COMMODITY FUTURES TRADING COMMISSION

DIVISION OF CLEARING AND RISK

ROUNDTABLE ON EXISTING, NEW, AND EMERGING ISSUES IN CLEARING

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Three Lafayette Centre

1155 21st Street Northwest

Washington, D.C. 20581

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P R O C E E D I N G S

MR. HUTCHISON: All right. Good morning. We're going to start off with some brief opening remarks by the chairman, and from there, some remarks by the commissioners, and then back to me. And I'll give some administrative items and get the day started.

But I'll just say a general welcome to everyone. Thank you for coming. And I'll turn it over to Chairman Behnam.

CHAIRMAN BEHNAM: Thanks, Clark.

MR. HUTCHISON: Mr. Chairman?

CHAIRMAN BEHNAM: Thanks. I appreciate everyone being here, different context this morning than our usual advisory committee meetings, but equally if not more important issues. So I do want to thank everyone for taking time out of their busy schedules, flying in from out of town. The series of issues that we're going to discuss -- and credit to Clark and DCR in pulling Gary out of retirement, which is no easy task.

I joke, but these are tough issues. I'm sure if you follow the agency, you've seen we've been dealing with a number of new structures, new ideas, which is fine, it's technology, it's disruption in our markets, and I think in the end it'll benefit the efficiency of markets.

But as we're going through these growing pains, we want to engage. We want to have a sort of inclusive tent to make sure that we're getting all the thoughts and ideas about what we should do, how we should do it going forward. There's issues around law, there's issues around policy, and there's issues around risk at the minimum. So we want your thoughts and feedback as we move forward as an agency under my chairmanship and beyond because I don't suspect these issues are going to change or veer off the course anytime soon. So I'm looking forward to listening to today's conversation.

Again, big thanks to Clark and the team at DCR for thinking of this event and this day, and I think we're going to all learn a lot from each other and hopefully take some positive things away so that we can ultimately achieve our shared interest of stronger, transparent markets, which I know we all want to have. So, Clark, I'll pass it back to you. Thanks.

MR. HUTCHISON: Thank you, Mr. Chairman. The commissioners couldn't be here today, but we have recorded statements from Commissioner Pham and Commissioner Mersinger, and so we're going to start off with Commissioner Mersinger. And I'll indicate to the AV people, can you please start the recording from Commissioner Mersinger?

COMMISSIONER MERSINGER: Good morning. Thank you all for taking time out of your busy schedules to be here today for this important and timely discussion that I know will benefit from the expertise of each of you gathered for today's roundtable. I value each of your perspectives. I wish I could have joined in person, but, unfortunately, I had a preexisting engagement today.

I want to thank all the panelists here, as well as both Clark Hutchison and Gary DeWaal, for their time and commitment in planning what I'm sure will be a robust discussion. Preparing for these roundtables consumes significant time and energy, but I believe these discussions are part of the deliberative regulatory process which requires this level of public engagement.

Our markets are as vibrant and dynamic as ever, and, as a result, the Commission is faced with new market structures, products, and participants. And since 2009, the clearing of derivative transactions has been internationally accepted as a central benefit to systemic risk reduction in our financial markets. The development of sound clearing practices and operations around new market structures requires consistent engagement by all market participants and regulators to ensure we continue to meet the overall goal of reducing risk. The Commission must comprehensively assess how new models fit within its principles-based authorities, while continuing to promote responsible innovation and fair competition.

Our job as a market regulator works best when we engage directly in forums like this, where the innovators and practitioners at the forefront of these developments share their thoughts and knowledge so we can do the best job possible as regulators.

Again, thank you for being here today, and I also want to thank all the agency staff who made today's meeting possible.

MR. HUTCHISON: Okay. And now we have some remarks from Commissioner Pham. Please play the remarks from Commissioner Pham.

COMMISSIONER PHAM: Good morning, and thank you all so much for coming today to the CFTC's staff roundtable on new and emerging issues in clearing. I want to thank Clark and all the staff of the Division of Clearing and Risk for this important roundtable with public engagement and input.

As I've said in the past, there's no doubt that we're seeing a renaissance in markets ushered in by new technology that enables direct access and continuous all-to-all trading. What and how participants can buy, sell, or trade and with who is changing rapidly. These new products and markets present new opportunities that are more accessible to more people, as well as risks. And I'm so glad that with today's roundtable, we are recognizing these trends and democratization of markets, and we are developing a robust administrative record with studies, data, expert reports, and public input from all of you here today.

Thank you so much for your time and your contributions. They will help the Commission fully understand these shifts in market structure to determine how best to ensure that our markets remain vibrant and resilient, while protecting all participants. I'm so glad that we are following on my call for these staff roundtables on innovation and market structure with today's event. Please enjoy the event.

MR. HUTCHISON: Okay. So I want to welcome you personally and thank you for coming today and traveling. To call out two people just to make it known, we have Jan Bart, who's come all the way from the Netherlands, and we have Helen Gordon, who's come all the way from London. And if there's someone else who's come from far, far away, please raise your hand. But I want to thank people for the effort to come.

Secondly, I've spoken to, I think, all of you personally, where all of you have said not only thank you for the roundtable, but expressed great eagerness for what we're going to accomplish today. And so I thank you for your eagerness to want to come and also thanking you ahead of time for participation.

I'm going to read a few administrative items so that we're all oriented, and then I have a few other introductory remarks, and we'll get started.

So from a logistical point of view, here's what we have. Wi-Fi is available on the table over there. There's Wi-Fi information posted so you can log in. Restrooms are in back of you, so if you go out the back door here, turn right, and then dogleg left, bring your driver and putter, you should find the restrooms. We have some tea and water in the back, so please feel free to help yourself. This meeting will be simultaneously webcast, and so it's important that when we speak, that your microphone is on, and you lean into the microphone. And you'll find when you look at the microphone, there's a little moniker with a person's voice. That's the button you press, and the red light will come on. But if you're not speaking, make sure that that's off, like you all have it now, so there's no red lights. So that's that.

I know that for ourselves we're all familiar with abbreviations, but for the public who's watching and isn't familiar with those abbreviations, please make sure that if you use one, to explain what that is so it's made clear for the recording. There'll be a transcript of this roundtable, which will be posted on the CFTC's website.

So a little bit more about the logistics of the day, we have eager participants. We've got 25, or 30. We can't all talk at the same time. And on purpose, Gary and I have made the time frame for each module very short. And there's something about time pressure that makes people get to the point. And I think what we're really after today is getting to the point. So when people speak, if you could keep your remarks to two or three minutes, that would be helpful so that everyone has a chance.

But as I think I've said to all of you in the introduction, at about the 35-minute mark -- and you'll see, we'll have a timer going -- we're going to try to corral the conversation down to what are recommendations that the CFTC should think about for perhaps actions going forward. So we are going to keep it time constrained.

At the same time, I think it's going to be important -- excuse me -- we're going to be doing some polling along the way. And I want to just say the gist of things is very important. I think about a compass. I want to know what north looks like. And I know sometimes to get north you have to go northeast or northwest, but at least it's the northerly direction.

So when people speak today, and we do some polling, if someone says something that basically you agree with, I call that the gist of it. And I think we're looking for the gist of things, so the more that people can agree to basically the theme of what someone has said or how the poll goes, that's helpful. We know that there's nuance. We know that there's probably some points of view that are important on the sides, but we're really looking for aspects of a northerly direction. So please, when you're voting, or if someone just says something that you really agree with, you can say, I agree with that, and it's helpful to get the gist of things.

So, with that, I'm going to introduce our moderator, Gary. And I'm sure most of you know Gary. And I have to turn to some remarks here because Gary has quite the resumé, as you know, and I've also known Gary a long time.

So Gary is a former senior counsel at Katten

Muchin Rosenman where he was the chair of the Financial Markets and Regulatory Team for much of his time there. Gary's career began at Mudge Rose Guthrie & Alexander, and in 1982, he joined the CFTC's Division of Enforcement and then left the CFTC in 1986 as a senior trial attorney. Don't know if all of you knew that Gary is an alum.

The majority of Gary's career was spent as group general counsel of Fimat, later known as Newedge, one of the world's largest clearing brokerage organizations. Gary left Newedge in 2013, establishing his own consulting firm, and there he began publishing his popular weekly blog Bridging the Week, which covered regulatory and legal developments in financial services, and then ultimately joining Katten.

So with that, I'm going to turn this over to Gary. Gary, thank you for helping today. Thank you for making the journey, and we'll leave it to you.

MR. DEWAAL: Oh, that one. Okay. Great. So much for my technical ability.

Welcome, everybody. This is going to be fun, but, as Clark has said, we're under a lot of time pressure, so this is really going to be like a Rorschach test. When we talk to you, we're going to be asking for your impressions or, as Clark has said, the gist. And again, if somebody has said something and you happen to agree with it, it's okay to say, hey, I agree with what just was said because that'll save you some time, and we can call on you later.

We really do want to try to get everybody engaged, so it literally means that it's not likely that people can speak on multiple topics. And I apologize in advance because I will be, as in the presidential debates, cutting people off after two minutes, although we won't be killing the microphones. We'll see how that all works.

All right. With that, why don't we get going with the first topic, which is digital assets. Okay. So in this section, we've been requested to explore whether depositories identified in CFTC regulation 1.20(b) are appropriate depositories without additional qualification in connection with customer funds that include digital assets. As a reminder, CFTC rule 1.20(b) entitled "location of customer funds" states that, quote, "A futures commission merchant may deposit futures customer funds subject to the risk management policies and procedures of the futures commission merchant with the following depositories: a bank or trust company, a derivatives clearing organization, or another futures commission merchant."

Section 149 sets forth further qualification for depositories, including depositories located outside the United States, while CFTC rule 39.15 discusses the handling of customer funds by derivative clearing organizations. In January 2024 the CFTC proposed amended rules that would extend to DCOs -- derivative clearing organizations -- certain requirements and practices currently relevant to customer funds to so-called proprietary funds of members.

Okay. So let's start off with the first polling question. By a show of hands, who believes that depositories identified in CFTC regulation 1.20(b) are appropriate depositories of customer funds that are digital assets? Raise your hand if you agree that it's okay.

[No response.]

MR. DEWAAL: All right. I don't see anybody raising their hand thinking it's okay. Raise your hand if you don't think it's okay.

[Show of hands.]

MR. DEWAAL: I don't see some hands raised, but I do see more noes than not.

Before opening the floor to everyone, let me ask Kaitlin Asrow, executive deputy superintendent for the New York State Department of Financial Services, to very briefly discuss requirements for trust companies handling digital assets in New York. Kaitlin?

MS. ASROW: Thank you so much, Gary, and to the Commission and Chairman for permitting us to be here.

So, as Gary said, my name is Kaitlin Asrow. I'm the executive deputy superintendent of research and innovation for the Department of Financial Services for New York State. In that capacity, I'm responsible for oversight of the BitLicense structure, as well as the limited purpose trust charter. Both of these we permit to custody and kind of engage in virtual currency business activity in New York State. So I'm going to share with you our regulatory structure and some of the background of these entities for those of you who aren't familiar.

So New York limited purpose trust charters in particular we feel have unique legal structures, as well as technical capacity with our direct oversight to custody digital assets and provide warehousing services for markets that we're discussing today.

New York banking law is over 200 years old. Trusts were formed under this law starting in the 1820s. In 1971, New York updated its law in response to the paperwork crisis, with a clear focus for these entities to provide warehousing and clearing services for the securities market. In

1981, the law was amended to expand the potential activities that limited purpose trust charters could perform.

Under this expansion in 2015, New York limited purpose trust charters were first approved to custody virtual currency and perform business activities for the digital asset space. This is almost 10 years of doing this type of activity with, again, our direct prudential oversight. This is based off Part 200, so this was a specific digital asset regulation passed under New York law that enabled kind of us to oversee the specialized kind of needs of the market. And we port this over to limited purpose trust charters, again, under the banking law. Currently, we have 12 trusts who perform these services.

I think something that's unique about New York State is, again, kind of the history of this law and the specialty in the services that they provide, but our digital asset expertise. So our supervisors and our trust have experience in cold and hot wallet storage, are working through new storage techniques, multiparty computation sharding, again, with our specialty kind of oversight.

We have supervision kind of expertise in BSA/AML that's specific to the digital asset space, transaction monitoring, KYC sanctions. Part 500 in New York has a special cybersecurity focus, which is especially important in this market. And we've issued clear guidance from the Department on the treatment of customer assets in the event of insolvency so, again, strengthening the custody regime.

So some aspects of the banking law and trust charters, again, to note here, limited purpose trusts are granted fiduciary power under the New York banking law, enabling them to offer bank-like services. This has given them the opportunity to meet qualified custodian standards under the securities law. Again, they operate under our banking law. They're empowered to deliver custody services in a fiduciary capacity and, like our chartered commercial banks, are subject to full examination and supervision by the Department.

They are supervised and examined like banks, so we're expecting them to comply with all federal and state anti-money-laundering laws, twice annual call reports, carrying capital satisfactory to DFS, and we do have specific capital requirements that are customized to digital asset oversight. Again, they must comply with robust cybersecurity requirements and meet fidelity insurance and examination expectations.

Now, I want to note the guidance that we released in January 2023, so almost two years ago, with our expectations around custodial structures that I think are relevant to this conversation. So, first, we expect our entities to segregate and account for customer virtual currency separately, so they must maintain and segregate customers' virtual currency from corporate assets at all times and its affiliated entities both on chain and in their internal ledgers.

They must indicate limited interest in and use of customer virtual currency. So when a customer transfers possession of an asset to a custodian for the purposes of safekeeping, the custodian will take possession only for the limited purpose of carrying out custody and safekeeping and will not thereby establish a debit or creditor relationship.

And finally, again, relevant to this, they must clearly disclose these aspects of their custodial structure to their customers in their terms and conditions, again, the segregation and accounting, and kind of the intent to enter into a custodial relationship, not debit or creditor.

So I'll also finally note that we also permit our full commercial banks to perform virtual currency business activity with the approval of the superintendent, and my division supports the banking division in that oversight.

Thank you, Gary.

MR. DEWAAL: Okay. Thank you, Kaitlin.

Terrence, if I may call you as a trust company, do you think there should be qualifications around the type of trust companies that are permitted to hold digital assets under

CFTC rule?

MR. DEMPSEY: I believe that market participants should have their right to choice of an entity that they want to do business with, subject to certainly certain key elements that are there that, you know, we should be ensuring are there to ensure, again, orderly markets, right? So as we think about many of the things that were just raised, you think about capital, you think about insurance, you think about cybersecurity, oversight, and things of that nature that you're going to want there, and certain standards, of course, that are there so that there are fair and orderly markets and settlements and things of that nature can happen.

You know, 12 in New York is still a relatively small number, right? So how do we think about what that set is and still allowing investors choice? And, you know, how do we plug in and settle transactions are all things that come to mind.

MR. DEWAAL: Now, Zach Dexter, you made a mistake before by reminding me of our old relationship.

Given the fact that you guys were the first clearinghouse that handled physical Bitcoin, do you think there should be qualifications around DCOs that handle physical Bitcoin or any other crypto?

MR. DEXTER: Yeah, of course. So we built a hardware security module-based custody system back in around 2017 and direct clearing member digital assets for around three years directly and then around four years through a trust company. The issue with digital assets is that the finality is very extreme. It's very final. It's not like a fed wire where you can potentially unwind the transaction pursuant to a court order if you really need to. It's not like ACH where there's not enough finality. It's at the other end of the finality spectrum.

So in the case of digital assets specifically, there really is a good use case for a purpose-specific custodian that is solely focused on cybersecurity and backups. I think that's really the ideal here. And we actually moved from direct custody at our DCO to a trust company. If I were doing that again today, I would probably choose something like the New York framework or one of the more well-defined frameworks. This is a case where a purpose-specific custodian makes a lot of sense, I think.

MR. DEWAAL: Matt, if I may bother you, Mr. Lisle, any concerns about just FCMs being allowed to custody digital assets?

MR. LISLE: Plenty. You know, the biggest one that stands out -- well, there's two. The first one would be, as an FCM, your responsibility with respect to your regulators, and what do they, A, understand about custody of digital assets, and B, whether or not they're comfortable with it. And then the second thing, which I think is a huge issue that perhaps this isn't the forum for, is how do you characterize those assets from the standpoint of legal regulation? Are we talking about Bitcoin? Are we talking about USDC? Are we talking about something else that perhaps is something that Mr. Gensler is concerned about?

So I guess my main point here is the uncertainties. But, at the same time Wedbush, we struggle with this internally because, you know, you're trying to serve your customers and align with your customer base. So there are competing concerns within the FCM that, you know, we end up having to balance in a way that, you know, is never entirely comfortable. So I'll leave it at that.

MR. DEWAAL: Helen Gordon, may I turn to you or for your views on the subject?

MS. GORDON: Sure. Thank you. So I wouldn't pretend to be an expert on 1.20(b), but I guess the logical extension is that if there is custody and collection of digital assets within an FCM, that it is being used as margin. And so I would point back to what are the fundamental characteristics that margin should possess. It should be liquid. It should perform well during periods of volatility. And from a DCO perspective, there should also be limits on the amount of that specific collateral that any one FCM can have.

So I think it's important to look at the use of digital assets in that broader context and also extend the kind of analysis on the topic to contemplate the use of traditional assets in tokenized form rather than exclusively focusing on digital assets because that has broader applicability, and there's already a much more established legal framework and risk framework supporting those assets.

MR. DEWAAL: Matt, may I call on you? I'm curious for your thoughts on the subject.

MR. HARABURDA: No, I didn't have anything specific to add or, you know --

MR. DEWAAL: Okay. Sorry. Does anybody else have some comments on this topic? Is the 1.20(b) requirement too broad or should they be more restrictive as to which entities can hold digital assets and what kind of qualifications should apply? Any thoughts? Yes, Joe.

MR. GUINAN: I got a different perspective, which is not exactly on topic, and I apologize, but I think if the CFTC is going to be looking at digital assets, there's a much broader question that should be investigated, and that is, what is the overall public good of having digital assets, cryptocurrencies, given the fact that, you know, ransomware attacks costs us over a billion dollars a year, given the fact that the cost of preventing ransomware attacks cost companies multiple billions per year. And given the fact that digital assets are involved in everything from sex trafficking, tax avoidance, money laundering, and so on, instead of just viewing it, the horse is out of the barn and we have them, I think we should take a step back and say, are they a societal good or not?

