unaffiliated arrangements and the operational records described in Part I. Aggregate affiliate volume can conceal very different circumstances: a firm may be indispensable in many small contracts and a minor competitor in the venue's largest ones. Measures should distinguish trading volume from displayed depth, time at the best price, and coverage when no other provider quotes. The Commission should seek implementation plans and provide transition periods tied to the work required. Matching changes, reviewer procurement, information controls, and customer interfaces have different dependencies. The transition should

avoid simultaneous withdrawal by multiple providers and permit orderly risk reduction for arrangements that ultimately do not qualify.

Questions 56 through 59

Independent regulatory oversight, effective recusal, and disciplinary processes insulated from commercial influence address the conflict that motivates the proposal more directly than a change in a compliant order's queue position. We support substantive regulatory independence and would retain the existing acceptable practices for public directors, regulatory oversight committees, and disciplinary panels unless the Commission establishes a need for binding prescriptions. Widespread adoption of a practice does not itself justify removing discretion to use equivalent safeguards. Governance should secure adequate regulatory authority and resources, independent escalation, effective recusal, and protection against interference by affiliate management or significant liquidity counterparties. The committee's responsibilities should expressly include oversight of the exchange's compliance with its parity obligations and of outcome determinations in which the exchange exercises discretion. The Commission should also verify its premise that codification costs will be minimal: an established exchange that already follows each practice and a new entrant building its governance structure are differently situated. The final standard should protect independent judgment and effective oversight while allowing organizational implementation to fit the business.

Questions 60 through 71

The distinction between control and economic alignment applies to clearing relationships as well as to liquidity arrangements. Control remains a useful trigger for requirements addressing the power to direct management, personnel, and systems. It should not be the exclusive measure of a material commercial conflict. Equity interests, equity-linked compensation, revenue participation with the DCO or an affiliated exchange, parent, or other affiliate, guarantees, preferential financing, and other contractual rights can align a clearing member's interests with the group without establishing control. The Commission should examine those relationships according to their substance and materiality, including the rights attached to an ownership interest, rather than rely on a single ownership percentage or treat the absence of control as the absence of a conflict. As discussed in Part II, ordinary capital investment should be distinguished from additional consideration or preferential terms supplied for services.

We support the principles-based formulation of the DCO conflicts requirement and do not recommend additional uniform procedural prescriptions without evidence that they are needed. A DCO should identify the decisions in which an affiliate or another material commercial counterparty has an interest and demonstrate that its controls protect independent risk management and impartial treatment. Appropriate controls may include access restrictions, recusal, independent escalation, and records of the reasons for discretionary decisions. Guidance should explain the protections sought while allowing implementation to fit the DCO's membership, products, risk model, and governance. A fixed checklist cannot anticipate every conflict, and compliance should remain capable of adapting as the business changes.[49]

[49] Proposal § IV.D, F–G, 91 Fed. Reg. at 50959–63 (DCO conflicts framework, alternatives, and Questions 60–71).

Financial safeguards should respond to actual exposures and dependencies. Margin, collateral, liquidity, concentration limits, and default-management decisions should follow objective risk criteria applicable to comparable risks, with any different treatment explained by those risks rather than ownership alone. Discretion over financial distress or default warrants particular scrutiny because delay or preferential accommodation can transfer costs to other members or impair the DCO's resources. The Commission should evaluate whether existing risk controls, documented decisions, and independent review adequately address that concern before imposing an affiliation-based ban, volume limit, additional capital requirement, or separate default-waterfall treatment. Volume and open interest can inform the inquiry, but neither is a sufficient substitute for measuring exposure and the consequences of default.

The DCO should disclose material relationships and explain its conflicts protections in terms useful to clearing members and participants, while safeguarding confidential customer and proprietary information. The Commission should obtain the underlying agreements, risk analyses, decision records, and implementation costs needed to assess the framework, and should distinguish a commercially significant relationship from ordinary participation under generally applicable terms. Its analysis should address the risks of particular clearing arrangements, including systemic consequences where relevant, rather than assume that common ownership alone supplies a complete account of either the conflict or the necessary remedy. That approach would extend the proposal's protections to the economic relationships that matter while preserving flexibility to manage changing risks.

