October 5, 2026

VIA Email: secretary@cftc.gov

Mr. Christopher Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

Re: RIN 3038—AF76: Notice of Proposed Rulemaking: Conflicts and Affiliations

Dear Mr. Kirkpatrick:

National Futures Association (NFA) welcomes the opportunity to comment on the Commodity Futures Trading Commission's (CFTC or Commission) Notice of Proposed Rulemaking (NPR or Proposal) regarding *Conflicts and Affiliations*.[1] The Commission's NPR indicates that it developed this Proposal, in part, based on the responses it received from its June 27, 2023 request for comment on the *Impact of Affiliations on Certain CFTC-Regulated Entities (*Affiliations RFC).

The June 2023 Affiliations RFC sought input about three separate affiliate relationships-derivatives clearing organizations (DCOs) and affiliated futures commission merchants (FCMs); designated self-regulatory organizations (DSROs) and FCMs; and designated contract markets (DCMs)/swap execution facilities (SEFs) and affiliated intermediaries (*e.g.,* FCMs, IBs, CTAs, and CPOs). In our view, the 2023 release raised important questions about the existing market structure in which DCOs, DCMs, and SEFs supervise the conduct of their members and participants when affiliate relationships exist. In submitting comments in response to the current NPR, NFA reviewed the Affiliations RFC and NFA's September 26, 2023 comment letter (NFA September 2023 Comment Letter) and incorporates those comments herein.

Today, under Chairman Selig's leadership, the Commission is proactive by advancing the *Conflicts and Affiliations* NPR. Markets and market structure continue to evolve at an ever-increasing pace, including with an increase in affiliated relationships among market participants. NFA's September 2023 Comment Letter noted that there were four registered FCMs and two pending FCMs with DCM affiliates. Since then, those numbers have grown exponentially to fifteen registered FCMs and six pending FCMs with DCM affiliates. In light of this growth, NFA commends this Commission for

[1] NFA's Board of Directors reviewed this letter prior to submission to the CFTC and, other than CME Group Inc., the Board is in full support of the letter.

its continued focus on the identification, disclosure, mitigation, and elimination, as appropriate, of actual and perceived conflicts of interest arising from FCMs', SEFs', DCMs' and DCOs' relationships with certain affiliated entities.

NFA is the industrywide independent self- regulatory organization (SRO) for the derivatives industry and does not operate a market or have affiliated entities. As an SRO, NFA provides front-line oversight of CFTC-registered market participants, including registered entities directly impacted by the Proposal. Currently, NFA is the DSRO for 30 FCMs. In performing our SRO functions, we work very closely with the Commission, and our principal objective is to assist the CFTC in overseeing the derivatives industry. NFA also contracts with certain DCMs and SEFs to perform regulatory services on their behalf, including trade practice and market surveillance, audit trail reviews, and reporting and recordkeeping.

Accordingly, many of NFA's comments address those portions of the Proposal which, if enacted, may directly implicate NFA in either its function as an SRO or an independent regulatory service provider (RSP) (*i.e.,* an RFA or registered entity), or the DSRO framework. Further, NFA recognizes that the Proposal has the potential to materially impact the operations of certain registered entities, including those with affiliate relationship(s), and NFA encourages the Commission to carefully consider the comments of those impacted market participants.

The Commission's Proposed Amendments to Regulations 1.52, 38.604, and 38.606

The Proposal indicates that while the Commission believes that market structure innovation and competition, subject to appropriate safeguards, advances the Commission's mission of promoting the integrity, resilience, and vibrancy of the U.S. derivatives markets, the Commission also recognizes that potential conflicts of interest arising within these market structure changes from affiliated relationships may pose certain risks to unaffiliated market participants, including retail customers. The comments below focus on specific issues raised by certain of the proposed amendments and provide responses to specific relevant questions raised in the Proposal.

The DSRO of an Affiliated FCM

CFTC Regulation 1.52 establishes the minimum standards that all SRO programs must satisfy to carry out their financial supervisory obligations. FCM financial oversight is reliant upon the longstanding framework in which DCMs and registered futures associations (RFAs) (*e.g.,* NFA), in their capacity as SROs, are largely responsible for adopting financial and related reporting requirements and for examining their members for compliance with those requirements. This regulatory oversight

framework relies heavily on the SROs' Joint Audit Program,[2] by which SROs delegate certain monitoring and examination functions to a DSRO.