MR. DEWAAL: Okay. My sense is that's probably beyond the scope of this session. But, Joe, I would expect nothing else from you other than a controversial topic that we should come back to at another time.

Anybody else have some thoughts?

MR. HUTCHISON: Gary, I'd be curious to hear from Jan Bart and what ABN thinks about this.

MR. DEWAAL: Okay. Jan?

MR. DE BOER: Thanks. If you look at other, say, derivatives products emissions, we were able to figure out how we could use emission certificates, which were held in some sort of register as collateral. We note in the commodity space that we can take warehouses all over the world if they are, say, guaranteed, or they are insured or they are on an approved list. So I would expect this industry to go towards a model where you can safekeep and therefore also margin digital assets, especially against futures.

MR. DEWAAL: Is there a consensus of this group that the entities named in 1.20(b) in and of themselves should not be authorized to hold digital assets, but should rely on entities that are more familiar or more regulated to hold the digital assets on their behalf like New York State trust companies? Terrence?

MR. DEMPSEY: I'd argue that a New York State trust company is named in that, right? It is a trust company, which was the first piece that you had said, right? I do think it is just restrictive, right? We talked about the BitLicense regime of New York State. Now, that is not a bank or a trust company, but could an FCM get BitLicensed and that, you know, be appropriate licensing for them to custody. I think that is a question, right? I think it is just a little narrow or restrictive as currently written.

MR. DEWAAL: So your suggestion is that FCMs, if they want to hold digital assets, should themselves get a BitLicense or equivalent?

MR. DEMPSEY: Well, no, you had them listed, right? But they could, right? I think if they were an FCM in New York, they probably would be required to get a BitLicense, just the way that might be written. But I think if there were an entity that wanted to be able to custody digital assets, right, there's more than just the trust company that meets that definition.

MR. DEWAAL: Okay. Anybody else? Dave.

MR. OLSEN: Thanks, Gary. I think entity type is probably the wrong starting point for the definition of who should be allowed to hold digital assets. I think it's the capabilities of the entity and whether it's through acquiring a BitLicense or another regulatory directive that ensures that they can be handled appropriately is probably the best path.

I also think that each of us is probably coming at this discussion from a slightly different definition of what digital assets we're talking about. I think the market at least appears to me to be evolving very quickly into having any underlying risk be able to be tokenized and moved and stored on-chain. So I think all of the existing collateral types that are acceptable by DCOs could meet the definition of a digital asset either now or in the very near future. So I would urge rulemaking that clarifies at least what the CFTC's stance is and where those borders are around each of those assets.

MR. DEWAAL: So maybe you can expand on your thinking there just a bit further. Are you suggesting that most types of collateral today are a type of digital asset?

MR. OLSEN: I'm saying that Treasuries, let's say, for example, we're already seeing groups tokenize Treasury risk and have a tokenized representation of a Treasury asset that is held backing that asset, a little bit like a stablecoin, but instead of using U.S. dollars as the backing instrument, you could use corporate bonds, you could use gold, you could use Treasuries. And so the form of transmission of the asset and how it's stored and whether it's on-chain and what cybersecurity risks exist around that, I think, need to be the focus of good policymaking rather than, for example, just thinking about, should Bitcoin travel on these rails? I think it's much more expansive than that.

MR. DEWAAL: And who should determine those standards and requirements? Is it the CFTC? Is it the exchanges on which the products trade? Is it the traders themselves that are trading the product? Who should make those standards?

MR. OLSEN: I think the DCOs have the responsibility, first and foremost, to determine what is appropriate collateral to hold to safeguard the institution in a crisis. Those parameters already have a very wide range of risk associated with them and commensurate haircuts. For example, you can post barely investment-grade 30-year corporate bonds at about a 30 percent haircut at the CME today. Those have got liquidity characteristics that are very different than Treasury bills. So I think that each of those could be tokenized. And you could imagine a responsible DCO thinking about the right concentration limits and tests to hold cryptocurrencies as well as part of that range, as long as they're haircut appropriately and limited.

MR. DEWAAL: Matt?

MR. LISLE: I think we're going around -- one of the bigger issues here is the technology that's underlying these protocols. And to get at the answer of whether or not there's reliability here -- and I think that that's the most important thing when you're talking about custody and when you're talking about collateral. I think that people in the digital industry will argue that the technology is actually safer than traditional financial technologies that we're aware of.

We haven't gotten there yet. I don't think the regulators are there yet. And when you're asking a question as to who is best positioned to make those determinations, I would point to New York. It sounds like they've got things going on. I'm not sure that my DSRO coming in is at this point equipped in order to answer those questions. There's a lot of technology here. Is it a closed chain? Is it an open chain? You know, look at Luna. You know, that algorithmic protocol where, you know, who understood it, you know?

So at the end of the day, there's a lot of mousetraps out there, and we are going to need a referee. And that referee is going to have to be qualified in order to make those determinations. And at the end of the day, perhaps we do leave it up to the market in the competitive marketplace. So --

MR. DEWAAL: Zach, if I may turn to you again and borrow from our conversation earlier, why are you out of the business of handling physical crypto?

MR. DEXTER: Well, this is just my personal perspective. I'm not speaking for Miami here. But I sort of thought that the developers of some of these protocols would think to add in some mechanism to address the finality of digital assets, and I think people who are looking at tokenization and traditional assets are considering that. But it didn't really happen with a lot of the Layer 1 coins. So you have all these issues like, how do we store this properly? And that implicates the need for --

MR. DEWAAL: I'm sorry. I'm just going to interrupt you. I know what Layer 1 is. I'm not sure most of the audience knows what Layer 1 is.

MR. DEXTER: Bitcoin, Ethereum, the big tokens you see in the news. Once you start thinking about, oh, this is final, and the laws of physics would prevent me from getting this money back if I send it to the wrong place or if I'm hacked, you have to start thinking about how to custody that correctly, and that gets into hardware security module supply chains and software updates that are very vulnerable to -- they're sort of soft targets for foreign actors.

So there are a lot more considerations once you start taking digital assets for custody if you're not doing that as your only job, and there's just a lot of risk. And, meanwhile, we've got incredible new payment networks coming online like FedNow, which could obviate ACH entirely and allow for an instant posting of USR collateral around the clock. So I think the digital asset protocol developers have got to think about, what do we do about finality?

MR. DEWAAL: Demetri, I see you nodding your head. I don't know if that means that you have agreement with Zach or you have your own thoughts.

MR. KAROUSOS: I'd love to reserve my time for some of the other topics. Thank you, Gary.

MR. DEWAAL: No problem. As I said, I just saw you nodding happily.

Anybody else?

MR. HUTCHISON: So, Gary, why don't we turn to a little bit about what David was saying. On the one hand, we have principle-based regulations about segregation. We have examinations on cyber system safeguards, BCP. We've got those in our regs, and many DCOs have also all those things in their regs. And is it okay just to leave it principle-based and let it sort itself out?

Because, on the other hand, people have said to us, you know, a trust company is not a trust company. And if we say for a moment that maybe New York State has the best mousetrap, but there are other mousetraps out there that might not be as robust but might have the name trust company, do we just let that meet the definition of bank, trust company, et cetera, for digital assets, and let caveat emptor rule to say there's principles, people do the best they can, and it is what it is, and people are responsible for their own due diligence. You know, can we at the CFTC say, you know, that meets the mark? What would your recommendation be? David, I see you having a response.

MR. OLSEN: Thanks, Clark. I think in this arena there has been an undershoot generally in predefining the rules for the industry to be able to configure itself around. And so I think, in general, I believe that a principles-based approach is correct, and you let competition organize itself around that. I think, in this case, being a bit more explicit where the Commission really sees the right lines being drawn and articulating them ahead of time for the industry, rather than allowing ambiguity about, you know, try it, wait and see if you did it right, and then find out after the fact would be the preferred course of travel here. So I would be a bit more prescriptive on where you see the boundaries.

MR. HUTCHISON: Okay. Great, Gary, I'm going to jump in. I want to ask Graham -- oh, wait, is there -- oh, Ann, I'm sorry, excuse me.

MS. BATTLE: Sure, just very quickly, I think, you know, ISDA hasn't taken a position on these issues, but we have done work that I think is in line with what some of the speakers have said about not necessarily looking at the entities or the entities by name or classification, but what the protections are, and just ensuring that the protections are what customers receive for traditional financial assets.

I think most people in this room are aware in May of 2023 we published a paper that essentially concluded that those protections could be made available. You know, it would be possible to hold these assets in a similar way, but there are a number of operational and other issues that participants have mentioned that just have to be sorted out. And so without going into those details, I think we would just want to say I think that's the way to come at it, you know, looking -- and I think you can do that in a principles-based approach. And perhaps others have views on that.

MS. WOODING: You know, I think NFA agrees with that. We're not opposed necessarily to digital assets being margined, but you still have to make sure. I mean, they're the most important thing. You have to make sure they're there to meet the needs of the customers, and that if you're holding digital assets as margin, and you're holding traditional assets as margin, those customers that have the traditional assets aren't impacted negatively if something happens to the digital assets. So, like she said, we need to make sure, not so much looking at what kind of entity is holding them, but that they do meet certain specific qualifications so that those assets remain safe. So I think it needs to be a little bit more prescriptive than just let the market work it out and it will happen organically.

MR. DEWAAL: And who determines what those specific requirements are?

MS. WOODING: And that's the hard part, right? I think you need expertise across a lot of different industries. The Commission clearly has to be involved, but I think they also have to involve -- you know, talk to New York State. What did they do? Talk to cyber experts. Talk to the people that are custodying assets. I think it can't be just done in a vacuum by the Commission alone. They have to really reach out to other experts.

MR. DEWAAL: Graham, did you have something to add?

MR. HARPER: No.

MR. DEWAAL: Still nothing to add. Okay.

Anybody else? I'm sorry, Clark, you wanted to follow up on something.

MR. HUTCHISON: Well, I was going to ask Graham, but, Graham, I don't want to put you too much on the spot, but maybe taking a little bit away from just the custody, you and others like you trade digital assets all day long in volume and arbitrage and so on. So I'm just curious, how do you make yourself comfortable with what you're doing such that, at the end of the day, you feel like you've made successful trades, but also whatever you might hold in custody, you feel okay about that?

MR. HARPER: I mean, we do our own due diligence with every exchange we trade on, so it's a case-by-case basis.

MR. HUTCHISON: And --

MR. DEWAAL: Is it by exchange or is it by crypto?

MR. HARPER: Both.

MR. HUTCHISON: All right. Well, Gary, why don't we use this moment to corral everyone and see if we can't come up with recommendations for us to consider.

MR. DEWAAL: What I think I've been hearing is that, in fact, the naming of the entities is not as relevant as the naming of the qualifications of the entities regarding their ability to hold digital assets. That's far more important.

MR. HUTCHISON: Right. So let's just do a show of hands. The gist of what Gary just said, how many people agree with that? Most people agree with that?

[Show of hands.]

MR. HUTCHISON: Okay. There were perhaps hands that weren't raised, and that might be because you don't want to, but does anybody disagree with that?

[No response.]

MR. HUTCHISON: Okay. So that's helpful.

MR. DEWAAL: Joe probably disagrees, but he's not going to put himself at risk again.

MR. HUTCHISON: Okay. So we've got naming and qualifications. So I guess the next question would be, do you think it should be the CFTC that determines those qualifications and gets a bit specific, rather than just staying principle-based? People agree with that statement?

[Show of hands.]

MR. HUTCHISON: Sean, you were going to say something?

MR. SEAN DOWNEY: Yeah, thank you. I was just going to note that there are some entities that are named today, 1.20, and then 1.49 talks about money center countries. I would say both of those are somewhat prescriptive and arguably historical, particularly if you look at the money center countries. So, ultimately, I don't think that the CFTC should necessarily provide prescriptive detail on the qualifications. Like that's something that we do ourselves. If we look at one of these entities, it could be named, but it could still, I think -- as Graham was pointing out, it wouldn't necessarily mean that we think that they would be appropriate to hold this type of collateral.

And so I think from our perspective, one thing to consider as we're talking about these two regulations from the perspective of digital assets, but more generally, they are somewhat prescriptive in some ways, and they haven't been reevaluated in quite some time. So I don't know if it's specifically just a digital assets conversation or if it's a broader conversation on permitted depositories, money center countries, locations, things like that. I think that's probably something that should be considered more widely beyond just this concept of who qualifies as a digital assets custodian or trust or whatever it may be.

MR. DEWAAL: So you're suggesting specifically a potential amendment to 1.49 that would, at a high level at least, set up some kind of qualifications?

MR. SEAN DOWNEY: I think I'm more just suggesting that those regulations are -- I don't want to call them old, but like well-established enough that they should be reconsidered.

MR. DEWAAL: So am I more well-established than old? I'm just trying to understand the new phraseology.

[Laughter.]

MR. SEAN DOWNEY: I mean, I think you're well-established and well-respected, and so are the regulations which we would certainly comply with.

MR. HUTCHISON: Okay. I'd be curious if someone could comment that, if confronted with a statement, I'm sorry, a trust company is not a trust company, your rules talk about trust companies, but they don't talk about other entities than we'll call it banks or trust companies, and yet, we're hearing, I think, a consensus that DCOs should have the ability to do their own due diligence and perhaps figure out how they want to handle things. And a DCO is a place to put things.

But if you don't want to put digital assets at a DCO per se and you want to hold assets in custody for your customers before they go to a DCO, what's acceptable? And we don't have a word for that.

And so it sounds to me like we're at the precipice of either having to stay silent and have this remain a conversation that's not coming to a conclusion or having a recommendation that we might change a definition to be more flexible. And I'm just looking for the wisdom of the group to say, what do we think we ought to do? So do you think we ought to modify and expand what the depositories are by name or by characteristic or a set of characteristics? Or should we let DCOs be the place that that gets decided and leave it up to DCOs as the depository of choice when people decide to use digital assets in our marketplace?

MR. THUM: Hey, Clark, it's Bill Thum here --

MR. HUTCHISON: Oh, there you are.

MR. THUM: -- from SIFMA AMG.

MR. HUTCHISON: I can't see you.

MR. THUM: Hi.

MR. HUTCHISON: There you are.

MR. THUM: You know, listening to the conversation, I'm wondering if, you know, we're a little off track in terms of identifying the types of entities, and the better track would be for these specific types of assets, clarifying what aspect would demonstrate safekeeping, what aspect would demonstrate exclusive possession or control. So with the existing principles-based rule set that has requirements for all these types of entities when they hold assets generally, do they need to be refined to some extent with respect to digital assets? And then compliance can be determined with respect to any of the entities based on how they hold the assets, not based on their qualifications.

So I'm just wondering if, rather than designating entity types, some clarification, if it's needed, would apply to what is the objective of the Commission with respect to safekeeping possession and control, demonstrating those sorts of things? That may be a different way to think about it.

MR. HUTCHISON: That's helpful, Bill. Thank you.

MR. DEWAAL: Allison, were you going to add something?

MS. LURTON: If I could get the mic on.

MR. DEWAAL: I think it's the second button over. Um-hum.

MS. LURTON: Thank you. I think, picking up on what Bill said and also what Sean said, they're not mutually exclusive that we would have principles-based regulation, and also some regulations that have very specific requirements like the definition of money center countries. And so, similar to what Bill Thum just said, I think if the Commission were to identify specific needs that could be coupled with identified entity types such that you can satisfy the protections you're looking for. I think we do that all over the regs now, so I see no reason why you couldn't do that. I think that would be important because we wouldn't be abandoning principles-based regulation. That would remain so you could keep items like the DCO individually assessing its own needs. But if there is something specific that you see in the New York structure that you think could be borrowed, an important component could be added as a specific element.

MR. DEWAAL: Kaitlin, after hearing all this, just curious whether any response as to what you think our industry can do better, thinking about what you guys are doing today.

MS. ASROW: I won't comment on the industry. It's not mine to comment on. But I will say we have spent significant time building expertise. So I think, you know, we have a team currently of over 60 individuals who are deeply kind of entrenched in digital assets in terms of how we oversee compliance. So I think that's something that we are able and willing and are sharing in all spaces. So I think it's an opportunity again for us to use this. And I will note, you know, we're working consistently with federal and international regulators who are taking kind of our technical assistance for this.

MR. DEWAAL: Okay.

MR. SLOCUM: Super quick --

MR. DEWAAL: Allison --

MR. SLOCUM: -- I think I would love to learn more about the New York experiment because I think you talked about that it's -- we're two years in with this new reg, and how much of it is, you know, reliant upon sort of self-reporting and how much of it is, you know, direct auditing oversight with this team that you've built just to get a better understanding about how that's working.

And back to Joe's point, you know, he framed it as being off topic, but I don't think it's off topic to go to the 30,000-foot level and ask, you know, whether or not this sort of theoretical purpose of digital assets is consistent with how it's being utilized in the economy today and whether or not it is a legitimate exercise.

And it's not happening in a vacuum, right? We're seeing unprecedented financial participation by the digital asset corporate community into our electoral system, which is largely responsible for why we're having these discussions because the crypto industry is sort of financing the political backing for some of this. And I do think it's important to recognize that crypto increasingly does appear to have, you know, a lot of illicit purposes. There's an awful lot of high-volume enforcement cases by the CFTC and other agencies.

And so I do think it's important as we talk about adherence to the Commodity Exchange Act that we do ask questions about what the general purpose of some of these commodities and assets are in the economy.

MR. DEWAAL: Yeah, I'm not arguing that it's not an important conversation, probably just not an important conversation -- we don't have time enough to have that conversation here today. But I'm sure Kaitlin can give some more insight as to what she's doing over at the New York State Department of Financial Services.

MS. ASROW: Yeah, absolutely. So one thing, we're 10 years in, and I think we're kind of beyond the experimental stage at this point and fully into having our feet under us, which I think you've seen over the growth of even the last kind of three years. We put out nine pieces of guidance, being prescriptive, but again, leaving the principle-based underlying regulation there, so kind of details in a more flexible way.

For our limited purpose trust, we have annual examinations, so these are full scope in the entity, looking at everything from capital, to cyber, to internal controls, to management, to BSA/AML and issuing ratings and reports of exam.