Questions 75 through 77

The Commission should specify who is responsible for the protections it adopts without creating overlapping offices or duplicative reports. A chief compliance officer, chief regulatory officer, or equivalent function should have sufficient authority, resources, access to records, and a direct reporting path to the regulatory oversight committee. Personnel responsible for commercial relationships should not control investigations, disciplinary decisions, or the review of discretionary outcome determinations involving liquidity counterparties. The Commission should explain the distinct responsibilities of any required officers, the committee, and an outside reviewer, permit existing functions to discharge compatible responsibilities, and require reports that address actual deficiencies and remediation. The agreements and supervisory record should inform the functions and independence protections needed; the title of an officer alone does not establish effective oversight.

Consideration of costs and benefits: baseline, competition, and implementation (Section VII.C)

The analysis should compare the proposed conditions against a feasible alternative regime of neutral matching, comprehensive parity, effective information protection, and independent review. The relevant baseline is not an uncontrolled affiliate with access to customer orders; existing core-principle obligations and the protections the proposal itself would codify remain part of the comparison. The Commission should separately assess execution costs, market coverage, entry by outside liquidity providers, and the fixed costs borne by exchanges. A rule that increases independent participation in active contracts may still leave less active contracts with reduced depth, and average spreads or total venue volume can conceal that result.

The analysis assumes that the market-maker agreement condition imposes no substantive cost and that incentive parity requires little change because exchanges generally offer comparable programs. Both assumptions require evidence about the full economic package. Posted fees may omit revenue participation, equity, minimum payments, expense support, or exclusive rights. Part I.A addresses the cost of extending parity beyond affiliate programs. The provisions also permit an affiliate to receive less favorable terms than unaffiliated providers, so their effect depends on how each exchange structures its programs. The Commission acknowledges foregone affiliate profits and the possibility that exchanges may lose liquidity or the ability to launch products. Its analysis should carry those effects through to participant execution prices, depth, product coverage, and hedging costs, with particular attention to less active markets. Recognition that liquidity could decline does not establish the magnitude or incidence of the resulting costs.

Consideration of costs and benefits: the estimate of order-subordination cost (Section VII.C, Questions 13 through 15)

The Commission estimates the cost of order-priority subordination by combining a Kyle's lambda estimate of 0.001 for markets on one exchange, drawn from a 2026 working paper, with internal data on net taker volume in one of that exchange's most liquid markets, the 15-minute Bitcoin contracts, between March 1 and June 15, 2026, and arrives at a conditional estimate of approximately $750 per day under its stated assumptions. That amount is a modeled estimate for the selected product, not an observed market-wide cost of the proposed rule.[50] A price-impact coefficient measures how prices respond to net order flow. It does not, without a further identification strategy, measure the change caused by moving the affiliate's orders behind later unaffiliated orders at the same price. That change consists of the executions the affiliate would lose, the worse mix of executions it would retain, and the adjustments affiliated and unaffiliated firms would make to their quotations in response.

The choice of market compounds the problem. A highly active, short-duration contract with frequent competing quotations is where subordination's mechanical effect is easiest to measure, but it is not representative of the thin markets in which the exception matters most, where information arrives differently and positions are held longer. A single per-day figure for one product says little about the effect on the hundreds of contracts an event exchange may list, or on a firm's decision whether to quote them at all.

The Commission should replay historical order messages under the proposed priority rule to estimate the mechanical reassignment of fills and the post-trade performance of the reassigned and retained executions, acknowledging that a replay holds behavior fixed. It should then evaluate plausible behavioral responses and, where available, evidence from exchanges that have voluntarily adjusted price-time priority for affiliates, controlling for product and venue differences and disclosing units, assumptions, uncertainty, and the basis for any extrapolation. The analysis should distinguish three effects: the mechanical reassignment of same-price fills, the response of affiliated and unaffiliated firms to the altered allocation, and the resulting change in customer execution quality. A replay can illuminate the first. Only evidence about behavior can establish the second and third.

[50] Proposal § VII.C(4)(e), 91 Fed. Reg. at 50980 & nn.353–357.