As the Commission is aware, not all DCMs conduct periodic examinations of their FCM members. CFTC Regulation 1.52(d) allows DCMs to delegate the SRO functions described in CFTC Regulations 1.52(b) and (c) (*e.g.,* on-site examinations) to a DSRO. The delegator DCM remains responsible, however, as an SRO for its FCM members' compliance. Today, only one DCM, CME Group, Inc. (CME), acts as a DSRO and conducts examinations of its clearing member FCMs. NFA conducts examinations of any FCM that is not a CME clearing member.

CFTC Regulation 1.52 does not currently address, including prohibit, a DCM/SRO acting as the DSRO for its own affiliated FCM. Unquestionably, when a DSRO shares a common ownership interest with an affiliated FCM, the DSRO has a perceived material conflict of interest:—it may be more lenient examining its affiliated FCM. Over the years, DCM/SROs have recognized this significant potential conflict of interest, and they have requested that NFA act as the DSRO for their affiliated FCMs. NFA acts as the DSRO for twelve FCMs that are affiliated with a DCM and has been able to seamlessly accept DSRO responsibilities for them.

To mitigate this conflict, the NPR proposes to codify current practice by prohibiting a DCM/SRO from acting as the DSRO for its affiliated FCM, and instead, would require the DCM/SRO to designate an independent third-party SRO to perform CFTC Regulation 1.52(c)'s financial surveillance obligations. Consistent with NFA's September 2023 Comment Letter, NFA fully supports this prohibition and has the capacity to take on DSRO responsibilities for additional FCMs affiliated with DCMs.

The FCM DSRO Function

The Proposal states that a "distinct concern" arises when a DCM/DSRO examines non-affiliate FCMs when that DCM/DSRO has an affiliate FCM competing in the same markets. The Commission observes that in these situations, a DSRO obtains for each FCM it examines significant non-public information, including detailed financial information, operational procedures, customer activity, market positions, and risk management practices. The NPR opines that the DSRO's acquisition or sharing of this information gives rise to both a competitive concern—the information could advantage the DSRO's affiliated FCM—and a concern that the DSRO's oversight decisions affecting non-affiliated FCMs could be perceived as benefiting its affiliate. Further,

[2] As the Commission's NPR notes, CFTC Regulation 1.52 permits two or more SROs to file a plan with the Commission to delegate the oversight responsibility to a DSRO for an FCM that is a member of those SROs. The Joint Audit Committee (JAC) maintains the Joint Audit Program.

under the current DSRO framework, non-affiliate FCMs are not afforded any means for examination by an SRO that has no commercial interest in its activities.

Therefore, to "provide a direct, registrant-side response" to this latter concern, the Proposal affords each FCM the option to elect NFA as its DSRO (DSRO Election Provision). Further, the Proposal establishes certain safeguards that would require an SRO with an affiliate FCM to create separate reporting lines for staff performing SRO functions and, except as necessary to comply with the SRO's responsibilities and obligations, prohibit an SRO from either accessing non-public information of its affiliate FCM or sharing, directly or indirectly, non-public information obtained from non-affiliate member FCMs. These information barriers are consistent with barriers required by existing CFTC rules with respect to other activities.[3]

The Commission poses several questions and requests input about how SROs would work with the JAC to implement the DSRO Election Provision. As the Commission is aware, the JAC has a longstanding history of delegating responsibilities to a DSRO to conduct prudent risk-based examinations without duplicating efforts among multiple SROs, including NFA. The Commission's DSRO Election Provision continues to permit a structure with multiple DSROs. However, NFA has been advised that industry participants, including FCMs, may recommend that the Commission mandate that an RFA serve as the DSRO for all FCMs. If the Commission adopts this type of DSRO mandate (DSRO Mandate), NFA does not object and assesses the impact on NFA of a DSRO Mandate as identical to that presented under the DSRO Election Provision if all FCMs elect to move to NFA. As further explained below, NFA is fully prepared to secure the necessary resources to act as the DSRO for all FCMs, which would foster a framework of consistent exam approaches and rule interpretations, and potential enforcement actions.