And then I think something that's unique about New York and something that's different from my past experience in kind of traditional prudential regulation is we do constant offsite monitoring in between those examinations. So we are on weekly calls, monthly calls, daily calls depending on the situation with our entities, understanding kind of where they are with what they're offering, their customers, their partners. So I think we have learned a really high-touch oversight regime is necessary here, and we've built the team to do that.

MR. SLOCUM: Thank you.

MR. DEWAAL: Clark, I think we have some consensus?

MR. HUTCHISON: Yeah, I think we have some consensus. So, first of all, thank you. I know that this is a hard topic because it's not well-baked, and we're trying to figure out, to use the phrase, how to bake the cake right. We don't want to overcook it, we don't want to undercook it, and there's still questions that we have to resolve. So I appreciate everybody struggling a little bit with us as we try to gain a consensus on what to do, so that's great.

Well, I'm going to have to figure out how to change the timer to the next module, but the next one is going to be on 24/7 and I think that's probably a topic that's a little less unknown and has challenges, and so we're eager to hear what people think about the advent of 24/7 trading. And I'll just introduce it a little bit. We kind of have it today. Markets do trade on a five-day week in the day and into night. We also have time zone differences, so when we're all asleep here in the U.S., other markets are going. We do have, because of that geography, some trading that ends up coming on Sunday night. So we're kind of there. We're kind of not. We, in my view, have backed into where we are just by the way the markets have developed and the way margins have flowed. But 24/7 brings another set of challenges, particularly when banks are closed.

So Gary and I would like to explore that topic with you and, again, looking for items that we should be thinking about to perhaps make the idea of 24/7 palatable and safe. So with that introduction, Gary, I'll leave it to you.

MR. DEWAAL: Can we reset the timer?

[Discussion surrounding timer.]

MR. DEWAAL: All right. While we're dealing with the technical issues, by a show of hands, who believes that noninterrupted 24/7 derivatives trading should be permitted?

[Show of hands.]

MR. DEWAAL: There's definitely some people not raising hands. Who believes it should not be permitted?

[Show of hands.]

MR. DEWAAL: Okay. So we have some diversion here. For those who voted yes -- I think most of the people voted yes -- who believes 24/7 trading should be permitted but only subject to guardrails? For example, requirements of pre-margin, restrictions related to qualifications of traders, restrictions related to structural clearing organization, i.e., intermediated versus disintermediated? Raise your hand if you believe there should be guardrails?

[No response.]

MR. DEWAAL: Interesting. Okay. Mr. Downey, you raised your hand in a very energetic way. What are your thoughts?

MR. DAVID DOWNEY: I did not raise my hand.

MR. DEWAAL: Oh.

[Laughter.]

MR. DAVID DOWNEY: I saw you moving in your seat in a very energetic way. Twenty-four/seven trading should be allowed or not allowed?

MR. DAVID DOWNEY: Organizations have reporting requirements that need time to process. Twenty-four hours is a concept, but if you want to do 23 hours and 15 or 45 minutes, I think I'm on board with that. But we need time to process and handle all the information at least once per day because that's how time is measured by regulators.

MR. DEWAAL: Okay. Contrary view?

MR. SEAN DOWNEY: Not contrary --

MR. DEWAAL: Sean?

MR. SEAN DOWNEY: -- but I would just note that the first question is market demand and interest. I think that might be asset-class-based. To the extent that there's benefit from hedging risk on a 24-hour basis in certain asset classes that may be valuable, but at the same time, people have to take into account the risk management consideration.

So you said guardrails. I wouldn't necessarily put it that way. I would put it more risk management best practices. How do you take the risk management that you do when the banks are open, when you have movement of value, and apply it on a 24/7 basis? So how do you margin positions that are open? How do you deal with positions that are taken during a longer time frame when the banks aren't open? So I think there are still some open questions.

But from our perspective, if there's market demand, it does benefit risk management for market participants, then you have to ask the next question of, how do you manage the risk from a clearinghouse and exchange perspective? And there are some different ways to consider that, but it's certainly a conversation that needs to be had in order to expand the operating hours.

MR. DEWAAL: Does it make a difference to whether the clearinghouse is intermediated versus disintermediated?

MR. SEAN DOWNEY: I mean as a general matter, we view FCMs and DCOs working very closely together to manage risk within the ecosystem. And I think we would expect that, to the extent that you did expand the hours, it's going to require additional work both from DCOs and FCMs. So I think our view is that that market structure and that approach to risk management is a best practice, and it's demonstrated that it performs well over a variety of different market conditions. So that's most likely the best path forward.

But, ultimately, it really just is a question of, how do you replicate the risk management that exists today in today's markets with that structure, which we view as very valuable, in a future world where you have expanded trading hours? And I don't think that's an easy answer right now with the fact that you don't have movement of value, you don't have financial institutions necessarily open, but it's one that I think we need to explore and figure out a way to kind of replicate those risk management practices to the extent that there is market demand for those expanded trading hours, which, as I noted, I think will be somewhat asset-class-specific.

MR. DEWAAL: I'm going to go to Demetri first as long as I'm looking this way first, and I can see he's eager to speak.

MR. KAROUSOS: Thanks, Gary. So I'll borrow some of the minutes from before -- no, I'm just --

[Laughter.]

MR. KAROUSOS: No, so we are supportive of 24/7 trading and clearing, but the key is how you risk manage it. And for us, we think there are some core principles that you need to have in place. One of them is a very robust pre-trade risk regime in place. That means not at trade and not post-trade, pre-trade. That means before an order hits the order book. And that's critical. It also means the ability to track existing orders that have not yet hit but are still live, right? Because that remains potential exposure for that participant.

The check needs to be a full portfolio check, not just the electronic trading that day, not just that day's activity, but a full portfolio check, i.e., preexisting positions are fully incorporated into that check. And all of that then requires real-time position monitoring, right? This is super critical. So without real-time monitoring, you don't really know when a position gets traded. Is that opening a new position? Is that adding to your exposure, or is that reducing your exposure? That's critical to proper risk management during the weekend when you don't have frequent cash flows from a normal margin cycle.

And then, finally, an added bit which would be new from a DCO perspective is that, in thinking about that pre-trade risk control and the trading capacity available to each of the participants and clearing members, it's important to also incorporate, we believe, what's called current exposure or variation margin of mark-to-market treatment. So this is to say that, as your positions are losing, you have less capacity to continue to trade, right? And this is to ensure that during an extended trading period that you're not just always trying to double down and potentially increase your exposure by, you know, making it up on volume, right? So that's an important consideration. So allowing current exposure or mark-to-market exposure to reduce your trading capacity is another key feature for managing risk explicitly during a longer period like a weekend --

MR. DEWAAL: What do you do with David's comment that you need some time to reset every day?

MR. KAROUSOS: So we think of that -- so I don't run a clearing member, so I don't want to get into that very specifically, but I think we think of that more in the context of having appropriate snapshots. And as long as you are capturing snapshots of trades, positions, everything all at one moment in time, you can do your reporting obligations and allow the market to continue.

So, for example, we have a midday margin cycle, which is, in all aspects, identical to our end-of-day margin cycle. So VM collected and paid out, IM collected and released if there's excess. We don't stop trading in the middle of the day just to run that midday margin cycle. We continue trading, right? But the way we run that cycle is we take snapshots at midday in order to have a cohesive set of considerations to run a proper margin cycle. Does that make sense?

MR. DEWAAL: Yeah. Allison?

MS. LURTON: Thank you. I just wanted to comment that a lot of the discussion thus far has been about the infrastructure facilitating the actual transactions in the markets, but there's an entire infrastructure behind that that supports it. And while FIA supports the operational efficiencies that folks are trying to capture from 24/7 trading, we can't disconnect that from the lack of 24/7 collateral movement and settlement.

And so I agree with what Sean said about risk management. That is also a component of what the FCMs are doing, and the DCOs. That comes from the fact that there's a disconnect now between when you can trade and when you can settle. And so it's difficult to fully support 24/7 trading environments when we all fully know that collateral cannot move at that speed. Specifically, it's either the DCOs or the FCMs, then, that are going to bear that risk of the gap. And so from the perspective of FIA, to really inform this discussion we need to acknowledge that the settlement and collateral movement is not currently 24/7.

MR. DEWAAL: J.B., if I may ask you your thoughts on this as an FCM?

MR. MACKENZIE: So, first of all, I think the client demand for 24-hour/seven-day-a-week trading is already there. There's no question. So it's in the marketplace. You see it in digital assets. You see it internationally. The fact of the matter is, when the world's moving, you know, news doesn't stop because of the fact -- or world events because of the fact that we're closed in our marketplaces.

I do think that there is questions and concerns over the infrastructure getting to the point to being able to support 24-hour trading, seven days a week. But I think if we take it from the perspective of how do we get there, it's something we're going to have to do. The market is going to demand it. And if not, what you're going to see happen is what I would say is different markets are going to evolve that are unregulated that are going to push people into them. We see it already internationally, whether you look at CFD markets, principle-based products that are out there globally, that's where investors are going to.

So I do think that we have to move there. There are risks that we have to pay attention to. I will tell you, as an FCM, we run a 24-hour-a-day, seven-day-a-week risk management program, real-time risk analysis looking at what's going to happen so that when markets open, we can take action as necessary. It's also important for individuals from a retail standpoint to control their own destiny as well, and they have to risk manage their own products just like we would do anything else in our lives.

So I think the market's going to have to evolve there. I think, to Allison's point, it can't get there overnight. It has to be in baby steps. But if we don't start moving toward it, other markets are going to get there because we're already seeing it happen globally.

MR. DEWAAL: Are you not concerned that you can't move collateral 24/7?

MR. MACKENZIE: I think you can move collateral in some cases 24/7. We do this already today with some of our banks and how we move collateral to support our digital asset trading. I also have seen it firsthand internationally in markets such as Singapore where there are banks that allow the movement of funds to and from. I think the question is what type of collateral should be allowed to be utilized over the weekend and how do we evolve to that? So going back to the question earlier about should digital assets necessarily be allowed, a product that can actually move 24 hours a day, seven days a week? So there are capabilities for us to make this happen.

MR. DEWAAL: Are you suggesting stablecoins?

MR. MACKENZIE: I'm not suggesting anything.

MR. DEWAAL: Um-hum.

MR. MACKENZIE: I just think we have to take the time to look at it. But I do think the world moves so fast, we can move assets ourselves, 24 hours a day, seven days a week. It's odd to me that we could just say that institutions and banks aren't able to do it because I don't think that's an accurate statement. I just think that we're not quite there yet in regard to the comfort level we need to be at to be successful.

MR. DEWAAL: Okay. Fair enough. Dave?

MR. OLSEN: I fully agree that we know the end game here. Markets will be trading 24/7 in the not-too-distant future. We're trading 24/7 today. A lot of Middle Eastern markets are open on the weekend. India has got Sunday sessions that spring up from time to time. There was a major fiscal policy announcement in China last weekend that happened to occur in the middle of the day our day on Saturday. So the risks don't go away on Saturday and Sunday, and those that are participating in the market are interacting with those today, just in other markets, international, less regulated, et cetera.

The focus on risk, like how could we possibly trade if you can't move collateral because you have to manage risk? Well, when the markets close on Friday evening, people go home with enormously substantial risks that are changing in value on Saturday and Sunday, and we seem to sleep calmly because you can't see it on the screen.

MR. DEWAAL: Right.

MR. OLSEN: Just because you know how much the position is moving now, you can trade out of it. And J.P. Morgan Coin is moving hundreds of millions of dollars 24/7. Partior is doing it interbank in the Singapore model. If the two of us have got the same settlement bank, we can move on their subledger 24/7. These are practices that are live today.

So what I would suggest is that, under the purview of the CFTC, we pick a pilot market where it's not a big bang where everybody has to be ready and the entire global infrastructure needs to be set, but you allow trading of one contract complex as a test case. The participants have breakout meetings. We talk about the design of collateral movement, whether or not there has to be prefunding. I think that can be a good idea for adding risk, but start moving forward in the U.S. to catch up with a lot of where the global marketplace is.

MR. DEWAAL: Yeah. Helen, Dave just referenced the J.P. Morgan Coin. I'm not sure everybody knows what that is. Can you describe it?

MS. GORDON: It's basically a dollar-for-dollar backed coin, which is offered by our Treasury Services Division, which enables the movement of funds outside of traditional hours. And this is definitely one of the use cases that works well in that construct because it doesn't have some of the same I guess liquidity or financial risk that you might get with a crypto-type asset.

I completely agree with what participants have said here about the move and increase of 24/7 trading is inevitable, but I do think that it's important that it is backed with the movement of collateral. I know there's been reference to prefunding. However, I think that it's imperative that you can actually move and have the ability to initial intraday margin calls or, yeah, to manage your risk over that period. Definitely parallels to the previous conversation around how do you extend the breadth of assets and the payment rails, whether that's tokenized collateral, J.P. Morgan Coin.

And I guess in some markets, if people feel that digital assets are appropriate for use with margin, I don't think it's a sensible model where that becomes the only backstop for moving collateral over the weekend, given the limits that should be on any specific collateral. And I think it's really important that there is demand and liquidity because what we have seen in certain markets is very high price movements or very large price movements when there is thin liquidity, and therefore, there has to be the demand to sustain the 24/7 trading. And even where established exchanges have very extended trading hours, they don't do it for all contracts. They obviously have a risk management protocol where they assess where there is going to be liquidity and order book depth in order to sustain that activity.

MR. DEWAAL: Um-hum. Kevin?

MR. MCCLEAR: Hey, Gary.

MR. DEWAAL: Hello, sir.

MR. MCCLEAR: It's been a little while. I'm having a flashback to your soups to nuts.

MR. DEWAAL: I'm not throwing out --

MR. MCCLEAR: Thirty years ago, you were the time filler.

MR. DEWAAL: -- toys today. No stuffed animals for you.

MR. MCCLEAR: I bit my tongue during the last panel. I didn't mention Sentinel but you and I are old enough to remember Sentinel.

MR. DEWAAL: Sadly.

MR. MCCLEAR: So for 24/7 trading, when I hear that like ready here, I immediately jump to clearing, 24/7 clearing. I'm a clearing guy. And

I agree with everything the other DCO said about risk management. I agree, Dave, with what you were saying about testing the pipes. If we ever do expand clearly beyond business hours, it's really -- I looked up the CFTC definition of business hours to refresh my recollection. It's 8:15 to 4:45, not including Saturdays, Sundays, and holidays. And I tried to find the history for that, what drove those times. I still haven't figured it out.

But if we do move to clearing -- and by clearing, we've touched upon it, we can make special ad hoc calls based on risk parameters. We're always monitoring the market, and as the market moves against positions, we have thresholds against collateral, guarantee fund deposits, capital, and we'll make special calls. If we make a special call, we always reach out to the Treasury Department of our clearing member. We give them a heads up. They've got an hour to pay. If they don't pay, they're in default.

And the last thing we'd want to do if we implement forms of 24/7 clearing and if we start clearing on the weekends, we don't want to force a default for liquidity reasons. The liquidity is during business days. That's when the banks are set up. That's the relationships the FCMs have with the banks. And even a clearinghouse, we're not liquid over the weekend or a holiday.

What we do with the cash -- at ICE Clear U.S., for instance, we have about $6 billion in cash, and we securitize it. So Friday afternoon, we're investing in U.S. securities. We securitize it to be -- in part, it's the right thing to do, but to be in compliance with the CFTC regs that say, as a DCO, we have to minimize the risk of funds. We have to keep those funds safe and sound. And the best way to do that is to invest in U.S. Treasuries.

And so on the weekends, we're holding Treasuries. If we have a call, a regular settlement call, and if a clearing member defaults to us, we have to pay the other side. We need the cash, or we're in default as a DCO. So we need to unwind those securities. Now, the Fed is proposing 22/7 cash movement over the Fed wire. They're not proposing 22/7 for the securities. You need that, too.

Or I got to do it, sorry, probably the fifth or sixth time I've done it on one of these panels. We need access to a Fed account, not to borrow, but to put our cash where it's safe and secure and liquid. And if we had our cash up at the Fed over the weekend, we'd be liquid.

MR. DEWAAL: What do you do with the suggestion that you could require all your members to have an account at J.P. Morgan so they can move their money using the J.P. Morgan Coin? Not that I'm trying to get them some extra business here.

MR. MCCLEAR: So --

MR. DEWAAL: Does that solve your issues?

MR. MCCLEAR: You'd force all our clearing members to settle through one bank using one form of payment. I don't think so, but --

[Laughter.]

MR. DEWAAL: Yeah, you don't like that idea.

MR. OLSEN: There are live today multi-bank versions of that. Partior has got --

MR. DEWAAL: Yeah.

MR. OLSEN: -- a network of banks where you can have an account at any number of financial institutions and accomplish a very similar --

MR. DEWAAL: Sure.

MR. OLSEN: -- pathway to the J.P. Morgan Coin.

MR. DEWAAL: Um-hum. Reggie, I see you have some thoughts.

MR. GRIFFITH: All right. I have some concerns, especially with the prefunding model. So I work for Louis Dreyfus Company. We're a large global agriculture merchant and processor. And the futures markets are essential to managing the risk associated with our cash business. And I think my first comment is we need to be very careful before we just jump into 24/7 trading. I also think we need to do a very detailed risk-versus-reward analysis. And, as Sean says, I think it needs to be done on a market-by-market basis.

So I'll take the ags. I think the ags do a pretty good job under the current model of managing risk. I think maybe a 24/7 model, there may be some potential perks to that, some potential benefits. But if that comes along with a prefunding model where a commercial has really two choices, we have to go put up an enormous amount of cash on Friday to make sure that, with 100 percent certainty, our position doesn't get liquidated, there's going to be an enormous cost to that, and that cost is not going to stop at the commercial. That's going to flow all the way up and down the agriculture food chain. So it's going to affect producers. It's going to affect end users. It can affect consumers.

If we don't, you know, fund our position to that 100 percent certainty, you know, that would cause a potential liquidation. And I know from an exchange standpoint that might reduce the risk, but that drastically increases the risk to commercials and to anyone, you know, that is using these markets to hedge.

So my one comment would be, I think we need to slow down. I think we need to make sure we understand the risk versus reward of moving towards this model. And I think we really have to look at it from on a market-by-market basis. And I ask that when we do this, we keep in mind, you know, the farmers, the commercials, the end users, and the consumers in that analysis.