Consideration of costs and benefits: implementation costs and alternatives (Section VII.C, Questions 16 through 23)

Matching changes, independent certification, and recurring notices require different implementations. The Commission should distinguish initial engineering, ongoing operation, independent testing, data retention, and provider fees, and identify whether each cost attaches to the exchange, the affiliate, the product, or a shared service. Existing surveillance infrastructure may reduce some costs, but that should be demonstrated rather than assumed. The analysis should also compare less burdensome alternatives that provide equivalent protection. An independent reviewer can test access controls and matching neutrality without replicating every trading system, existing event logs may support verification without a separate data pipeline, and initial and material-change disclosure may achieve the disclosure objective with less recurring friction. No alternative should be accepted merely because it is cheaper; each should be evaluated for whether it protects participants effectively.

Antitrust considerations (Section VII.D)

The proposal has identifiable competitive effects that warrant analysis. Affiliation-based subordination allocates executions by corporate status rather than quotation terms or arrival time, reducing the reward for displaying liquidity early and potentially changing willingness to quote. Paragraphs (b)(2) and (c)(1)(ii) permit less favorable treatment of affiliated providers, although they do not compel exchanges to impose it. Verification and disclosure impose fixed costs on one form of liquidity provision that may fall more heavily on smaller exchanges and new entrants. The proposal leaves broader questions about selective enrollment, equity and revenue arrangements, and operational exclusion unresolved. The Commission should measure these effects and consider whether a framework covering the underlying economic relationships would achieve its objectives with less distortion.

Less anticompetitive means are available. Neutral application of disclosed matching rules, with any customer-priority rule applied equally to all professional liquidity providers, addresses preferential execution without allocating executions by ownership. Comprehensive parity across all liquidity programs, open eligibility, and records of benefits actually provided address preferential incentives more completely than an affiliate-only rule, and they strengthen rather than restrain competition. Information barriers, access logging, and independent regulatory oversight address information leakage and compromised enforcement directly. Section 15(b) directs the Commission to endeavor to use those means.

Recommended amendments to proposed § 38.852

The following language would implement the parity framework described above. It uses proposed § 38.852(b)(2) as a reference point; corresponding SEF provisions should be adapted to the relevant execution methods rather than conformed mechanically. Material liquidity-program terms would be published and filed under the applicable part 40 requirements, while ordinary impartial onboarding and technical support would not become a separate program each time assistance is provided. The Commission should calibrate the definitions, treatment of noncash benefits, capacity provisions, and implementation requirements using the agreements and records it obtains under Regulation 38.5.

(b)(2) Liquidity programs; equal opportunity.

(i) Definitions. For purposes of this paragraph (b)(2):

(A) Liquidity benefit means compensation or preferential assistance provided by a designated contract market or its affiliates for liquidity or market-making services, including payments, rebates, guarantees, revenue participation, equity interests, reimbursements, and data, connectivity, capacity, or technical support. A preexisting ownership relationship, ordinary capitalization, or bona fide capital investment shall not alone constitute a liquidity benefit. Additional consideration or preferential terms for liquidity services remain subject to this paragraph regardless of transaction form.

(B) Liquidity program means a rule, schedule, agreement, or arrangement establishing material compensation or preferential economic terms for liquidity provision. Material terms shall be disclosed and submitted under applicable part 40 requirements. Routine onboarding, connectivity, testing, or support provided impartially does not alone constitute a separate program, but remains subject to paragraph (iii).

(C) Qualified liquidity provider means a person satisfying published, objective eligibility criteria reasonably related to the services, financial and operational risks, and trading requirements involved. Applicants shall have impartial access to the processes and assistance needed to establish qualification. Production trading remains subject to applicable trading-privilege and conformance requirements.

(ii) Equal opportunity. A designated contract market offering a liquidity benefit shall make comparable benefits available to every qualified provider undertaking comparable obligations, whether or not the market has an affiliate principal trading firm. Eligibility and performance criteria shall be transparent, proportionate, and consistently applied. The market shall not reserve participation, limit the number of qualified providers that may participate, or grant exclusivity or competitor approval rights that prevent capable firms from qualifying, subject to justified constraints or distinct services under paragraphs (v) and (vi).