Under either a DSRO Election Provision or DSRO Mandate, it is imperative that SROs continue to cooperate and work within the JAC framework to ensure that their members meet their obligations. For example, the current JAC agreement provides that DSROs must share information, including reports of each risk-based examination, with each SRO of which the examined FCM is a member. Further, a DSRO upon written request shall provide each SRO of which the examined FCM is a member full access to the working papers generated during an exam. This important oversight information should continue to be voluntarily shared at no charge going forward.[4] Further, NFA remains committed to continuing to work closely within the JAC

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[3] For example, CFTC Regulations 23.605 and 1.71 require information barriers in the context of research and activities relating to a firm's business trading and clearing units.

[4] NFA recognizes that DCMs/SROs and their DCOs also have financial and risk oversight obligations pursuant to CFTC Regulations Part 38 and 39, respectively. To the extent not already covered by the JAC Agreement, NFA is willing to establish a mechanism to share information, as requested by

structure to ensure that examination modules are updated for changing risks, examination standards remain applicable, and other SROs are afforded an opportunity to contribute to the process and have their recommendations considered and adopted, as appropriate.

Current CFTC Regulation 1.52(c)(1)(i) requires DSROs to maintain staff of an adequate size, training, and experience to effectively implement a supervisory program, which includes discharging the CFTC Regulation 1.52's obligations. Today, NFA complies with CFTC Regulation 1.52(c)(1)(i)'s requirements for their respective oversight of FCMs. Further, our FCM oversight program is aligned with CME's program. The JAC develops uniform FCM examination modules[5] and has adopted common examination standards approved by the CFTC.

NFA's views and responses to those portions of the NPR that would directly impact NFA's operations are set forth below.

Questions 15 and 20: Resources and Funding

Today, NFA maintains staff of adequate size, training, and experience to not only conduct examinations of FCMs for which NFA acts as the DRSO but also to monitor those FCMs' activities each day. To perform this oversight, NFA has developed and implemented a comprehensive set of rules[6] and the necessary systemic infrastructure to perform several critical functions, including with respect to: (1) segregated funds, whereby NFA confirms daily all customer segregated, secured, and cleared over-the-counter collateral fund balances by obtaining confirmation statements directly from the depositories that hold these balances; (2) capital compliance, by reviewing monthly unaudited financial statements and certified annual audited financial statements; (3) operational risk, where NFA reviews each FCM's quarterly Risk

DCM/SROs and DCOs, for them to meet their Part 38 and 39 obligations, relating to NFA's periodic DSRO examinations and our ongoing surveillance of FCMs' activities.

[5] CFTC Regulation 1.52(d)(2)(ii)(A) requires that the Joint Audit Program assess FCM compliance with minimum net capital and related financial requirements, the obligation to segregate customer funds, risk management requirements, including policies and procedures relating to the receipt, holding, investment, and disbursement of customer funds, financial reporting requirements, recordkeeping requirements, and sales practice and other compliance requirements.

[6] CFTC Regulation 1.52(b) requires each SRO to adopt minimum financial and related reporting requirements, and risk management requirements, for FCMs. NFA Financial Requirements Sections 1, 4, 7, 8, 9, 10, and 16, and NFA Compliance Rule 2-26, impose various financial, operational, risk, and reporting obligations on NFA Member FCMs. In addition, NFA FCM Members must comply with NFA Compliance Rules 2-8, 2-9, 2-10, 2-29, and 2-30, which address supervision, sales practices, AML requirements, and recordkeeping obligations.

Exposure Report and any notification(s) made to NFA upon the occurrence of certain events that would materially alter an FCM's risk profile; (4) compliance monitoring, which entails a review of the annual Chief Compliance Officer Report required under CFTC Regulation 3.3(e); and, (5) reviewing and, if applicable, investigating any complaint filed by the investing public.