MR. DEWAAL: But following up on Dave's comment before, isn't the system today subject to tremendous risk over the weekends because you go back on a Friday afternoon and then the market moves dramatically over the weekend, or something happens over the weekend and the clearinghouse now is sitting on tremendous potential exposure?

MR. GRIFFITH: I mean, over the weekend they are, but we're hedged.

MR. DEWAAL: Yeah.

MR. GRIFFITH: You know, you have your cash risk and your futures risk. You ask me for money on, you know, first thing Monday morning, I'm going to send you anything you need.

MR. DEWAAL: Yeah, but how about the risk that the clearinghouses are being exposed to over the weekend?

MR. GRIFFITH: Well, I mean, I'm giving you the perspective of, I guess, from the commercial. I mean, I think the other part, if we do want to move towards that, I think that there's got to be a better model than a pure just prefunding to your maximum potential exposure. There's got to be a way to move money over the weekend. You know, maybe that's a way that both sides can reduce their risk.

MR. DEWAAL: Okay. Tyson?

MR. SLOCUM: Yeah, so I think echoing your calls, I mean, the original purpose of these commodity markets was to allow producers and consumers to protect against, you know, price risk exposure. And, you know, it was mentioned by an exchange here that, you know, their clients are asking for 24/7 trading. And I'd be interested to know what types of clients they are. I would be surprised if they are producers, consumers, or other traditional commodity players. I imagine it would be more of the speculative interest.

And as Ms. Gordon from J.P. Morgan accurately said, you know, when you move to 24/7 trading, you are greatly expanding the number of tradable hours where you've got very low liquidity and you're going to see significant price disruptions. And that's the whole point, and that's why there's eagerness to move to 24/7 trading because the profit opportunities on this brand-new arbitrage are enormously appealing. They are not enormously appealing for those end users that are now exposed to additional price risks that they may not have the resources to participate in 24/7.

I know some commodity traders. I follow a lot more on Twitter. It does seem that some of them experience various mental health crises as commodity markets go haywire. I can't imagine what the mental health capacity is going to be if you formally expand all this to 24/7. So I'm thinking about not just the capital exposure for end users and producers, but also for the human capital of traders tormenting them to 24/7.

So I just see enormous risks. I don't see that the CFTC has the resources. And, furthermore, I think we would need profound changes in the current position limit regime if you're expanding trading to 24/7 where you've got so many hours where you've got far less liquidity and more opportunity for a relatively small number of traders to unilaterally influence the price in very meaningful and disruptive ways.

MS. LURTON: Gary, can I just comment on the weekend risk element that --

MR. DEWAAL: Yes.

MS. LURTON: -- Reggie had mentioned?

MR. DEWAAL: Of course.

MS. LURTON: Because I think FCMs, we've been dealing with the issue, for example, of holiday processing for a long time, and we've had conversations with Commission staff about it. I think when you think about that weekend risk, it is being borne currently by FCMs and DCOs --

MR. DEWAAL: Um-hum.

MS. LURTON: -- and that's pursuant to regulation that require things like residual interest calculation, aging margin calls. The entire regulatory structure is designed for managing the risk through those extended periods.

When we have discussed with the Commission the fact that holiday processing can be a challenge for FCMs over certain extended holiday periods, the Commission has dealt with it, along with the JAC, with regulatory advisories on how to deal with it. So that risk is currently being managed through regulatory obligations.

MR. DEWAAL: But you're suggesting only an intermediated model?

MS. LURTON: Well, I mean, the DCOs have similar requirements to remain liquid --

MR. DEWAAL: Um-hum.

MS. LURTON: -- so I think it's -- all of the infrastructure is currently through regulation managing that risk, and so those regulations are not yet ready for 24/7. We've had conversations about how to deal with holidays, and as far as we know, the Commission is not ready to change those regulations, so just to comment on where that risk is housed --

MR. DEWAAL: Sure.

MS. LURTON: -- and how it's managed.

MR. DEWAAL: Absolutely. Demetri?

MR. KAROUSOS: Thanks, Gary. So I'd love to recenter the conversation back on risk because I think this is --

MR. DEWAAL: Sure.

MR. KAROUSOS: -- most important consideration. So let's start with weekend risk, right? So I think it's already been said -- I'll just echo it -- that we already face weekend risk. And it's not just in those derivatives that have spot markets that price every minute of every hour of every day during the weekend like crypto, but also other products, right? So, you know, God forbid something happens in the Middle East over the weekend. You know oil is spiking even if there's an electronic trading board telling you exactly what the price is. You know that's happening, and whether that's natural gas or electric power.

So the key thing is, is your risk model already taking into account weekend risk? If you have a properly designed risk model that is measuring risk over a very long period of time and looking at the business day change from Friday to Monday or Friday to Tuesday, and your risk model focuses on tail risk, if those weekend periods represent the riskiest, biggest price moves during the long historical period, then you are managing weekend risk today for existing positions. You are doing it appropriately under existing regulation. There is no gap in managing weekend risk under existing regulations.

Then the question becomes, okay, but 24/7 allows for the addition of new positions, not existing positions, but new positions. That's why we began the discussion with pre-trade risk controls because that's managing new positions. And to be clear, I didn't mention prefunding. That pre-trade risk check can be against a prefunded cash amount, or it can be against a credit limit that you've assigned to your customer. It depends on the FCM's relationship with that customer, right? Some customers, you only want to give them the leash based on the cash in the account. For some customers, you think they're good for a certain amount of credit exposure.

So that's why the pre-trade risk is so critical because it is key to managing how much incremental risk you're going to allow over the weekend. And when you have real-time position management, you can measure it and cut off additional trading at any point. So it all comes together if you're thinking about how to manage each of the individual risk.

What hasn't been discussed yet is how trading over the weekend actually provides risk benefits. So now you have the ability to pick up the phone, call your trader, or, in the case of the clearinghouse, to pick up your phone and call your clearing member and say, hey, you're getting a little long here, you're getting a little short here, could you reduce your exposure? And now you can do that over the weekend in a measured, thoughtful manner, and you can't do that today. So weekend trading actually allows for risk diminution that doesn't exist today.

MR. DEWAAL: How do you address Reggie's problems and issues?

MR. KAROUSOS: Well, oh, so if you do adopt a prefunded model, I agree with you, the model should not be all of a sudden you show up on Friday, and your margin requirement goes from 10 percent, 20 percent of notional that you've been holding to 100 percent. That wouldn't make any sense. So if you were to adopt a prefunded model, it should be for incremental positions only, meaning you have your margin requirement for your existing positions, but, hey, if you're going to trade, you know, a thousand lots of, whatever, Bitcoin over the weekend, you need to have that thousand lots prefunded from a risk perspective over the weekend. So whatever that margin requirement is, you need to have that in your account before you're allowed to trade. All of this comes back to having an effective pre-trade risk control that prevents any addition of risk beyond what the clearing member or the clearinghouse is comfortable with.

MR. DEWAAL: How do you deal with Tyson's comment that we're just trying to accommodate speculators, that the end users really don't have an interest in this?

MR. KAROUSOS: So from an exchange perspective, we spend a lot of time thinking about what products we launch and how they add value to our marketplace. From a clearinghouse -- I'm wearing a second hat here. From a clearinghouse perspective, we are primarily concerned about is this a product that we can properly risk manage? We leave it to the exchange to decide what its market is desiring, what its market looks for in terms of new products. Our job is to make sure that it's appropriate from a risk perspective and that we can manage it appropriately.

MR. DEWAAL: Okay. Alicia?

MS. CRIGHTON: Yeah, I'll key in on a couple of points that Demetri made, I think in particular the idea of pre-trade risk management. And, again, I'll agree with differentiating between pre-trade risk management and pre-trade funding. I would argue, and I think we've long talked about even around this table the importance of that not just in weekend trading, but also for kind of day-to-day trading, so for 24/7. The ability to be able to set limits, define a credit capacity, particularly for the one who's actually standing in and guaranteeing the risk is an incredibly important part of the role that many of us around this table really focus on and provide to the market.

I think, over time, as velocity has sped up, as volumes have increased, and market structure has evolved, there's been a natural kind of separation between what we think about from managing execution risk to managing clearing risk. So I think the conversation here really needs to be focused on how do we think about bringing those two back together and thinking about uplifting the ecosystem to be able to provide clearing services and really the right infrastructure and support around the ecosystem to ensure that we can facilitate the functions of clearing and settlement and actually appropriately manage the market risks that we're all navigating.

I think Allison's point is the right one. We're already dealing with this in terms of weekends, but we need to think about solving this a little bit more holistically, which involves bringing those two functions together, thinking about how they kind of relate to each other. You can't execute without thinking about how you clear and settle and who actually pays for that risk and that they have the ability to cover that risk in the appropriate and timely fashion.

And I think this really relates to a lot of the topics that we'll focus on over the course of the rest of the day. I think these become inextricably linked, particularly as we think about this efficiency of margin and that, again, places an even more kind of increasing role on the focus of margin as that first layer of defense in all of this.

MR. DEWAAL: Joe, I was going to call on you whether you raised your hand or not. Go ahead.

MR. GUINAN: Yeah, I just want to highlight the fact that if the trading week increases by 40 percent, there's going to be a significant cost on every FCM. You're going to need 24/7 risk management people monitoring client positions. And to the point that a couple people in the room made, the illiquidity in the market will likely be profound at different times in different products, and that can lead to, you know, FCMs being forced to try to exit client positions because of a move in an illiquid market. And so I think it exposes the FCM community to a lot more risks because there's already sometimes liquidity problems in the overnight markets, and I think those will only increase if you go to 24/7.

MR. DEWAAL: But I guess what I'm struggling with, as a former FCM guy, don't you have liquidity issues throughout the trading day? There are periods that you want to liquidate and you can't because the market just isn't there for you.

MR. GUINAN: I think the only time that we kind of see that is a little bit overnight, but it's not a big problem. It's currently not a big problem. But, again, like, I don't know what Sunday morning trading would look like.

MR. HUTCHISON: Hey, Gary, you've got two behind you.

MR. DEWAAL: Oh, okay.

MR. HUTCHISON: Actually, three or four. Excuse me.

MR. DEWAAL: All right. Let's start with Stephen.

MR. BERGER: Thanks. For just a few reactions and observations to some of the points I've heard, I do agree that you could probably do 24/7 trading without requiring prefunding, but I think the combination of 24/7 trading and the next topic of non-intermediated clearing, like, I think there's a direction of travel that suggests there's going to be a move to more broadly requiring prefunding in the market. And I think to pick up on the concerns that Reggie raised, I do think that creates challenges from a capital efficiency perspective. To the extent there's a bunch of different liquidity pools that you want to be active in, you have to split up your capital and pre-deploy it ahead of time. And that has, I think, knock-on concerns with respect to market liquidity and market resiliency to the extent that there's less capital efficiency and you have to split up your capital to be able to be ready and positioned to either trade or maintain a portfolio in the face of price movements.

So I just think that's a -- like that's not a reason not to explore it, but I think it's a consideration we have to bear in mind because we don't know where the end is. And if we start down the road to markets all moving to having to prefund margin, you know, I think we need to be aware of the consequences there.

Again, not to dampen the enthusiasm for 24/7 trading, but it is not the universal direction of travel. I think we've actually seen a number of markets in recent years strongly consider reducing trading hours in an effort to concentrate liquidity. So I think the U.K. and the EU were looking at this in their own equity markets within the past few years, and we've seen, for better or for worse, an increasing amount of trading occurring in closing auctions in the equity markets, for example, given a desire to be able to trade like at that benchmark for certain types of funds.

I think to the point that Kevin and others made, I do think a lot of the questions do boil down to how the clearing and the risk management at the clearing level are going to work. So I guess I'm curious about, you know, when does the daily strike occur that, you know, determines the mark-to-market and the VM obligations that are going to be associated with it? I think there's a lot of concern in the institutional investor community about the potential for intraday margin calls just today, and so I can only see that potentially being exacerbated going forward. And then I do, you know, question, how, you know, default management and liquidations of portfolios will occur at different points in time.

I guess one final observation, and I do want to preface like all the -- all the questions I just raised are not indicative of not a desire to see evolution and innovation on this front. They're just things I think we should be mindful and consider and solve for as we go forward.

And then the last one, I think, which is maybe something for the CFTC to consider, as we go in this direction from just a licensing and registration perspective, there's going to be a need for employees around the world to be involved in tasks that are relevant to, you know, CFTC-registered entities. And so I think we'll need to be thoughtful about how that licensing and what sort of registration requirements will apply to both personnel and offices around the world that we'll need to have live and active to support 24/7 trading.

MR. DEWAAL: Dave?

MR. OLSEN: I want to quickly address the question of like, well, why would anyone want to trade on the weekend who might not be a speculator? I think geopolitical events and the price of natural resources is an obvious opportunity for those that are end user participants in that market to manage their inventory, manage their production risk.

You know, you think about the last month, we've seen hurricanes strengthen from category 1 to category 5 in 12 hours. If you have orange groves in Florida and you had the ability to hedge your position, you know, while that was unfolding over a weekend instead of waiting 72 or 96 hours to go back into the market and hedge your crops, I think the agricultural community for sure.

It is more difficult to trade in thin markets. I don't expect the same liquidity to exist at the outset on the weekend, but I think from a policy standpoint, should those end user participants have any market access at all should they choose to participate or have that remain closed?

And then, finally, I think this is a terrific opportunity for the United States to lead what is a global trend. We are frequently getting incoming calls from exchange groups around the world that are looking at addressing this vacuum that exists in the market. I'd love to see that happen in the United States in a safe, orderly, controlled way rather than having that vacuum filled offshore.

MR. DEWAAL: J.B.?

MR. MACKENZIE: Well, I just want to quickly address this conversation of sort of who the market is for? Is it for hedgers? Is it for speculators? Because I actually think in this case, this is one of those well-established or maybe older rules that needs to be updated. And what I mean by that is, under the current CFTC rules, right, a hedger is a bona fide hedger, right? Myself, who may have $50,000 in a variety of NASDAQ stocks that uses the E-mini NASDAQ to hedge his portfolio, I'm still a speculator.

So I think this idea that it's only hedgers and speculators out there, I would argue probably

95-plus percent of the market are speculators in there looking for price movement or hedging some smaller part of their overall portfolio. So as we figure out who's going to be participating in these markets, it is not just retail investors. It's not just hedge funds. It's smaller funds. It's participants across the world that want to come in there because of what Dave was mentioning about here where there are markets that are moving and there's events that are occurring.

So I think if we think about who's participating, it's not just about large institutions that have an agricultural focus. It's for individual small funds, people that have exposure to the markets because they actually own securities, equities, et cetera, along the way.

MR. DEWAAL: Jan, you had your card on the side.

MR. DE BOER: Yeah, I was going to add to that. Ultimately, of course, we would like to go to central bank money. And ultimately, we also need to be able to move securities in the weekend.

But we see many markets around the world, spot markets where it's prefunded. We deal with the Golden Week in in Japan. So up to a certain moment, probably our community can handle these markets with, what, call it pre-trade risk or prefunding. But if we really want this movement to continue so it's not just, well, mostly retail because that's what we see in the CFD markets around the world, probably other steps need to come as well.

MR. DEWAAL: Got you. And Bill?

MR. THUM: Hi, thanks. So I just wanted to address the speculator issue as well, you know? And I know many of our members currently pass the book around the globe into liquid markets as they appear because they know that they need to hedge the risk. They know they need to take advantage to meet portfolio objectives. I think the issue of prefunding or, indeed, speculators taking advantage of an illiquid market suggests that that market isn't ripe for 24/7 trading. So it would seem to me an exercise akin to T+1 and the whole industry coming around to that, so a multi-year effort where all constituents have to demonstrate that there's the infrastructure, the wherewithal, the interest to be able to achieve it because, absent that, you're going to have a very illiquid market if it's not during core trading hours. People are going to take advantage of it. Prefunding for many of our members is just not an option for reasons that Stephen said. So I think if we could get to the point where the infrastructure could support it and, indeed, liquidity was developed and things like prefunding weren't needed because there would be live margin transfers, the infrastructure would support that, then that would be something that I think our members would appreciate and actually have to do to meet investor demand.

FEMALE SPEAKER: Actually, Matt Daigler had his card up. Matt, did you want to say something?

MR. DAIGLER: Yeah, I was just going to make just a couple thoughts. I think that certainly this is something worth exploring, 24/7 trading. And certainly there's an appetite in certain circles. It seems to me that it depends a lot on the asset class. And we've been talking about digital assets and where it may make the most sense. I don't know what the appetite is, at least among the institutional investor community for 24/7 in some of the more traditional markets. And, you know, it's not to say that that's a bad idea, but as one of the gentlemen remarked, there are costs in having to monitor your positions 24/7. We've raised issues about margin calls.

And then I also wonder, we're only talking here about the derivatives markets, CFTC-regulated markets. There are obviously the related equity markets, options on equities. Are these markets going to get out of sync if they're trading on different, you know, time frames? So I just think there's just a number of considerations here. Someone made a comment about the potential for a pilot program. That is one way that this 24/7 could be addressed incrementally, start very slowly with one kind of product, one kind of product or asset class, and then see how the experience is and let the infrastructure develop.

MR. DEWAAL: So as we try to wrap this session up, Clark, I think what I'm hearing is a consensus is that, generally, people want to explore 24/7 trading, but it's not going to happen overnight, and there's a lot of thought that has to go into it in advance.

MR. HUTCHISON: I agree with that summary. I know the clock says we have some time, but we have a little bit more time because we finished early on the other one, and I'd like to pose a counter argument just to see what people say.

So a clever person could come to me and say, look, 24/7 can be allowed, but you've got to do many, if not all, of the following things to allow flexibility. So I'm going to look for a raise of hands when I finish. So if you're an FCM or even a clearinghouse, letters of credit. People can have letters of credit, guaranteed letters of credit, money will flow on Monday when the money can flow, but over the weekend, you've got a letter of credit against which I'll call it credit can be given so that positions can be understood.

You could have prefunding. Prefunding at what level, that could be determined, let's just say, but prefunding is an option. Some people don't want it.

What about residual interest? You know, an FCM has the ability to risk manage and have a credit appetite with its clients, as it does today over the weekend, for example, but residual interest could be increased such that risk could be covered.