(iii) Impartial administration. Application, onboarding, testing, certification, production access, data, connectivity, capacity, and support shall be administered under impartial criteria suited to qualification and proposed activity. Applications shall be handled without discriminatory delay. Adverse participation decisions shall be explained and subject to appropriate independent review. Material program and prelaunch information eligible for distribution shall be made available on equal terms.

(iv) Transparency and records. Material liquidity-service benefits shall be governed by disclosed program terms. The designated contract market shall maintain records sufficient to demonstrate impartial qualification, access, performance assessment, and delivery of benefits, consistent with applicable recordkeeping requirements.

(v) Genuine constraints. Necessary technical, operational, or budget constraints shall be documented and administered through objective, transparent allocation. Restrictions shall be proportionate to the resource actually constrained and reassessed as conditions change. A constraint shall not justify reserving unrelated benefits for selected providers.

(vi) Comparable services and noncash benefits. Different benefits may compensate objectively different obligations or distinct services. Every corresponding opportunity

> shall be available to qualified providers able to undertake comparable obligations. Comparisons shall address the complete economic package and use an objective, documented valuation method where identical compensation is impracticable. Distinct or indivisible services may be procured through a fair, transparent process; bundling them with liquidity services shall not exempt comparable liquidity compensation from parity.
>
> (vii) Indirect action. A designated contract market shall not avoid this paragraph by acting through an affiliate or by placing liquidity compensation in another form of agreement.

The Commission should replace the entirety of proposed § 38.852(c)(1)(i), including its separate requirement that the affiliate be filled last at every price level, with the following: "The designated contract market's trade matching system shall apply its published matching algorithm to the bids and offers of the affiliate market maker on the same terms as to those of every other member, without preferential matching, latency, or access; provided that the designated contract market may adopt a disclosed customer-priority rule applicable equally to every professional liquidity provider, whether affiliated or unaffiliated, under which eligible customer bids and offers are filled before professional liquidity-provider interest at the same price." The Commission should specify customer and professional-provider criteria appropriate to the market and safeguards against circumvention through account labels.

In proposed § 38.852(c)(1)(ii), "on terms no less favorable to the designated contract market than" should be replaced with "on terms equivalent, for comparable obligations, to." The inventory restriction should expressly permit positions acquired in meeting quoting obligations, positions that reduce or hedge that inventory, and positions held through resolution under documented risk limits. That clarification would preserve bona fide market making while excluding unrelated proprietary strategies.

The Commission should also expressly permit advance distribution of listing, contract-specification, incentive-program, and necessary technical information to qualified liquidity providers and applicants preparing to qualify, where eligibility is objective and published, the same information is available simultaneously on equal terms, and appropriate confidentiality and security protections apply. This permission should not extend to nonpublic customer orders or positions, surveillance or investigation records, pending discretionary outcome determinations, or other restricted information. The Commission should reconcile the exception with the proposed acceptable practice requiring distribution to all market participants, so that neutral preparation by eligible providers is clearly permitted.

The core information-protection and documented-conflicts requirements should apply to significant liquidity counterparties under a definition and materiality standards developed from the record, with independent disciplinary review and appropriate recusals. The regulatory oversight committee should oversee parity compliance and discretionary outcome determinations, and the exchange should monitor dependence on a sole provider. The Commission should calibrate their precise scope using the agreements and supervisory evidence it obtains under Regulation 38.5.

Novig supports the proposal and recommends that the Commission direct this rule at the competitive problem present in the market today: unequal access to the benefits exchanges provide for liquidity. Its own economic analysis finds that incentive parity protects fair

competition, attracts market makers, and improves price discovery and risk management. Those findings support extending parity to every exchange-supported liquidity arrangement, with open eligibility and records of the benefits actually provided, while preserving information barriers and independent oversight and replacing ownership-based handicaps with neutral rules. The Commission should use its part 38 authority to obtain the agreements and records needed to calibrate those requirements, and if it retains affiliate-specific conditions, it should at a minimum adopt the modifications described above. That approach would better satisfy sections 15(a) and 15(b) and the core principles requiring competitive, open, and impartial markets. We appreciate the opportunity to comment and would welcome discussion of these recommendations with the Commission and its staff.

Respectfully submitted,

Novig