NFA acts as DSRO for FCM/broker-dealer entities. Moreover, NFA's swap dealer (SD) examinations oversee covered SDs' compliance with NFA/CFTC capital and initial margin (IM) requirements, which include analyzing financial statements and capital/margin models of large, complex global financial institutions. Currently, NFA oversees 32 SDs (28 corporate families) for capital compliance[7] and 43 SDs (29 corporate families) for IM compliance.[8]

At this time, NFA is uncertain if the DSRO Election Provision will have a material impact on NFA's resources and staffing. This uncertainty arises from the current lack of knowledge about how many, if any, NFA Member FCMs may exercise this election and request that NFA serve as their DSRO. If a few FCMs exercise this election, then there would be no material impact. If a larger number do so or if the Commission adopts the DSRO Mandate, then there would be a greater impact that NFA would prudently manage by hiring individuals with FCM examination and oversight experience. With respect to the potentialities under either the DSRO Election Provision or DSRO Mandate, NFA is well prepared to address our resource and staffing needs. As evidence, since 2025, NFA's FCM DSRO responsibilities have increased from twenty-one to thirty FCMs. To address our expanding FCM resource needs, NFA has relied upon external hiring, shifting internal resources, and training and developing staff to ensure that we have highly qualified and proficient FCM examination and oversight staff.[9]

Additionally, throughout its history, when NFA's role has expanded to assume additional oversight functions (*e.g.*, retail foreign exchange dealers, swap dealers), NFA has seamlessly secured and allocated resources to perform the required

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[7] NFA has experience and expertise in examining SDs for capital compliance with respect to three alternative capital computational approaches: net liquidating assets (*e.g.,* FCM/broker-dealer capital), bank holding company, and tangible net worth.

[8] Moreover, if NFA is the DSRO for an FCM that is also an SD or has an SD affiliate, NFA would seek to coordinate the examinations of these FCMs/SDs, if appropriate.

[9] In addition to internal and sponsored training and professional development, NFA examination staff are required to successfully complete the Series 3 exam and Swaps Proficiency Requirements mandated for certain NFA Member associated persons. Additionally, they are required to obtain Certified Fraud Examiner credentials and meet the continuing education requirements established by the Association of Certified Fraud Examiners.

oversight responsibilities. NFA currently believes that its FCM assessment fee paid by customers is a sufficient revenue source to pay for undertaking the additional responsibilities associated with serving as an effective and adequately resourced DSRO for FCMs.[10]

In sum, under either the DSRO Election Provision or DSRO Mandate, NFA maintains a well-established infrastructure and revenue mechanism to ensure that it has adequate operational resources, staffing, and funding to effectively fulfill its DSRO obligations for FCMs pursuant to CFTC Regulation 1.52.

Questions 10 through 13: Notice Periods and Cycle Duration of the Proposed DSRO Election Provision

If the Commission adopts the proposed DSRO Election Provision, then NFA recognizes that it must work very closely with JAC, the current other DSRO (*i.e.,* CME), and the CFTC to determine the logistics associated with the transfer of any DSRO responsibilities. NFA agrees with the Commission that a DSRO accumulates significant expertise in overseeing FCMs and, during any period of transition, DSROs must collaborate and share historical and current examination data to ensure consistent and effective regulatory FCM oversight.

The Proposal correctly notes that the DSRO Election Provision, if given immediate effect, may impair a DSRO's ability to recruit, train, and deploy qualified examination staff. NFA believes that any transition between DSROs must be handled correctly to avoid potential short-term disruptions. NFA has a long-standing history of actively collaborating within JAC and, importantly, effectively transitioning FCM oversight responsibilities over the years to and from other DSROs. During these prior transitions, NFA closely coordinated with JAC to ensure each respective DSRO fulfilled its minimum examination cycle obligations pursuant to CFTC Regulation 1.52.

Based on our experience with prior transitions, NFA believes the proposed six-month minimum notice period strikes the appropriate balance between an electing FCM's interest in a timely transition and the DSRO's ability to absorb DSRO responsibilities for the FCM. However, there may be circumstances in which multiple FCMs select NFA as their DSRO at the same time or in very close succession. Depending on the number of FCMs electing NFA, and the size, scope, and complexity of those FCMs' operations, six months may not afford an adequate transition period. As such, NFA supports the Proposal's language that allows JAC to establish a reasonable

[10] In May 2026, NFA's Board of Directors reduced NFA's FCM assessment fee to $.02 r/t futures contract effective July 1, 2026 through June 30, 2027. The Board's objective is to draw down NFA's reserves. As of July 1, 2027, the fee may revert to $.04 r/t per contract.

phase-in schedule for the FCMs' elections' effective dates, not to exceed 12 months following the required notifications. Similarly, the JAC may face the rare occurrence where resolution of a DSRO's investigation or remediation of material exam deficiencies may extend beyond twelve months. If this occurred, the DSRO and the JAC should have the flexibility to limit an FCM's ability to elect a new DSRO until these events are resolved.