What about qualifications of market participants to trade 24/7? Maybe it should be that only people of a certain credit rating could trade. People of a certain commercial characteristic could trade and maybe not open to retail, let's just say.

What about the idea of changing the CFTC rules such that now we make a big deal -- I don't mean to be pejorative -- about separating foreign currencies from U.S. dollars? What happens if we didn't care about that anymore? Australia is open a lot when we're closed, and why can't, over the weekend, Australian dollars be used, for example, to deal with debits and credits, and on Monday, everybody returns it back to dollars? But we understand that, you know, currencies are currencies and haircuts, and you have liquidity in banks in other countries when our banks are closed.

What happens if some combination of all of this is put into a rubric by which 24/7 can happen when, until we get to the point where our banks are open, and, as people say, the infrastructure and everything is there?

So I just pose that as the contra. And so by a raise of hands I'd ask in some combination of what I've just said, would you vote yes, that we should consider all those things in some way, or would you vote no and say, you know, interesting, but too hard to do? So who would vote yes on some of those contras?

[Show of hands.]

MR. HUTCHISON: So I put those as guardrails, so we have some yeses. Who would vote no, and then there may be undecided. Anybody want to vote no?

[Show of hands.]

MR. HUTCHISON: Okay. A couple of noes. Okay. We have noes. And then the undecideds, I guess, well, you know, you want to think about that some more. So that's all I wanted to add to the conversation is just corral a little bit more of the thought from what you just summarized, Gary. Okay.

FEMALE SPEAKER: Well, actually, Demetri, do you want to get the last word?

MR. HUTCHISON: Demetri, you can have the last word.

MR. KAROUSOS: Oh, that's quite kind. I just wanted to provide a couple clarifications. One, I think there was a comment about concerns about how marks could be used over the weekend for surprise calls or whatnot. Stephen, just to be clear, when I was referring to the concept of current exposure, the concept of mark-to-market, it was simply for the purpose of managing your trading capacity. We agree that there should be a lot of thought and time associated with the production of settlement prices, which then lead to formal margin calls. But just for managing pre-trade risk capacity, the idea of watching how prices are moving and trying to prevent you from doubling down, we think that's an important and useful adder.

And the other bit is we do agree -- and maybe I hadn't made this clear -- that we should in fact think about different asset classes differently here. I mean, the one thing to note is in the major, for example, crypto category, there is spot trading going on 24/7 today, and weekend trading is not demonstrably lower in terms of liquidity from weekday trading, right? It might be 60 percent in that range, plus or minus, but we're not talking about liquidity completely disappearing during the weekend. So I just want to have that as a clarification when thinking about this topic.

MR. DEWAAL: Clark, if I may, I want to turn to Kaitlin for a second.

MR. HUTCHISON: And we have Alicia, too, so --

MR. DEWAAL: Yeah, I want to talk to Kaitlin for a second.

MR. HUTCHISON: Yep.

MR. DEWAAL: You regulate stablecoins also in New York State. Under MiCA, there's now going to be robust regulation of stablecoins in the European Union. Obviously, you're hearing that people want to use really good collateral in connection with potential 24/7 trading. Would you feel comfortable if our industry relied on regulated stablecoins by the State of New York?

MS. ASROW: Again, you know, I'll defer to kind of your industry's comfort, but I will note, you know, we do have deep experience. And currently, all of our regulated stablecoins that are on our green list are out of our limited purpose trust companies. And we have issued guidance, I believe, about two and a half to three years ago on the reserve assets, the kind of settlement, the liquidation of those stablecoins, redemption rights, disclosures for consumers. And we are partnering with Europe on how we move forward in kind of overall stablecoin oversight.

So we do feel, obviously, very confident in the oversight of our stablecoins. We're doing real-time monitoring on those reserve assets at all times. And, like I said, we do expect other regulators to kind of, you know, reach harmonization.

MR. HUTCHISON: Great. Thank you. Alicia?

MS. CRIGHTON: Yeah, I guess just one other comment. I think, you know, part of the ways that we've been thinking about this is very much in a bilateral way, right, between the participant and the clearinghouse; or between the participant, the exchange, and the clearinghouse; or between the participant, their clearing member, and the vertical. And I think what we're forgetting here is that we're all actually part of a linked ecosystem because we are part of a mutualized pool, so decisions that one part of the ecosystem makes naturally impacts every other participant. So I think it sort of really forces us to need to take a step back and, again, think about joining up execution and clearing risks, the alignment of incentives, and how the ecosystem needs to respond to this.

So, Clark, it's not really a yes or a no answer. It's just kind of thinking through what does this mean for the ecosystem because none of the decisions that we make will have bilateral impacts.

MR. HUTCHISON: Okay. Thank you.

We are actually pretty much on time, so thank you very much for allowing that to happen. Let's take a break. And according to the master schedule, we'll reconvene at 11:00. And why don't we make that five after 11:00? And then the following two modules will occur after that.

And I just want to say with the next two modules, they're closely related in many ways, and I think it may be difficult for us to keep things separate, and I don't know how we're going to navigate that exactly, so think about that when you make your comments, and we'll try to navigate these two together as best we can.

So I'll see you at 11:05. Thank you.

[Recess.]

MR. HUTCHISON: Okay. I need to ask that everybody take their seats and we'll get going again. Okay. We're going to get started on the last two modules. Thank you for keeping this on time.

So the next module is -- I have it in my notes here -- is direct clearing and margin, but what I really want to say is non-intermediated clearing with margin. And I want to make sure that we establish a boundary on this. I and the chairman had a roundtable back in 2022 on this topic, and what we don't want to do is rehash what it is that we already did a couple of years ago. I think we're all very familiar with the idea of or the challenges posed by clearing that is non-intermediated and with margin. So I don't think we have to rehash a lot of what we know. So I think where we want to head with this is, are there ways in which this can occur or not? Are there ways in which perhaps -- well, I'll leave it like that. I won't lead you with some thoughts. That would be number one.

But then number two, we can drift into the next module as well because affiliations and the idea that in a vertically integrated model, which we have today, where exchanges and clearinghouses can be related, but we have market makers that could be related, we have FCMs that are related, we could have separate custodians that are related, and we could have non-intermediation within that in some respect, I can see an overlap. So Gary is going to try to lead us through an organized conversation, but I know it will drift, but let's not rehash what we did two years ago.

So with that, I'm going to turn it back over to Gary and we'll get started.

MR. DEWAAL: Oops, sorry. All right. Let's start with a bunch of polling questions first just to sort of get the sense of the audience. So, by a show of hands, who thinks that DCOs that are disintermediated and deal directly with non-FCM members should themselves be required to additionally register as an FCM or be subject to rules that impose requirements on FCMs to which they currently are not subject?

[Show of hands.]

MR. DEWAAL: Raise your hands higher because I see half -- okay. Okay. For those of you guys who voted yes, who believe that such requirements should apply to DCOs that deal directly with any non-FCM member or solely to DCOs that deal with any non-FCM member that is not an eligible contract participant or another measure of sophisticated or institutional client? So the question here is, you know, should those requirements of paralleling FCM rules only apply to disintermediated DCOs that deal with, you know, non-sophisticated clients or to sophisticated clients? So for sophisticated clients, the rules wouldn't apply. Who agrees with that approach?

[Show of hands.]

MR. DEWAAL: Only one. Okay. All right. Let's explore this in a bit more detail, and let's start with you, David.

MR. OLSEN: [Off mic].

MR. DEWAAL: Sorry, that's the danger being the only guy who raises their hand.

MR. OLSEN: The way I interpreted the question was, if there is a participant in the market that is sophisticated enough to meet the standards for direct exchange membership and direct clearing membership --

MR. DEWAAL: Um-hum.

MR. OLSEN: -- that that is a separate matter than, let's say, a retail or smaller institution that could not satisfy those requirements.

MR. DEWAAL: Well, provided that the requirement on that exchange would only allow sophisticated clients to be members. Remember, on many of the disintermediated exchanges, the members are retail clients.

MR. OLSEN: Right. So I think that the standard setting for what capabilities and capital amounts and liquidity profile, assuming those are set to a high enough standard, I don't think you need to go into additional classification of the DCO. But I think if it is open to those types of participants that could not meet those criteria, then that's behaving much more in spirit like an FCM does today, and a DCO should have the capabilities and oversight that are comparable.

MR. DEWAAL: So traditionally -- and, Clark, you'll have to tell me on this one if I'm wrong -- the CFTC has required disintermediated DCOs/exchanges to represent that they'll act -- for example, they'll honor the BSA as if they were an FCM. Are you suggesting that even those kind of requirements shouldn't be required?

MR. OLSEN: No, I think that's appropriate.

MR. DEWAAL: So there are some things out there. Is there anything else other than BSA that you can think of that even for a DCO that deals with sophisticated clients, they should pick up FCM obligations?

MR. OLSEN: You know, without recalling the comprehensive list, I would say almost certainly there would be, and it would depend a lot on the definition of sophisticated.

MR. DEWAAL: Got you. Alicia, I'm looking at you. I think you have some views on this subject.

MS. CRIGHTON: So I'm kind of thinking back to your first question. And I think, you know, if I go to the heart of what we're trying to address, right, you know, thinking of the vertical, DCM, DCO, SRO, and now potentially layering in an FCM into that chain, it kind of brings me back to, you know, some of the comments I made earlier. One is it continues to kind of think about, one, how we think about margin as a first line of defense, the sufficiency of margin. Where do the checks and balances exist to ensure that margin levels are appropriately calibrated to protect the system? The more you integrate into that vertical, particularly, again, DCM, DCO, FCM, and SRO, the less of the kind of a set of checks and balances you have to ensure that those functions that they each perform and are regulated to perform are appropriately calibrated.

So it brings up a set of conflicts that I think are present in the existing model. I think it certainly increases the amount of conflict on the forward. But it also brings into question a number of things that I think we're grappling with in the current market structure. And, again, I like wear the sign about sufficiency of margin, right? It's a concern we have. This increases my level of concern exponentially.

And, again, thinking about the ecosystem risk that we all face -- and I made that comment in the last session -- all of those things become incrementally heightened as we think about putting these things together or having more of a disintermediated model, the risk to the ecosystem becomes even more pronounced. And I think we have to think about each of those things. What is the regulation around that? What are we intending to do with that regulation versus just heading down this road of disintermediating a function that's provided a lot of safety and soundness to the overall market for a very long time?

MR. DEWAAL: Okay. So for this panel, we're going to assume that there actually is no FCM in the chain. The question is, should the DCO pick up

FCM requirements, or should DCOs also be required to pick up an FCM registration in order to be disintermediated?

MS. CRIGHTON: I have a little bit less of a view on that because I'm assuming I wouldn't be in the chain, but --

MR. DEWAAL: Um-hum.

MS. CRIGHTON: -- to bring it back to the principles, right, of --

MR. DEWAAL: Yeah.

MS. CRIGHTON: -- you know, customer protection, safety and soundness. How do we enforce some of the principles that are core to the model today and are core to the functions that FCMs do provide? So how do you actually kind of recreate that in a model where I don't exist?

MR. DEWAAL: Okay.

MS. WOODING: Gary, we have a view on that.

MR. DEWAAL: What's that?

MS. WOODING: NFA has a view on whether that DCO needs to be an FCM.

MR. DEWAAL: I had a hunch you might have a view on this.

MS. WOODING: So, I mean, we've obviously put this in our comment letters, but we really do question whether the CEA lets a DCO deal with a customer with a margin or leverage basis. And so we do think that the definition of FCM, if those are FCM activities, you're required to be an FCM, whether you deal in futures or cleared swaps. So we do think they either have to become an FCM or does Congress have to work with the Commission to create a different registration category for these non-traditional DCOs? Because they really do serve, in many respects, a different function.

And we think that one thing that is missing, even if you just applied FCM customer protection requirements, say, DCO, you have to provide these protections to your -- let's even just say your retail clients, there's no SRO that's overseeing that. Obviously, NFA plays a very important role --

MR. DEWAAL: I was just going to ask you, do you believe that DCOs that are disintermediated should have an SRO?

MS. WOODING: I do.

MR. DEWAAL: Um-hum.

MS. WOODING: And NFA really does believe that. We think that, especially for their customer-facing activities, there's very little difference there. The individuals that customers may be dealing with at a DCO aren't registered. You're missing all those protections as well. So there's a reason FCMs are part of the infrastructure in this industry, and there's a reason that all those rules are there, and they just fall aside when you have a DCO that's directly dealing with a customer. And, again, we go back to that really threshold question, can a DCO even do that without an FCM registration?

MR. DEWAAL: Bill?

MR. THUM: Yeah, I'd just like to weigh in and say we certainly have members that want to be direct participants in the model, but I think that, you know, getting to Alicia's point, the FCMs currently provide such a fundamental customer protection regime and through contributions to the default fund. and the whole scenario that we've looked at over the past 10 years really provides stability for the market overall.

I don't think it's just that the DCO would have to perform as an FCM. I think there would have to be a fundamental reevaluation of how the system operates. So, you know, our members -- and certainly, whether it's the CFTC or the SEC, our members are interested in being direct participants. But, you know, I scratch my head and say, how does that work in terms of the safety and soundness of the overall model? That's my personal question there --

MR. DEWAAL: Okay.

MR. THUM: -- but I agree with Alicia.

MR. DEWAAL: Matthew?

MR. DAIGLER: No, I just want to add -- and I don't want to harken back to a couple years ago, but I think there's also the risk of creep. So, you know, you maybe have a disintermediated model that works maybe for certain asset classes or for certain kinds of products, but there are lots of questions about how it spills over to maybe the more traditional model. It's not just the risk of, you know, one type of clients that pose to other types of clients, but just that if we have kind of a novel model for maybe one asset class, like, say, digital assets, that maybe works for that given its particularities, what are the implications if we start taking those same changes and move it over to a model that's frankly worked very well for many years and, you know, where there's been important protections of the FCMs? So I just think it's a lot to be thinking about.

MR. DEWAAL: Kevin, you knew I was going to call on you because I'm thinking about ICE NGX.

MR. MCCLEAR: So let me give a description of ICE NGX because I'm not quite sure everybody quite understands what kind of clearinghouse it is. It's used as an example of a direct clearinghouse, and it is, but we clear directly with certain types of counterparties. We call them CPs, contracting parties, so they enter into a clearing arrangement with us. They are approximately 230 active CPs. But it's a physical market. That's very important. It's a physical market in gas and power. So each and every one of those CPs has to be in a position to make or take physical delivery of gas or power. So it's a different type of clearing member.

They don't have customers. They each clear for their own benefit. So it's not the retail direct clearing model that we're sort of talking about right now. It's a different model. And it's important to understand, too, that it's a DCO, and we apply all of our risk management framework practices to NGX. We have our counterparty reviews. We have an internal credit rating methodology. We rate each and every one of those 230 counterparties, and we monitor them on an ongoing basis. And then we collect margin. We have our core margin, but we also have our addons. We have shortfall margin, which is a credit-based margin. Depending on their creditworthiness, we put them in different buckets of their capital. And we mark those positions to market. We're monitoring them every day. We make calls. They're fully collateralized. It's more of a traditional clearing model applied to a physical market.

MR. DEWAAL: Carol, I turn back to you. Would you think there should be a distinction between disintermediated DCOs that deal solely with sophisticated clients versus non-sophisticated clients?

MS. WOODING: I think probably. I mean, those clients, those sophisticated clients have the resources and the wherewithal to provide much more, you know, due diligence to protect themselves. And I think a lot of the direct clearing DCOs we're seeing are actually -- most of their clients are retail clients, and that's why I think NFA feels strongly that there has to be some different type of infrastructure put in place because it makes no sense that just because I'm a retail person dealing directly with a DCO, that I am not getting these customer protections that have worked so well over, you know, the decades that these markets have been trading.

MR. DEWAAL: Tyson, I have a hunch you might have some views on the subject.

MR. SLOCUM: I actually don't right now.

MR. DEWAAL: Oh, I'm surprised.

MR. SLOCUM: But thank you.

MR. DEWAAL: Okay. Allison?

MS. LURTON: Yeah, I guess I just want to clarify maybe a couple things. In the first set of questions we explored, I'm not clear if the question is whether a DCO that discharges all of the duties that an FCM also does needs to also register, or if you're just saying a DCO doesn't need to also observe and honor those requirements. Because I think when we were in this room a couple of years ago, we did discuss all of those detailed things that an FCM does --

MR. DEWAAL: Sure.

MS. LURTON: -- in the equation. And I'm not clear exactly what we're talking about. There are capital resources. There's customer protections. But there's more. There's a system of checking. Operational errors are caught when you separate functions. So the idea that the CEA intentionally separates these functions adds a layer of risk that I don't think can be replicated necessarily when you completely remove it.

You could, however -- in the situation that Kevin's just talked us through -- in that instance, I always assumed the Commission went through the exercise of determining that the risks were minimal there, and it made sense. You're talking about entities that have to be licensed to take delivery and all the other elements that Kevin's outlined. So it's not that it can't exist at all, but it seems to me if we're talking in generalities, it's not 100 percent clear to me what the question is. To me, a DCO should register as an FCM and discharge all of those duties. I don't know so much about the paper registration so much as the separation of functions, including the SRO.

I mean, in other parts of our rules, we have concentration risks, limits. There are limits when you concentrate risk in certain areas, including where you invest customer funds, for example. So I guess we see an element of concentration risk as well in discharging the duties in a single entity.

MR. DEWAAL: Yeah, I'm not sure you can solely, as the rules and the law currently is written, just sort of tack on an additional registration because there is overlap just in the capital area, for example. I don't know how you apply that to one entity holding two licenses. So the --

MS. LURTON: So is that the question? Does the act permit or require --

MR. DEWAAL: No, no, no, no, the answer --

MS. LURTON: -- a separate registration?

MR. DEWAAL: -- is more theoretical. The answer is more --

MS. LURTON: Okay.

MR. DEWAAL: -- theoretical as to whether it should be, you know, you have to register as an FCM or pick up the requirements of an FCM --

MS. LURTON: Okay. I see --

MR. DEWAAL: -- you know, depending on how --

MS. LURTON: -- the question.

MR. DEWAAL: -- and how the regulators decide is the most appropriate means.

Reggie, I'm turning to you. So, you know, there at least some of your competitors, I believe, have been clearing members of exchanges for a long time. I don't know whether Louis Dreyfus --

MR. GRIFFITH: Yes, we have an entity that is a direct clearing member of a number of exchanges.