With respect to the DSRO Election Provision's requirement that an FCM, following the effective date of an election, retain its elected DSRO no fewer than three examination cycles, NFA respectfully requests that the Commission extend this period to five exam cycles. NFA agrees with the Commission that a minimum exam cycle requirement is critical to prevent repeated switching that would impose recurring transition burdens on DSROs, complicate the continuity of examinations and negate the staffing investment that a DSRO must make to absorb electing FCMs. As support for this request, NFA notes that while CFTC Regulation 1.52 mandates that a DSRO examine an FCM once every 18 months, CFTC Financial and Segregation Interpretation 4-2 (CFTC Interpretation 4-2) sets forth a slightly shorter mandatory cadence for exams. Specifically, CFTC Interpretation 4-2 requires that DSROs examine an FCM within nine to 15 months of the prior examination.

As a practical matter, since January 2022, NFA's FCM exams average 13 months between exams, which for a three-exam cycle equals just over three years. The Commission's proposal appears to utilize CFTC Regulation 1.52's 18-month examination period, which would correctly set a three-examination cycle at four-and one-half years. The CFTC's NPR suggests that four and one-half years should appropriately reflect the period necessary to balance NFA's continuity and staffing interests against an FCMs interest in its ability to revisit its election, and NFA agrees with this proposition. Therefore, to achieve the Commission's expected four-and one-half year period, NFA requests that the Commission modify the proposal to require FCMs to retain an elected DSRO for not fewer than five complete exam cycles.

The Commission's Proposal also requests comment about the circumstances that would permit an FCM to revoke its election prior to the elapse of the minimum duration period, and whether those circumstances should account for certain "material" changes under which an FCM may seek a new election. As a practical matter, if a DCM/SRO is acting as the DSRO for an FCM that withdraws its membership from the DCM/SRO, then the DCM/SRO will transfer its DSRO responsibilities to another SRO as required under existing JAC standards. NFA believes that this DSRO allocation arrangement should remain in place if the Commission finalizes its Proposal. NFA further requests that the Commission establish within CFTC Regulation 1.52(d)(2)(i)(D) extenuating and unforeseen circumstances (*e.g.,* a merger, acquisition, or significant enforcement action against the DSRO) under which an FCM is permitted to revoke its election prior to the elapse of the minimum exam duration period. In doing

so, the Commission is making clear that, absent one of the specified circumstances, an FCM may not revoke its election. This avoids the situation in which an FCM may attempt to change its election merely because it is dissatisfied with a DSRO's examination findings, an outcome that would weaken the integrity and public trust in the DSRO framework.

Other Matters

The NPR's Question 7 asks whether CFTC Regulation 1.52, as proposed, should apply to SRO oversight of an affiliate introducing broker (IB), or market maker. Our comments relating to market makers are set forth beginning on page eleven. All registered IBs are NFA Members and subject to our examination oversight, so if the CFTC determines to adopt this provision, from NFA's perspective there should be little, if any, practical implication as to how NFA fulfills its oversight of IBs.

CFTC Financial and Segregation Interpretations 4-1 and 4-2 supplement CFTC Regulation 1.52 by providing instructions to DSROs regarding examinations of FCMs, among other requirements. The Commission last modified these Interpretations in 1985 and 1999, respectively, and the industry has continued to evolve with the introduction of new products, business practices and risks, and additional regulatory requirements. Both Interpretations would benefit from updates to outdated requirements and overall modernization for current examination practices. If the Commission elects to undertake an update process, NFA welcomes the opportunity to engage further with Commission staff and JAC members on potential updates to these Interpretations.

Part 38—Financial Surveillance and Third-Party Regulatory Service Providers

As the Commission notes, DCM Core Principles, and CFTC Regulation 38.604, require a DCM to monitor its member FCMs for compliance with the DCM's minimum financial standards, which includes the requirement to "continuously monitor the positions of members and their customers" and to continually survey the obligations of each FCM created by the positions of its customers (hereafter referred to as Intra-Day Financial Surveillance). Further, since its adoption in 2012, CFTC Regulation 38.606 has permitted but not required DCMs to outsource their Intra-Day Financial Surveillance obligations to an RSP.