MR. DEWAAL: Okay. How do you feel about the subject? Do you have any issue with the DCO dealing directly with you as a clearing member, or do you think that it should be picking up some FCM requirements in order to do that?

MR. GRIFFITH: So I think the direct clearing model works very well for certain large, sophisticated firms. And I think the same protections are in place, but the DCO basically puts the exact same FCM standards, besides some of the customer protection rules, directly on the market participant. They have regular risk reviews. So I think for large participants, you know, I think the direct clearing model works.

But let's be very clear that they're very high-risk management standards. It's probably not a model that works for the majority of the market, but I think for a certain small amount of customers that are sophisticated, I think it's a very viable model for sure.

MR. DEWAAL: Zach, I'm turning to you again.

MR. DEXTER: So I want to take a quick 30,000-foot view. I think there are structural reasons why new venues tend to want to go for a two-layer DCM, DCO, disintermediated model at first. And there are things that could be done to address those structural incentives. I think even in our case there was always a desire to go to a three-layer model, not to register as an FCM even though that would be good on the protections front, but to actually add other FCMs for capital efficiency reasons because we thought it would be better for the end customer.

But when you're running a new venue and you're trying to get off the ground, it's often easy to start on a fully collateralized basis, to start without the tech lift of integrating with brokers, to start without the guarantee fund. And that, in turn, drives product choice. I mean, a lot of the new products we're seeing in binary options and fully collateralized digital asset products, I think that's been driven by the structural incentives of people wanting to start with a two-layer model.

So if there were, like, a crawl-walk-run approach for the three-layer model that's clearly laid out, like you can maybe start with intraday margin at your FCM members but no margin at the clearinghouse, and then in phase two, you have, you know, low position limits and a high margin period of risk, and you kind of scale that down over time. I think new venues would be structurally incentivized to choose the three-layer model, which is actually where most of them want to end up, not all, but most want to end up there.

MR. DEWAAL: David, I'm curious. You just started a new exchange and clearinghouse where you expressly went to an FCM model. What's the thinking about that?

MR. DAVID DOWNEY: We are sickened that the FCM model has declined. We understand why. CFTC regs, when they went to net-to-gross margining, it decimated the model. We believe that that model needs to be resuscitated. I believe in the FCM community we're going to give them incentives to rejoin.

And now I must say my model is fully collateralized, so I don't have the exact same problems that everybody else does. And I don't want to try to impress upon you what you should think about when you deal with your own risk, but for a fully collateralized position, we are uniquely situated. And even in those positions, I believe the FCM should be there. All of the protections that they provide have value to me, and as long as they provide their value at a reasonable cost structure, I think it should be encouraged and not discouraged.

MR. DEWAAL: All right. Matt?

MR. LISLE: So let's go to the land of

unicorns and rainbows and think in broader strokes. I think we need a new acronym, and I think the exercise should start with an analysis of what a DCO does and what an FCM does. An analysis, if you can put those two together, then I think that we can come to some sort of common ground.

I think that there are overlaps between what a DCO and an FCM does. I think you can find some efficiencies. But I think everybody's saying the same thing here, that FCMs provide a very, very crucial role that can't be discounted. I think that the term disintermediation is kind of fallacious in that, you know, maybe you're getting rid of the FCM, so dis-FCM'ed, but in terms of that function of intermediary, you still are going to have to have it, you know, whether it's BSA/AML, whether it's credit monitoring, all of those things that we know that a DCO isn't necessarily focused on.

So I think that if you can just strip it down and then kind of come back at it and say, well, here are the crucial functions and how do we address that and set up a structure, you know? But that will be in the land of rainbows and unicorns because you'd have to get an amendment to the Commodity Exchange Act.

MR. DEWAAL: How do you address Zach's issue that it's quicker to market by eliminating the FCMs, at least in phase one of the development of a new exchange with new products?

MR. LISLE: Well, Wedbush is pro-competition and certainly is always open to new models. Does that mean that we can compete in that arena as well just as a strict FCM? I don't think so. And so I think we would point to the fact that, you know, you're still blind to some of the risk that we address.

MR. DEWAAL: Got you. J.B., do you have some thoughts?

MR. MACKENZIE: So I think the FCM model is crucial. I think the expectation for any end customer should be to have the identical protections, whether they go through an FCM or go directly to a DCO. It seems odd to me that we would ever want to separate them out. It just, in my opinion, creates more confusion.

I don't know initially that it also stops innovation per se. I think the question of being is, as these new DCOs and DCMs are coming up, are they engaging with various FCM participants to see whether or not that product fits for what they're trying to do? If the answer is, I just want to try to prove that there is demand to trade in these products by getting as many people as possible to come through my doors, it doesn't necessarily incentivize me as an FCM that has a large retail base to go to that marketplace. If I have a DCM or DCO that comes to me and says, hey, how should we build this product? How does it fit your client's needs? And I can go and guarantee that when that client comes through my doors, they get the same protections, whether they go to ICE, CME, or to MIAX, that's what we should strive to have at the end of the whole conversation.

MR. DEWAAL: Okay. Demetri, you must have some thoughts.

MR. KAROUSOS: I do. I just don't know how to avoid Clark's prohibition about retreading territories. I'll do my best, Clark. So, look, we think the FCM model is critical in lots of ways, right, but most of all because we're talking about the derivatives industry, not the cash markets, right? And so inherent in the derivatives industry is risk, is the fact that you can buy something or take a position on something for 10 percent or whatever the value, right?

So given that risk is there, what the FCM model has delivered over the years is a second set of risk judgments on every activity that takes place. It's a second set of judgments on your risk model, on your risk practices. It's a second set of judgments on the traders' willingness to take on risk because the FCM is guaranteeing that performance, so now the FCM is second guessing those decisions. And that has proven to be a very safe model to trade with a decent amount of risk, right?

So we were very concerned about breaking down that model, whether it's this discussion or the next discussion of the DCO and the vertical integration between the DCO and an FCM. For us, it's the same thing. We are breaking down a distinct FCM layer. And so from just a pure risk management perspective, we have some concerns.

Secondly, we don't think it's great for customers, right? So the existence of competing FCMs that cater to individual customers' needs. Some FCMs cater to larger utility type or, you know, larger institutional customers. Some cater towards retail customers. The FCMs generally get to know your business. They get they get to understand what's motivating you, what -- you know, and so removing all of that and having effectively a single mono FCM at the DCO doesn't feel particularly pro-customer either, right? So I worry about that. And we certainly see customers exercising their freedom to shift from one FCM to another. That disappears in this model as well. So we just have some serious concerns about abandoning that traditional model.

MR. DEWAAL: Does full collateralization solve a lot of your issues?

MR. KAROUSOS: Yeah, I mean, that's almost not a DCO. I mean, in that world, we think that just deserves a different category altogether. And I think it would clarify all the rules associated with normal DCOs versus fully collateralized entities. We don't think of that as the DCO model. It's a different model and should probably have custom rules for that model, but that's a very different model, right?

MR. DEWAAL: So I'm hearing a different model on full collateralization, and I'm hearing about unicorns and -- okay. Sean?

MR. SEAN DOWNEY: General thoughts?

MR. DEWAAL: General thoughts.

MR. SEAN DOWNEY: Yeah, so I will echo Demetri and say I will work really hard not to harken back to two and a half years ago. But, I mean, as a general matter, we're supportive of the model that exists today. It's been through quite a few market events successfully. It's very challenging, I think, to replicate all the protections in place based on the different layers, based on the resources, based on capital that exists in today's model. And so the question I would just ask is how you actually successfully do that? I mean, I will point out we do have direct participation, but those direct participants meet all the standards that FCMs do, other than the customer protection side of it.

So I think, you know, from our view, the model works really well. We're very happy with all the customer protections that are in place. And it's just a question of, could you actually replicate those on multiple different levels, which I think would be a challenge, and I think a challenge that has been observed in recent events.

MR. DEWAAL: Okay. Joe, thoughts?

MR. GUINAN: I think if a DCO is dealing directly with its clients, I don't see a big problem with that. I do think it should have to register as an FCM.

And I also think on a related, call it a corollary topic maybe, I think that only FCMs should be hitting the big clearinghouses. So the clearinghouse has mostly FCMs and a few non-FCMs. I think everyone that accesses the big clearinghouses should be required to be in the FCM even if it's a prop shop or something else because I think having the CFTC oversight of everyone that is participating in the clearinghouse helps ring-fence the clearinghouse. So I know that's a corollary topic --

MR. DEWAAL: Even commercial ends users?

MR. GUINAN: If the majority of the members bringing the trading to the clearinghouse are FCMs, I think all the members should be FCMs, and thereby ring-fence the clearinghouse.

MR. DEWAAL: Reggie, any thoughts about that?

MR. GRIFFITH: I mean, I think we're really already there.

MR. DEWAAL: Um-hum.

MR. GRIFFITH: All the applicable rules, besides the fact that we only trade for ourselves, so the customer protection, they don't make a lot of sense, we're already complying with. We already have a DSRO. We have very thorough audits from a risk standpoint, so I think we're really already there in substance.

MR. DEWAAL: Okay.

MR. HUTCHISON: Gary, we've got David and we've got Ann.

MR. DEWAAL: You know, I'm looking around constantly, and then as soon as I turn my back, that's when they put their cards up. This has got to stop. Ann?

MS. BATTLE: Thanks. I think we support some of the comments that have been made about, you know, taking it to a higher level, looking at CCP best practices for risk management and applying that to a different model, as opposed to trying to say that the role that the FCM plays could just be imposed on in addition to the role that the DCO plays.

I think a lot of those best practices were discussed two and a half years ago so I won't go into those, but just to emphasize a couple, including what Alicia and Bill said about margin, margin for cleared transactions is something where a lot of global work is going on, ISDA, along with other trades and our members, were very involved in the recent BCBS and IOSCO consultation on ensuring that margin models don't fall too low, including in low volatility periods.

And I think if you go to a model where the FCM is no longer guaranteeing the trades, that work becomes even more important, and it's important to look at it both when you have that guarantee and when you don't. Similarly, default fund sizing, a lot of work has been done at the global level on that, and that's something that you'd have to actually look at when you have these direct participants clearing on margin.

And I take the point that some of that is happening today, but if it were, for example, to be expanded, I think you really need to look at it fresh from that perspective instead of trying to put the role of the FCM that was developed for a different purpose into the role of the DCO.

And then the last thing I will say, which I don't think has been mentioned is, you know, ISDA has also done a lot of work on recent capital proposals, and, you know, the impact that those would have on clearing, which I think is beyond the scope of today. But it is, I think, one of the reasons we're looking at different models, not the only reason, but one reason is definitely the balance sheet constraints on FCMs. And I think addressing that could actually go a long way in ensuring that the role the FCM plays in the clearing landscape can continue.

MR. DEWAAL: Okay. Dave?

MR. OLSEN: I'm not sure I was raising my hand, but I'd be happy to comment. I think there's a big difference between having the DCO itself provide direct clearing to levered customers that are not necessarily direct clearing members in the sense of today, which is making default fund contributions and participating in liquidation drills and things like that, but just being kind of regular way users of the exchange and clearinghouse versus having a wholly owned affiliate that acts as an independent FCM for access into the DCO. And I think that, you know, the potential to solve some of these challenges might lie in the ability to ring-fence, regulate, and ensure that a wholly owned, affiliated FCM that might serve the strategic purposes that the DCOs are trying to put forward would work.

In our conversations with participants that are exploring the direct model, it appears to me to be less motivated by profit opportunity or cost reduction through disintermediation, but when they launch a new product or even a new exchange, you just can't get FCMs to show up. It's very costly when there's no liquidity to take a flyer as an FCM, do all the technical integration, dedicate the education of your sales force, all those things when you don't know if there's going to be any liquidity.

So I think that these are incentives that the DCOs are trying to promulgate new markets, and it's the, well, if no one else will do it, we kind of have to do it ourselves. And thinking about how to solve that entry point problem for new markets and new contracts might alleviate some of the tensions here.

MR. DEWAAL: Graham, any thoughts?

MR. HARPER: I agree with all that. I mean, I think the idea of dual registration, I don't know. I mean, statutory considerations notwithstanding, I'm not sure that's absolutely necessary. I think the replicating of those functions is, though.

MR. DEWAAL: So you would agree with the idea, which we can deal with in the next session, but you agree with the idea of potentially requiring the firms to have an FCM within their organization?

MR. HARPER: No, not necessarily.

MR. DEWAAL: Oh, not necessarily? Okay.

MR. HARPER: No.

MR. DEWAAL: So --

MR. HARPER: But, again, meeting the regulatory --

MR. DEWAAL: -- [inaudible] 100 percent with

Dave.

MR. HARPER: -- obligations is a different question.

MR. DEWAAL: Got you. Okay. Matt?

MR. HARABURDA: Yeah, I think of this largely, you know, in terms of risk. I mean, you have this world where, you know, large, sophisticated customers could become direct clearing members, and you know --

MR. DEWAAL: Pull the mic a little bit closer to you.

MR. HARABURDA: -- and clear for themselves. You know, small retail customers, you know, starting -- you know, trying a new product on a new exchange or something, you know, a fully collateralized model, you know that. But, you know, the reality is, most people live, you know, in the world of where, you know, you're trading multiple exchanges across multiple different asset classes, across multiple different regulatory regimes, and the FCM, you know, provides an extremely important risk management service there, you know, both to its customers, but really to the larger ecosystem.

So if you get more and more, you know, direct, you know, exchanges allowed to, you know, clear their customers directly, whether that's with an FCM or without an FCM or whatever, like I really worry about the risk across, you know, the entire world.

MR. DEWAAL: Is the concern, again, only where there's margin involved, if the DCO was fully collateralized?

MR. HARABURDA: Well, it certainly raises it. I mean, it's --

MR. DEWAAL: Um-hum.

MR. HARABURDA: -- you know, there's a spectrum there.

MR. DEWAAL: Right.

MR. HARABURDA: Yeah.

MR. HUTCHISON: We shouldn't forget David. He's had his card up.

MR. DEWAAL: Okay.

MR. DAVID DOWNEY: My card doesn't work.

MR. DEWAAL: Ah, your card doesn't work. There you go.

MR. DAVID DOWNEY: I don't know David, but he's a very smart dude.

MR. DEWAAL: It goes with the first name.

MR. DAVID DOWNEY: He goes by Dave.

No, being an innovator, it's very frustrating to work with the FCM community because they do look at this from a profits perspective. And there's one question that all of them ask is, how are you going to populate my books and records? And they are hesitant to do that because they don't want to introduce a risk into their current state of books and records. And so innovators must look for alternatives. And in order to have the safety of an exchange or DCO, they must go alone because the FCM community is not prepared to move forward. They're not prepared to move forward without tremendous cost.

These people, these innovators, should not be shunned. They should be embraced. They should have limits upon them so they don't put any systemic risk in the marketplace. If you want them to prove their concept, let them prove their concept, but don't kill them. Don't strangulate them. Let them proceed. But if they want to grow beyond some metric that you'll have to come up with, introduce and encourage the FCM community to provide the necessary protections that we all have come to know with the FCM community.

But that is why they want to go with the disintermediated. There is some cost involved, yeah, but the FCM community provides a great deal of value at a great deal of cost, and that bridge needs to be built to carry that divide.

MR. DEWAAL: Helen, and then I'll get to Alicia. Helen?

MS. GORDON: Thank you. So I guess just picking up on something there around the FCMs being entirely profit motivated, we are obviously a customer-led business and will be led by customer demand. But the primary function that I believe FCMs assess when joining a new market is the risk profile of that FCM, the level of margin, the default waterfall, who are the other market participants, and are we acting in the best interests of our shareholders in terms of joining that market? That is the fundamental decision-making process that would come first.

So I would agree with a lot of the other points that people around the room have made. I think, you know, market structure evolution is a feature of markets, but we have to make sure there isn't a dilution of standards. We obviously have a very in-depth set of rules that can be examined to assess how they could be met by different parties. Are there rules that are no longer necessary, or are there different rules that would need to be introduced?

And I think it's also worth looking on an international perspective. You know, ESMA have come out to say a CCP can't be a member of another CCP. And you've then got a two-year window to address that. And I think the principles for financial market infrastructures, which, again, we assess all of the CCPs that we are members of to see how they stack up against those PFMIs. Do they need to be evolved on an international level to accommodate these different types of structures? And how can those principles be evolved such that the market structure has changed, and therefore, a different set of principles are required to address that?

MR. DEWAAL: [Off mic.]

MS. CRIGHTON: Yeah, look, I think that was really well said, Helen. You know, I think as FCMs we are supportive of innovation, we're supportive of competition, but the seat we sit in, we have to evaluate the markets that we operate and participate in and the clients that we cover. We think about that through whether it's a risk lens, a regulatory lens. You know, how we think about our role in the market and the burdens that are placed on us are quite significant, right? So the apparatus around us is then equally significant to make the number of decisions that we need to make in order to choose which markets and products we support, where we support it, the types of clients we provide that to, right? We have a series of duties that we have an obligation to think about and navigate.

And so the other question I would ask is, if we have created a path where it is just much easier to launch a product or to launch a service without the engagement of an FCM, then what are the standards, and what are the things that we are giving up by allowing that kind of separate laneway? And I think we have to think about, how do these two models intersect, right? There is a reason that we have the burdens and the obligations that we have, and all of those have been codified and are well known and well understood. But what are we giving up and what are the tradeoffs by allowing that laneway?

MR. DEWAAL: Bill?

MR. THUM: I think, you know, the observation I would make, having worked closely with the FCMs over the past 10 years from the buy side, the FCMs really engage with the DCOs in a very productive way. They hold their feet to the fire. They make sure their risk management is sound. You know, why does the buy side embrace clearing? Certainly, it's more expensive than it was in the old days when it was bilateral trading, but it's a much more robust system.

And in addition to the FCMs holding the feet to the fire to the DCOs and vice versa, the FCMs are the ultimate backstop to the risk. So the transition to clearing that, you know, Dodd-Frank envisioned was not simply DCOs. It was a collective assessment of risk, certainly credit risk for the FCMs, market risk from the DCOs, and the backstop from the FCMs and the default fund was a fundamental component of that. And I think that that shouldn't be discounted for the sake of innovation.