The Commission notes its preliminary belief that a DCM's financial surveillance of an affiliate FCM presents potential conflicts of interest that may not be addressed by the current CFTC Regulations and, accordingly, the Commission proposes that a DCM can comply with CFTC Regulation 38.604's Intra-Day Financial Surveillance obligations by either outsourcing them to an RSP, or by adopting and implementing procedures to identify, address, and manage conflicts involving its affiliate FCM.

Question 24: Mandatory RSP Designation

NFA recognizes that if a DCM determines to outsource its Regulation 38.604 obligations to an RSP, it may help mitigate any real or perceived conflicts of interest that may exist if a DCM elects not to adopt and implement the conflict-of-interest procedures contemplated under the Proposal. Further, while it is true that NFA currently performs market regulation functions as an RSP for several DCMs[11] and as an RFA separately receives on a routine basis periodic financial information from FCMs for which it is the DSRO, no DCM either before or after the Commission adopted CFTC Regulation 38.606 has outsourced their Intra-Day Financial Surveillance obligations to NFA.[12]

Further, NFA understands that DCMs in discharging their Intra-Day Financial Surveillance obligations may rely, in part, on their DCOs to supplement these obligations by obtaining critical and timely information regarding changes in margin and collateral requirements, position offsets, variation margin pay/collect amounts, and other risk metrics internal to the DCO. This may be an indication that DCMs have determined it is more prudent, from a risk-management perspective, to perform Intra-Day Financial Surveillance within the DCM/DCO structure, rather than outsource these functions to an RSP. Therefore, NFA strongly supports the Commission's core principles approach, which permits a DCM to adopt mitigants for managing conflicts of interest rather than adopting a mandatory obligation to designate an RSP to perform Intra-Day Financial Surveillance obligations for all DCM members, including its affiliate.[13] Further, NFA encourages the Commission to closely consider the views of DCMs/DCOs as to the specifics of these mitigants involving separate applications and systems, personnel, and office space.

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[11] NFA's Market Regulation Department provides third-party regulatory services to DCMs and SEFs as follows: trade practice and market surveillance, investigations, referral of disciplinary matters, and audit trail reviews. NFA currently provides regulatory services to three DCMs, 11 SEFs, two additional DCMs that the Commission has approved but are not yet active and six other DCMs and two SEFs, which are pending regulatory approval with the Commission.

[12] If a DCM determines to outsource under CFTC Regulation 38.606 its CFTC Regulation 38.604 obligations to an RSP, the RSP would have to closely coordinate with a DCM, and its DCO, to ensure reliable and timely access to position data, margin requirements, and other risk information that would be relevant to understand the DCM's members' obligations. Further, in a volatile stressed market environment, DCMs and DCOs, not an RSP, have the most current information for positions across all its members and may be best situated to react in real-time to mitigate market risks and disruptions.

[13] NFA believes that it is important for a DCM to clearly disclose all affiliate relationships. Accordingly, we would support requiring a DCM with an affiliate FCM to clearly and prominently disclose the affiliate relationship to all DCM participants, including that the DCM conducts Intra-Day Financial Surveillance for all DCM members, including its affiliate.

Question 28: Estimated Cost

As noted above, NFA has significant experience in providing market regulation services to assist DCMs and SEFs with meeting their non-financial-related obligations. Since NFA does not currently provide Intra-Day Financial Surveillance functions for any DCM, it is difficult to predict the estimated costs of doing so. NFA would need to closely review the data, systems, and additional staffing needs necessary to assume these responsibilities. This analysis will likely vary based on the products available to trade and the member financial requirements of each DCM. Further, any costs will also be highly dependent upon the number of DCMs that seek to outsource these functions given economies of scale.

Exchange-Related Conflicts and Mitigation

Proposed New Commission Regulations 38.852 and 37.201—Conflicts of Interest Involving an Affiliate Market Participant

The Commission's NPR also addresses conflicts of interest that arise when a DCM or SEF is affiliated with a market participant that directly or indirectly executes, introduces, or otherwise facilitates trades on its exchange. The NPR distinguishes between the conflict that arises when an affiliate market participant (AMP) acts as an intermediary (*e.g.*, FCM or IB) that trades on behalf of customers versus an AMP that acts as a principal trading firm (*e.g.*, a hedge fund or market maker) trading on its own behalf. While DCM Core Principle 16 and SEF Core Principle 14 direct DCMs and SEFs to establish and implement rules designed to minimize conflicts of interest in their decision-making process and establish a process to resolve them, the NPR indicates that these existing Core Principles do not specifically address conflicts that arise when an exchange has an AMP(s).