MR. DEWAAL: Are there no other mitigants that can substitute somewhat for collateralization, requiring a default fund of some amount? Is there nothing else that satisfies your risk concerns?

MR. THUM: Well, I think to say is there nothing else, you know, certainly I couldn't say no to that, you know, but, you know, this has been a 10-year process of interacting between the FCMs and the DCOs to strike the right balance in terms of risk and the default fund backup. And I'm not sure the dialog is finished yet, but it has gotten better over time through that dialog. So is there a magic way that we could have all that happen without the FCMs? Maybe, but I haven't seen that happen. I've seen the dialog be the thing that produces the best result.

MR. DEWAAL: Okay.

MR. HUTCHISON: We have a few minutes left. I'm going to ask another devil's advocate question. So we have the equity markets, a very big retail equity market. I'm sure most of us around the table hold stocks. The brokerage firms that we use, at least by my experience, are merely order takers, and the transaction occurs and the stocks are in your account. If we trade on margin rather than fully paid for, we've got 50 percent margin with stocks today. So in that model, some margin is used. A lot of people don't use margin. The reasons why they don't use margin are probably varied. One, they don't understand it and don't want to do it; or two, 50 percent margin is pretty high.

But nonetheless, there's a very active retail equity market that doesn't have -- even though there's an intermediary, their broker, the role that they're playing in that model is very different than what we're talking about. And so is there a simple answer to say you can have a non-intermediated model or a lightly intermediated model, but it's a matter of margin? And then all of this risk discussion we're having might become obviated. Clearly, at fully paid for, we've made the view that it is obviated, but if you crank that back to 50 percent, I'm just saying, and there is auto-liquidation that occurs every day in the equity market when people don't have enough money. Is that too simple a counter argument to this? And David has put his hand up.

MR. DAVID DOWNEY: So back in the mid '90s when we started interactive brokers, we deployed an auto-liquidation methodology. We were highly sophisticated participants. We understood access into the marketplaces. We understood our customers. We understood risk. It was our risk, so we spent a lot of time with it. Auto-liquidation is not a solution. It's very, very difficult, and the amount of money that we -- you'll have to ask Thomas how much he's lost -- but it's in the billions of dollars. It is not a solution. And when I was reading --

MR. DEWAAL: And you're referring to Thomas Peterffy.

MR. DAVID DOWNEY: Sorry?

MR. DEWAAL: You said Thomas. I'm not sure most people know who you're -- that's Thomas Peterffy you're referring to.

MR. DAVID DOWNEY: Sorry, Thomas Peterffy. And when I was reading the FTX proposal some years ago and I ran into -- that was the solution for auto-liquidation. I put the document down. I never read it again.

MR. DEWAAL: Matt?

MR. LISLE: So I want to go back to an earlier comment from David.

MR. DEWAAL: Move your mic down a little bit.

MR. LISLE: I want to go back to an earlier comment from David concerning -- you know, he called the FCM model perhaps sick. I don't think we can ignore the statistics that we're seeing in terms of companies leaving the FCM business, lack of profitability, and those kinds of things. And my point is, a lot of that has to be probably from an inefficiency standpoint in terms of how can you make that model more profitable? There are a lot of sort of longstanding, inherent issues with the model, and I think that this hybrid, in my land of unicorns and rainbows, should be explored, if only to try and identify and try and promote a model that could address that illness or sickness in the FCM model.

MR. DEWAAL: Okay. Bill, Demetri, and then we'll try to come up with some consensus. You have opted out. Demetri?

MR. KAROUSOS: Thanks, Gary. So quite

quickly, look, I think we're sympathetic to some of the thoughts that you just articulated, Clark, that -- and I didn't mean to be flippant about the fully collateralized, but it is such a different beast that it obviously takes care of the risk associated in the derivatives business, right? So, of course, that works, right? It's when you start introducing risk. At what level, Clark, you know, I'll leave it, but I appreciate where you're thinking from the equities business.

I just wanted to say, though, that, you know, we haven't been around forever, right? We've been around since 2009 and, you know, at the risk of sounding like, you know, the doctor that doesn't understand the complaints of interns, there is something to be said for having to prove yourself as an exchange looking to launch products and either solving clearing yourself or going out and finding a clearinghouse that's willing to clear your business, and then signing up clearing members who are willing to support your business. That's a separate step as an exchange. There's some real value to that process.

And I not sure that -- if the problem we're trying to solve is exchanges can't launch fast enough because they have to get someone else to support them should be the problem we're trying to solve, and not because I'm anticompetition. I mean, we're taking on some of the biggest competitors in the world, but because there's real value in going through that gauntlet of hurdles.

MR. DEWAAL: Okay. Carol, before we go to consensus, I'm going to think that you don't differentiate some of the customer protections that come from an FCM registration, even where there's full collateralization versus non-full collateralization?

MS. WOODING: Yeah, I mean, I think that's right. There's still customer protection issues. Obviously, as everyone said, the risk is much less if it's fully collateralized. But I think there's other things an FCM does for customer protection that would be missing --

MR. DEWAAL: Got you.

MS. WOODING: -- in the retail market.

MR. DEWAAL: Okay. So I'm not necessarily hearing a lot of consensus here, Clark.

MR. HUTCHISON: No. Well, I think we've achieved some real value. In other words, two years ago, we had quite the roundtable. We then had some events that occurred after that roundtable that were quite something to witness, and we've all seen that and learned from that. We've continued to have new entrants. If you sit in my shoes, these new entrants, to David's point, you know, would like to get started. They would like things to move along. We have our rules and regs. We have lots of people trying to instill in us that there's new ways of thinking about things.

And so this conversation today is a marker on how has the ball moved. Has consensus changed, or is this still a bit of a conundrum? I think we have some hints as to what some solutions might be, but those are hints, not, I think, easy to employ hints, but nonetheless, hints as opposed to no. And the conversation needs to keep going. You know, I didn't expect that we would get consensus here today on here's the path to making a disintermediated, non-intermediated marketplace work and churn out a solution by tomorrow. So the conversation has advanced.

MR. DEWAAL: All right.

MR. HUTCHISON: So in that regard, I'll make the transition. And again, I'm going to thank you. We were actually very much on time, which I'm really enjoying. I think people had warned me that we didn't have enough time to get into these topics completely. But I do think that time constraint has forced people to get to the point. And I appreciate the points that are given, so that's great. and I appreciate you letting me play devil's advocate just to get other ideas on the table.

So in the last module here, it will reflect a little bit of what we just spoke about, but it is about affiliations, conflicts, and vertical integration. And I know that we all know that, today, we have vertical integration. We have exchanges and clearinghouses that are affiliated. They've been that way since kingdom come, and so we don't need to redefine that. But then there's a new idea of putting new pieces of the puzzle into the already existing vertical, and we've hinted at that today about affiliated FCMs, perhaps affiliated market makers.

And I think what we're interested in is, yes, there's conflicts, and maybe people can speak to the conflicts they see. I think we're all pretty cognizant of what some of those might be, but I think also the idea of guardrails. Can we have a vertical model that has guardrails? And do those guardrails obviate the risks and conflicts? And if so, is that helpful to spurring competition and alleviating, I think, the innovator's dilemma when trying to come to the market. So we may tread back to the previous conversation, we may not, but I think that's an important aspect of where we need to go.

So with that, I'll turn it back.

MR. DEWAAL: All right. So our last polling question of the day, by a show of hands, who believes that, with appropriate guardrails, DCMs and DCOs should continue to be authorized to have affiliated other market participants, including FCMs and liquidity providers? So if you think there should be affiliates, raise your hand.

[Show of hands.]

MR. DEWAAL: Who thinks no, no affiliates?

[Show of hands.]

MR. DEWAAL: Most people have no opinion on the subject?

MR. HUTCHISON: So let's just say that again. So we have a room of 25 people, and only two people have raised their hands. There's been one for affiliates and one against affiliates. But does the rest mean it's undecided, or we haven't asked the question accurately enough?

MR. KAROUSOS: Well, you combine DCMs and DCOs --

MR. DEWAAL: Yeah.

MR. KAROUSOS: -- so in many ways, those are two different questions, so --

MR. OLSEN: And affiliate market makers and FCMs. So --

MR. DEWAAL: Didn't use the word market maker, liquidity providers.

MR. OLSEN: Liquidity providers --

MR. DEWAAL: Um-hum.

MR. OLSEN: -- and FCMs that are -- the complexity of the question makes it hard to give a yes or no response.

MR. HUTCHISON: Okay. So, Gary, I'm going to ask you, let's redefine it in baby steps.

MR. DEWAAL: Let's break it down, yeah. So since this is a clearing meeting, should clearinghouses be permitted to have affiliates that are liquidity providers?

[No response.]

MR. DEWAAL: How about exchanges? Should exchanges be allowed to have affiliates that are liquidity providers?

[Show of hands.]

MR. DEWAAL: Yes, okay?

MR. HUTCHISON: People who think, yes, that exchanges should have affiliated clearing providers -- and I'll throw in -- Gary didn't ask it -- with guardrails. We haven't --

MR. DEWAAL: Yeah.

MR. HUTCHISON: -- figured out those yet, so let's throw in guardrails. Should that be allowed? How many think the answer to that is yes?

[Show of hands.]

MR. HUTCHISON: So we have one, two.

MR. DEWAAL: Okay. Oh, I didn't see the second one. Okay. And how about FCMs? Who thinks that clearinghouses should be allowed to have affiliated FCMs?

[Show of hands.]

MR. HUTCHISON: A few, okay.

MR. DEWAAL: Who thinks the answer is no to that?

[Show of hands.]

MR. DEWAAL: Okay. I think we're going --

MR. HUTCHISON: So --

MR. DEWAAL: -- to have some interesting discussion here.

MR. HUTCHISON: Yeah, I'm just going to say this is not what I would have predicted. I'll just put it that way. So this is very interesting to us. So we've got, evidently, a lot of undecideds, or we still haven't asked the right question. So let me just --

MR. DEWAAL: Or people are realizing it's noon and they're hungry and they'd rather have lunch.

MR. HUTCHISON: Yes. So because of our questions in lack of hands, how many people think we still haven't asked the right question?

[No response.]

MR. HUTCHISON: Or is it just that people are undecided, and this is hard, which, believe me, I understand.

MR. DEWAAL: I have a hunch if we start the discussion, we'll find out where people come out.

MR. HUTCHISON: Okay. Go ahead.

MR. DEWAAL: All right. I want to start with you, Tyson.

MR. SLOCUM: Sure. Well, I mean, you know, under the Commodity Exchange Act, you've got DCOs, DCMs, SEFs that, you know, have responsibilities for supervising market participants. So I think that there are inherent financial conflicts by allowing affiliation. And so the question is, can guardrails -- we don't have a whole lot of fleshed out --

MR. DEWAAL: When you say affiliation --

MR. SLOCUM: -- guardrails --

MR. DEWAAL: -- are you even talking about exchanges and clearinghouses?

MR. SLOCUM: Possibly, yeah.

MR. DEWAAL: Okay.

MR. SLOCUM: And then I think you also have to define what affiliation is because this can get tricky sometimes. You've got sometimes very complex or opaque financial structures. I've had a lot of experience over at your sister agency, the Federal Energy Regulatory Commission, where we forced that agency to redefine affiliation because we kept finding examples of where entity -- because FERC had like, the CFTC, a firm standard of 10 percent or more. And I kept delivering to FERC example after example where entities had 1 percent ownership but had folks on the board of directors. And I was like, you know, if you've got someone on the board, you clearly can control that entity. And FERC was like, gosh, you're right. So they've had to establish new protocols.

And, you know, just there are certain private equity structures or other financial arrangements where even entities that claim to be passive in nature can exert influence over management. And so, you know, for other agencies, we have forced them to consider disclosure of limited liability agreements that clearly define what entities have legal authorities under certain situations for that entity that further illuminate who actually controls those entities, more than just the hard 10 percent or more standard.

I think that there are a lot of complexities about what determines affiliation and then some of the inherent financial conflicts of interest that arise with affiliates in these markets.

MR. DEWAAL: Okay. Go to Mr. Downey. Mr.

Downey, thoughts? You were a vehement hand raiser.

MR. DAVID DOWNEY: Do they have access to our application? Does everybody have --

MR. DEWAAL: Yes, it's on the website.

MR. DAVID DOWNEY: So I don't want to bore you, but if you want to see my complete thought process on affiliations with DCMs, DCOs, FCMs, and affiliation market makers, please read my application. When staff put out a proposal on affiliations, Graham did not reply, and I've been asked why because we did apply. On March the 10th, 2022, I submitted an application for this structure, and I have not changed that application since. We were approved. We are running. It works. It does take substantial guardrails.

And to summarize them is a completely different tech stack, completely different access requirements. I built mine on a completely different technology. I built it in the cloud, inconsistent with my affiliates who still are running on servers. I proposed a novel derivative and a novel market mechanism inconsistent with my affiliates' way of looking at the markets. I do not believe that affiliations create common goals and huddle fast. They don't. They produce conflict that needs to be decided over time.

But the allure of these is great. The concept of a DCO as a bricks and mortar and a DCM as a bricks and mortar is not there. ForecastEx resides on a chip. It's a piece of silicon, and all functionality resides on that silicon. Obviously, we duplicate it and replicate it. And the speed efficiencies, the cost efficiencies, it cannot be denied.

Now I choose the FCM model, as I've mentioned. They provide enormous amounts of benefits from a regulatory perspective. That they are affiliate does not mean they're not doing their job. And because I have an affiliate doesn't mean that I am not doing my job. And we have explained it in detail to staff in writing, in our application, in multiple discussions of question and answers exactly how that works. And staff, apparently, after two and a half years, decided they were comfortable with it. And again, I never changed that application. It's still there. It's been out there for three years. You can read it. And that's how you do it.

MR. DEWAAL: Alicia, I think you had some thoughts on this.

MS. CRIGHTON: I think I made a lot of the comments before. You know, I guess the question really for me comes down to, if you have the complete vertical, DCM, DCO, FCM, SRO, there are absolutely conflicts inherent in that model that we need to think about. How do we address it, through a regulatory apparatus? You know, should it be prohibited? Are there sufficient guardrails in a principles-based regulation model that can be implemented to give us comfort that, particularly in times of market stress, that the appropriate risk management decisions for the ecosystem will be made.

So I think there are conflicts, particularly the more that you add in that stack. And I think the question really should be, you know, should it just be prohibited, or are there sufficient guardrails that we can implement, particularly in a principles-based regulation?

MR. DEWAAL: Can you imagine those guardrails?

MS. CRIGHTON: I have some thoughts. I think it really comes down to transparency, capital placement in the waterfall. You know, a lot of the topics that we've touched on today, I think those are some of the thoughts that need to be brought into the dialog. My first stop would be prohibition. Again, I think the power of that stack in today's markets should not be underestimated, and I think we need to think we need to think about it appropriately from a regulatory standpoint.

And so those are only some of the kind of early topics that I would consider. But I think it has to be meaningful amounts of capital. I think it needs to sit in a very different place in terms of the waterfall. The information barriers need to be real. Like there's a lot of considerations that need to go into it and a healthy amount of dialog that needs to support that discussion.

MR. DEWAAL: David?

MR. DAVID DOWNEY: I failed to mention I run a fully collateralized model, and a lot of the fears that you have are mitigated, and I don't need to deal with them.

MR. DEWAAL: You didn't have to put you card on the side. I was going to call on you anyway.

MR. OLSEN: There are examples in the financial system of single entities, let alone affiliates dealing with massive conflicts. You know, we hire FCMs. Our trade information is secret, and we're very sensitive to that. And the firms that clear some of our trades have traders whose mission it is to sniff out valuable information and trade on it.

And we're completely comfortable that Bank of America or J.P. Morgan or anyone with a large trading business attached to all this sensitive information that we're providing them by regulation and by internal policy has the information barriers and consequences for reaching them in place in a way that makes sense.

I think where you get into trouble -- and I think way back historically to something called the GFX Corporation. This was an in-house liquidity-providing entity that the CME had to trade currency futures and spot FX contracts, and they, as far as I could tell, and as was reported in the press, reported up to the same person who oversaw both sets of businesses. I think those kind of conflicts we need to address very specifically and clearly. But I think you can have a conflict management paradigm within the regulatory community that has teeth and can work.

MR. DEWAAL: So appropriate guardrails would solve a lot of the problems. Allison?

MS. LURTON: Yeah, I think just to go a little bit further than that, I do agree -- and we're talking about so many different combinations of entities. I do think guardrails can be effective. We've talked about some of them.

I do think there's one instance where I think the Commission should propose a rulemaking that prohibits common ownership, and that is where a DCO is also registered as an FCM and runs the SRO that is overseeing both its own FCM and the FCM that it competes with. And I think, given the experience we've had working with the SRO and the CFTC and the buy side over the last 10 years on some very specific issues, it's clear that we need regulatory action here. And so that one is one I think we're ripe for a rulemaking where the Commission should come right out and say that is just not an ownership structure that should be permitted.

The rest of them, perhaps there's guardrails that we can assess, and I think we've elaborated on those in the comment letters we've written in response to the FTX proposal, but also in response to the request for information that the Commission let out on conflict, so we detailed those. But I do think on that one -- we did not say in that letter, but I think we can say now, the Commission should propose a rulemaking on the SRO issue.

MR. DEWAAL: I have a hunch the person to your right might agree with you.

MS. LURTON: I hope so.

MS. WOODING: I absolutely do, obviously. And we also raised this in our comment letter. I mean, when you have an exchange that is actually acting as the SRO for its affiliated FCM, you know, there's too many conflicts. One of them absolutely cannot be mitigated, and that is with that exchange acting as the oversight DSRO for their own affiliated FCM, too many conflicts, easy solution, prohibit it.

And there already are other contexts where NFA acts as the DSRO for FCMs that clear an exchange, and we've seen an increase in that with some of these FCMs that have purchased or have FCMs in their family -- I'm sorry, DCMs that have FCMs in their family. They have come to NFA voluntarily and asked us to take over the DSRO responsibilities, which we have, but we really think it needs to be a rule that says if you own an FCM, you can't be their DSRO.

MS. LURTON: And I said DCO, but I meant DCM.

MR. DEWAAL: Okay.

MS. LURTON: Sorry about that.