The Commission's NPR, therefore, proposes to address these conflicts by establishing a principles-based conflicts-of-interest framework for any AMP acting as an intermediary and trading on an affiliated DCM or SEF. This framework is reliant, in part, on the adoption of acceptable practices to Appendix B of CFTC Regulation Parts 37 and 38 to provide guidance regarding the appropriate separations (*e.g.,* applications and systems, personnel, office space) between a DCM or SEF and an AMP. NFA is supportive of this approach and the need for appropriate separations in these key areas but encourages the Commission to closely consider the views of DCMs/SEFs, particularly with respect to the specific constraints placed on sharing office space and personnel.

Though the Commission preliminary believes the proposed principles-based conflicts-of-interest approach will be sufficient to address conflicts arising from an affiliated intermediary, it makes a preliminary determination that these safeguards do

not adequately minimize the conflicts presented by an affiliate principal trading firm (APTF), which are neither Commission registrants nor NFA Member firms. Consequently, to sufficiently mitigate conflicts associated with APTFs, the Commission's NPR proposes to prohibit an APTF from trading on an affiliated DCM unless it meets the proposed definition of an "affiliate market maker" and the DCM complies with certain Commission-established safeguards for its APTF's market-making activities.

These safeguards include adopting conflicts of interest procedures to identify, address, and manage conflicts involving an AMP (an affiliate FCM or APTF), which shall, at a minimum, address and provide appropriate separations (*e.g.,* applications and systems, personnel, office space) in key areas. A DCM must also meet proposed CFTC Regulation 38.852(c)'s trading obligation requirements for APTFs acting as market makers[14] relating to trade-execution subordination and written market making or liquidity provider incentive agreements, which at minimum must contain requirements that the APTF maintain continuous two-sided quotes, uphold its obligations for a minimum number of trading hours, and its trading reasonably contribute to the market in a fair and orderly manner.

Of particular interest to RSPs, including NFA, the NPR requires a DCM that permits an APTF to trade on its market to designate an RSP to conduct intra-day financial surveillance of an APTF as if it was an FCM (with respect to the DCM's CFTC Regulation 38.604 obligations).[15] Further, pursuant to proposed CFTC Regulation 38.852(c)(2), the NPR requires an RSP to review and monitor the DCM's compliance with its conflict-of-interest procedures applicable to an AMP and annually certify to the Commission and the DCM's Board of Directors (or other similar body or officer responsible for regulatory compliance) that the APTF acting as a market maker satisfies the aforementioned proposed conflicts of interest and market-making trading obligation requirements.

NFA recognizes that an APTF trading on an affiliated DCM presents a fundamentally different conflict than an AMP acting as an intermediary (*e.g.*, FCM or

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[14] Proposed CFTC Regulation 38.852(b)(2) provides that if a DCM offers an incentive or similar program filed under Part 40 of the Commission's Regulations that applies to APTFs, the DCM must have procedures to ensure that the DCM's unaffiliated members can participate in such programs on terms no less favorable than those offered to an APTF. Irrespective of this Proposal, NFA strongly recommends that the Commission adopt and enforce a requirement for DCMs to identify and maintain a record of members who participate in each respective incentive or participation program.

[15] NFA acknowledges that if the NPR is finalized as proposed, a DCM with an APTF may seek to utilize NFA as its third-party independent RSP. With respect to conducting certain intra-day financial surveillance of a DCM's "affiliate market maker" as if it was an FCM, NFA's comments above relating to acting as an RSP for a DCM's affiliated FCM apply equally in this context.

IB). If the Commission is not going to prohibit APTFs[16], then a few DCMs may allow them to trade (or continue to trade) on their markets. DCMs are SROs, and they are obligated to comply with the Commodity Exchange Act's (Act) Core Principles, including Core Principles 12 and 16, and Commission Regulations with respect to their APTF's activities. DCMs have an obligation to operate fair and orderly markets and to surveil their participants, including an APTF(s). The Commission acts as the front-line regulator for DCMs and performs rule enforcement reviews of their activities and compliance with the DCM Core Principles, which would entail reviewing a DCM's APTF trading activities and the DCM's compliance with any Commission established requirements relating thereto.

NFA believes that these DCMs, and not an RSP, should ensure and certify that their own APTFs comply with any Commission-established conflicts of interest and market making trading obligation requirements. Therefore, we strongly recommend that proposed CFTC Regulation 38.852(c)(2) be amended to require a DCM [not an RSP] to review and monitor its compliance with its conflict-of-interest procedures applicable to an AMP, and its Chief Executive Officer and/or Chief Regulatory Officer should annually certify to the Commission that an APTF acting as a market maker satisfies any Commission-established market making trading obligation requirements. The type of review contemplated by proposed Regulation 38.852(c)(2)(iii) would require an analysis of a DCM's full electronic audit trail data, including all bids, offers, modifications, trades and other messaging. DCMs possess the critical data to perform this analysis and are appropriately equipped to evaluate if its APTF is complying with proposed Regulation 38.852(c)(1)(ii)(A)-(D)'s requirements.

If the Commission does not adopt NFA's recommendation and finalizes CFTC Regulation 38.852(c)(2), as proposed, then NFA as an RSP will work with the Commission and impacted DCMs to further define the contours of the analysis required, particularly to determine if a DCM's APTF has satisfied the conditions set out in proposed CFTC Regulation 38.852(c)(1). A DCM with an APTF can certainly submit its full electronic audit trail data to an RSP to perform the review required by CFTC Regulation 38.852(c)(2)(iii) and an RSP will likely charge considerably for this review.[17]

Further, NFA also encourages the Commission to consider whether an RSP is critical to performing the analysis proposed. DCMs may want additional

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[16] NFA strongly encourages the Commission to carefully consider the comments from other market participants, including non-affiliate market makers, as to whether the Commission should prohibit DCMs from having APTFs.

[17] In NFA's view, an RSP is not going to certify to the Commission that a DCM complies with proposed CFTC Regulation 38.852(c)(1) for its APTF unless the review performed by the RSP is exhaustive as to the APTF's market making activities on the DCM.

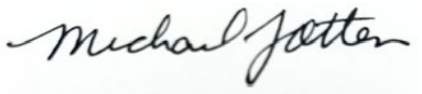
flexibility as to persons (*e.g.,* third-party trade surveillance firms) who may be qualified to perform this review. NFA recommends that they have that flexibility provided they are held responsible for the third party's selection and performance.[18]

Last, although not currently proposed, NFA strongly encourages the Commission to adopt safeguards within proposed CFTC Regulation 38.852 that requires DCMs to (1) publicly disclose to market participants that an APTF trades on its market and (2) be required to provide material data as to the extent of the APTF's trading activity (*e.g.,* what percentage of the time is the APTF the counterparty on trades). This type of disclosure's objective is no different than the disclosures that FCMs must provide to customers pursuant to CFTC Regulation 1.55(k). Just as an FCM's business and financial information is extremely relevant to its customers, data relating to a DCM's APTF's trading activity is critical information for market participants to evaluate to determine whether to trade on the DCM.[19]

In conclusion, thank you for your consideration of NFA's comments, and NFA again applauds the Commission under Chairman Selig's leadership for addressing the conflicts arising due to changes in market structure. NFA is a strong supporter of the SRO model, the DSRO framework, and the historical expertise housed within the JAC that have served this industry extremely well over the decades.

As always, NFA stands ready to work with the CFTC, the JAC, and market participants to carefully implement any final rules the Commission determines to adopt. If we can provide any further information or other assistance, please do not hesitate to contact Dale Spoljaric, Vice President, Capital and Exams (dspoljaric@nfa.futures.org) or me (motten@nfa.futures.org).

Respectfully Submitted,



Michael J. Otten
Senior Vice President, Head of Member Oversight

[18] Many CFTC registrants, including DCMs, utilize third-party service providers that are not RSPs to assist in complying with their various regulatory obligations.

[19] Similarly, pursuant to CFTC Regulation 5.18(e)(1), retail forex dealers, which offer trading platforms and act as counterparty to retail customer transactions, must disclose for the preceding four calendar quarters their total number of non-discretionary customers and the percentage of accounts that were profitable or not profitable.