MR. DEWAAL: And, David, before I get to Stephen, you were concentrating on FCM affiliates. How about liquidity providers? Any different issues with liquidity provider affiliates?

MR. OLSEN: You know, again, the banking model shows that those conflicts exist with the same organization and have been, you know, relatively well managed over the years. I think the difference with liquidity provision versus the FCM question, although at the limit, the most interesting part of running an FCM is when you're liquidating, so --

[Laughter.]

MR. DEWAAL: I never actually thought the word interesting, the way I would --

MR. OLSEN: Yeah.

MR. DEWAAL: -- describe that. It's not fun by any stretch, but you have -- probably the most important role of an FCM is in a crisis when you're liquidating portfolios, so I don't want to neatly separate those two into completely individual buckets. Even though you can mitigate those with appropriate guardrails, liquidity provision, and being a DCM or a DCO, I think the question of, is it in the best public interest to have the appearances of those conflicts or the temptation of those conflicts exist in a financial system that plays such a vital role in the world? My answer to that is no.

MR. DEWAAL: Okay. Stephen?

MR. BERGER: I mean, to pick up on that last point, I think you certainly cannot eliminate the appearance of the conflict of interest, which I think poses questions with respect to confidence in the system. But guardrails sound great in the abstract, but I don't know how you solve, even with all the guardrails you can imagine, like the fundamental motivation that if you're running an exchange and you own a market maker on that exchange, how you don't in some way, shape, or form preference that liquidity provider or market maker. Same thing goes for a clearinghouse. If you're running a clearinghouse and you own one of the clearing members on a clearinghouse, I don't know how, in a default scenario, you just some way, somehow don't preference, you know, the clearing member you own over the others. So open to guardrails that I haven't wrapped my head around, but there just seems to be a fundamental conflict that's hard to resolve.

MR. DEWAAL: Why do I think I turn around and see your card on the side, David?

MR. DAVID DOWNEY: The way you handle the affiliated liquidity providers, you cripple them.

MR. DEWAAL: Explain what you mean by that.

MR. DAVID DOWNEY: You take away their price time priority, so anybody else who can observe their marketplace who really believes the liquidity provider has an advantage can simply write a simple algorithm -- a 10-year-old could write this stuff -- that any time you read the market data and you observe a liquidity provider acting like that, you step in front of them because you now have priority over them. It eliminates the desire for liquidity providers to participate.

MR. DEWAAL: So effectively, an affiliated liquidity provider is always last in the queue?

MR. DAVID DOWNEY: Again, you cripple them.

MR. DEWAAL: Okay. Demetri?

MR. KAROUSOS: Yeah, so, you know, I think it's worth talking about the affiliations that we feel more comfortable with because it might elucidate why we feel more comfortable with them, right? So the exchange DCO, the exchange in clearinghouse affiliation is well trodden, has the fewest conflicts. And the reality is, is because the conflict that does exist already just exists at the DCO itself, which is the conflict between commercial interest and risk interest, right? And so the DCO is managing that, whether the exchange is an affiliate or whether the exchange is a third party. Both are knocking on their door, saying, what are you doing with your risk? And you ask the clearinghouse, saying, listen, you know, we've got to manage this appropriately in order to survive and thrive. So that's why I think that that exchange/clearinghouse combo doesn't pose a lot of issues. So I think it's important to understand the why.

And exchanges in FCMs, I think, you know, this is a little less concerning, again, because it is really just about managing information flows. Here, the key thing is that, you know, the FCMs should not be getting information from the exchange prior to other -- affiliate FCMs should not be getting information prior to other FCMs. That would disadvantage those FCMs for competing for customers and so on. But I think information flows like that are relatively easy to manage, not inherent conflicts in that sense. It's just making sure that those conversations and that data flow is separate.

MR. DEWAAL: But, by the way, on that one, I can imagine a situation where a clearinghouse has an FCM that has gone under, and it has to move positions to another FCM.

MR. KAROUSOS: I'm about to go to that. If I'm on an --

MR. DEWAAL: Got you. Okay.

MR. KAROUSOS: -- exchange, an FCM --

MR. DEWAAL: Okay.

MR. KAROUSOS: -- which is why we're, again, managing information flows. A DCO FCM, you know, for us is probably the trickiest --

MR. DEWAAL: Okay.

MR. KAROUSOS: -- combination. And again, it's because one of the pillars is the two-tiered risk model of the derivatives industry. And so where the DCOs are primarily tasked with commodity risk, market risk, and credit risk of their FCMs, right, of their clearing members. So the real underlying question is, does the DCO, does the clearinghouse manage the credit risk of its affiliate clearing member the same as other clearing members? Or does it, either directly or indirectly, end up subsidizing that risk via the loss-sharing capacity of the other clearing members in the default waterfall? So that's just a really hard conflict to manage. I'm not sure what guardrails you put in place for that, right?

And then to a much smaller extent, but still a real consideration, is look at with an FCM and a clearing member goes down, more often than not, that FCM is part of a larger company. And, you know, for reputational risk or other risk considerations, we've heard from many of our FCMs that our parent companies would come in, right? Like I'm not saying that's how we manage our risk, but it is a real consideration that there's third party capital that can step in and support an FCM if their own capital base is insufficient at any moment in time.

When you combine that FCM with a DCO, you're suddenly removing the potential for that third party capital to come to the rescue because it is, in fact, the same third-party capital or additional capital outside of the considered system that a DCO itself would rely on, right? So once you get beyond skin in the game, there may be other resources that a DCO has to bring to bear. If that's already been used by defaulting FCM --

MR. DEWAAL: Um-hum.

MR. KAROUSOS: -- you're now dipping twice in the same pot, right? So it's a separate consideration, but not an unimportant one.

MR. DEWAAL: Reggie, I'm curious, as you hear this conversation, are you concerned about affiliations among your clearinghouses and exchanges with FCMs, liquidity providers, or whatever?

MR. GRIFFITH: I'm trying to map out all the different potential conflicts here, so my --

MR. DEWAAL: By the way, we even talk about the possibility that they might have custodians for crypto assets as an affiliate, too.

MR. GRIFFITH: I think my oversimplified opinion is I think it's a case-by-case basis, and it's also, there's perfect world, and there's who's there to fill the need of the market.

MR. DEWAAL: You mean unicorns and rainbows?

MR. GRIFFITH: I guess unicorns and rainbows. I mean, I think the stacked model, like Alicia said, is, you know, look, that's the ultimate model. That's the gold standard. But, you know, there may be a point where we need other firms to step up and fill the void, you know?

I think in summary, besides Allison made a comment that made me question my initial opinion, maybe the SRO would be an absolute prohibition if there are other regulators to step up and play that role. But, in general, I think we want to stay away from prohibiting things and move more towards, let's see if they make sense for the business -- I mean, for the industry from a risk-reward standpoint. Let's see if we can put proper guardrails in place to make it happen if it makes sense.

MR. DEWAAL: Okay. Dave?

MR. OLSEN: I think this conversation so far, rightly, has focused on conflicts of risk or the opportunity for nefarious behavior to happen within one institution or complex. What we've touched on a little bit less, which I feel like is important, too, a lot of the market structure in derivatives is naturally monopoly-forming. Liquidity begets liquidity. The more products you bolt on, the more it becomes difficult for new entrants to innovate and get shelf space.

And I think the concerns about, let's say a DCO has an affiliated FCM or is an FCM, would the commercial temptation be there to increase DCO clearing fees just a bit and have your FCM run with no clearing fees and so that you were the only logical point of entry into that clearinghouse over time? That's an exaggerated version, simple model, but those types of commercial behaviors, these are profit-seeking enterprises that often tilt the landscape for their commercial benefit. And I think even with guardrails in place, it may be more difficult to draw a line on that, versus, say, inappropriate use of information or the other things that we've been talking about.

MR. DEWAAL: Again, I had a hunch your card would be on the side. Mr. Downey?

MR. DAVID DOWNEY: I'm going to admit I'm in it for the money.

[Laughter.]

MR. DAVID DOWNEY: But the way I make money, I have contracts that don't resolve until 2036, and that's when I collect my penny. That's my profit motive. But I agree. I'm in it for the money. Read my application. There are reasons why I'm so convinced that I've solved this problem.

MR. DEWAAL: Can you give a high-level explanation?

MR. DAVID DOWNEY: Yeah, you have to encourage conflict between our affiliates. And it's necessary for that to succeed. And then you have to use -- and, again, the real egregious one that everybody can agree on is the potential for a liquidity provider to come in and be scalping money out of the positions, out of the activity. In my market, I have a liquidity provider so it's not blank. The screens aren't blank. He makes 10-up markets in a 50 cent, so he's making a $5 up two-sided market. What do you want to do? It's for purposes of no blank screens.

In my markets, we've been running now only since August 1st, but the liquidity provider is not much of a participant. Ninety-nine percent of our activity is customer to customer. That market maker is not participating at all. He's been disadvantaged. He's not actually -- we have been able without novel derivative and novel market mechanism approved by the regulators in their wisdom and has produced an outrageous result. Ninety-nine percent of our contracts are customer to customer without a liquidity provider. So I think a lot of the fears are theoretical. I have an application that is actually running and producing results that are -- even I am stunned by it.

MR. DEWAAL: J.B., just curious some of your thoughts.

MR. MACKENZIE: I mean, I think you can definitely use guardrails to get around the conflicts. I think the issue for conflicts is the perception more than anything else. And I think even in David's model, the end result of the feeling that his market maker or only one market maker is at conflict, it's impossible to resolve. I think he has good ideas on ways in which to bring guardrails and rules to disadvantage it so that you try to get the participation of customer to customer, but I do think it kind of becomes a bigger concern is how do you get that perception out there, and how do actually end clients understand that? I think just disclosure-based like, hey, it's in a disclosure, it tells you that. I don't know that that does enough. I think sometimes people don't go through the details of all of the disclosures because there's so many of them.

But I do also think an idea of getting to innovation, you have to allow some of these newer exchanges to have the ability to onboard, but they should be at the same level in the requirements that we have as FCMs. So allowing them to onboard, I think, should be allowed. It should have to be at the same level we have to do as an FCM. But if you don't do that, then it's always going to stifle that opportunity to create a net new market.

MR. DEWAAL: Okay, Ann. And Jan Bart next.

MS. BATTLE: Not a lot to add to this, but, I mean, ISDA has been involved in this issue and commented on the CFTC's request for comments. I think stating that guardrails could -- there are inherent conflicts. I think no one's arguing with that. Guardrails, including guardrails that are used in other aspects of the financial markets, informational barriers, transparencies, those can and must be put in place if this were to be considered.

I think the guardrail for the issue that some have mentioned just regarding how you treat affiliated and non-affiliated FCMs, I don't think we have really a good example of a guardrail for that, and so that would be what we would encourage the CFTC to consider if that scenario were to go forward. And then I think once there's more of a discussion on what that guardrail is and what it looks like, and, you know, how that would mitigate the conflict, then, you know, the market and the regulators together can consider this going forward.

MR. DEWAAL: Jan Bart?

MR. DE BOER: Yeah, even the conflicts

between, say, the exchange and the central counterparty are not always that well defined. I think we have seen now two situations in the recent past where, say, markets were going wild in between an exchange and the central counterparty who is calling it a stop and still debated in court, or not calling it a stop, the EU power markets. And if, at that same moment, there is also an FCM in the room who's part of that same family, that's even going to make that whole debate more difficult. And then at that moment those guardrails are probably going to go out of the window anyway.

So it kind of looks like it's a nice way of allowing exchanges to launch more products sooner, but you already are in some sort of a -- yeah, a relationship between, say, quite often, monopolistic kind of exchanges and a group of FCMs, and you're making it even more difficult.

MR. DEWAAL: If you can help us, how are conflicts addressed on the other side of the Atlantic, in Europe?

MR. DE BOER: Well, I think there they, for a while, tried everything to make it all horizontal --

MR. DEWAAL: Um-hum.

MR. DE BOER: -- because that was going to be the solution to this conflict that has failed. But clearly, the whole thought of bringing then also the clearing member in that same group is definitely not on the radar, and clearly, probably because of the power situation and because of the LME, there's a new thinking about, oh, by the way, how is this relationship between an exchange and a central counterparty organized, and who is calling the shots? Who declares a market to be wild? And I'm just thinking that that poor FCM person then sitting in this large group is totally going to be out of scope.

MR. DEWAAL: Um-hum. All right. Matt?

MR. HARABURDA: Yeah, I just wanted to comment further on the commercial aspects. I mean, you know, like what Dave was saying and then what, you know, Matt Lisle was referring to a little bit earlier. You know, the FCM model is stressed. And, you know, for a professional liquidity provider, you know, there's a lack of clearing choices out there. So, you know, I think that is a very real concern, a real, practical concern. You know, conceptually, are we against an exchange or clearinghouse owning an FCM? Not no, but I don't think the commercial aspect should be ignored.

MR. HUTCHISON: Okay. Sean?

MR. SEAN DOWNEY: Sorry. I think I'm going to disappoint everybody because there's an assumption that I'm going to disagree with Dave and Allison and everyone else. But, I mean, generally speaking, to GFX point, I think it wound down in 2018, don't disagree with the position taken there.

From the perspective of an affiliated FCM, the SRO point, totally understood, no issue with that.

And then, finally, I'm going to disappoint everyone by saying I don't know anything about our FCM application because I'm sitting in the clearinghouse, so there's not much I can say from that perspective because of the walls that are in place. But I think, generally speaking, I think the points that have been made previously make a lot of sense.

And then just not to echo Dave again, but the point he made about the financial system does have inherent conflicts in different parts of it, and they are managed, and it's important to manage those appropriately to the extent that they exist. And that's not unique to the CFTC, FCM, DCO. The DCM world is actually applicable much broader and banks and broker dealers and all sorts of areas. So, unfortunately, no fireworks here. I tend to agree with most of the comments that have been made.

MR. DEWAAL: Zach?

MR. DEXTER: I mean, I think there are or have been situations where having an appropriately walled off but affiliated intermediary might help bring some new products online. But, generally, I would say that vertical integration of ownership is not the same as vertical integration of technology and operations, and those things should definitely be separate for all the reasons everyone has enumerated.

MR. DEWAAL: Jan Bart, did you have another comment or you already did it? Okay. Tyson?

MR. SLOCUM: Yeah, just real quick, you know, we've danced around some of the potential guardrails, you know, information barriers, and firewalls. And, you know, there are examples where these internal rules can be effective, but then there are many, many dozens of examples where internal firewalls were immediately breached when a crisis occurs or when there is a ginormous pile of cash sitting there.

And so from the public interest perspective, you know, internally enforced firewalls or information barriers are typically not very inspiring deterrents.

MR. DEWAAL: But if they were inspiring, could you live with them?

MR. SLOCUM: If there was some, you know, direct enforcement by the CFTC or other appropriate agencies on a routine basis, we could become more comfortable. But just relying on, you know, self-disclosures or waiting until the crisis has already happened and then the discovery that the firewalls were breached long ago, again, this is not hypothetical or speculative. This literally happens over and over and over again. So our, you know, satisfaction with those internal walls are just not -- we're just -- we have zero confidence.

MR. DEWAAL: Okay. Anybody else have some thoughts on this before we try to figure out whether we can achieve some consensus? Clark, any thoughts?

MR. HUTCHISON: No, I have, I think, consensus thoughts, but let's see where that goes.

MR. DEWAAL: So I'm getting the sense that the consensus is one, divide the question more accurately among --

MR. HUTCHISON: Right.

MR. DEWAAL: -- the different participants because the answer may be different for different participants. And then the question is, what are the guardrails? What are the guardrails? How are the guardrails enforced? But that's what it sounds like. It sounds like, from what I'm hearing, people are not necessarily fully opposed to guardrails, but they need to be robust and somehow enforced. Is that what I'm hearing?

[Heads nod.]

MR. DEWAAL: No one's objecting, or everybody's being very kind to me.

MR. HUTCHISON: I think that's right. I think we also heard that disclosure isn't the answer.

MR. DEWAAL: Correct. Correct.

MR. HUTCHISON: Okay.

MR. DEWAAL: All right.

MS. LURTON: I think, Gary, one thing I did pick up, too, from the discussion is the appropriateness of considering incentives. We've heard some suggestions that they can be managed that way. And I think if you read our comment letter carefully, we express concern with incentives not being there or discretion allowing for certain things to be outcomes we would not like.

I do think, as we think about the guardrails, at the risk of stating the obvious, thinking about them in a default scenario or a crisis scenario and what incentives that creates is the best way to figure out whether those tools actually manage and function as guardrails. And again, that's a little obvious. On the other hand, it has been an underthought or an undercurrent of today's conversation in my mind.

MR. DEWAAL: Okay. No, I think that's right. Okay. Clark --

MR. HUTCHISON: Okay.

MR. DEWAAL: -- I'll leave it to you for final words.

MR. HUTCHISON: Okay.

MALE SPEAKER: The chairman.

MR. HUTCHISON: Well, Mr. Chairman, do you have any final words? And I'm happy to conclude after that.

CHAIRMAN BEHNAM: Thank you, everyone, very good discussion. I think it is indication of a lot of the issues that we're going through right now.

You all have been a part of that, whether it was the roundtable a few years ago here now. It's not going to be easy to sort of resolve anytime soon, but I think this was -- and again, credit to DCR and Clark for having this discussion today because we have to, I think, collectively, talk about these issues. They're not going to go away, and we really have to think about what the path is going forward.

So thanks again to everyone for your participation, your willingness to share your thoughts, and traveling here. And, Gary, thanks for your moderating. I think you'll have a nice career in academia maybe at the sort of Socratic method being very effective and disliked at the same time.

[Laughter.]

CHAIRMAN BEHNAM: So anyhow, thanks for being a part of it. And, Clark, that's it. Thanks again for everyone for being here.

MR. HUTCHISON: Okay. I, too, will thank you all again. I appreciate the eagerness to come. I appreciate the effort to come. That's not always easy. I appreciate also a little bit of a different kind of roundtable. I know that we compress the time, we put people on the spot, we ask provocative questions, and I appreciate the honesty by which you've given answers.

And it's clear that there's not consensus on a lot of this. I think that's indicative of why we had this. It's hard, and we're progressing down the road as best we can with this hardness to try to do it both logically and fairly.

With that, what I'd like to ask you all is just join me in thanking the AV people and the people who set this up because it's not trivial to get all this set up at the CFTC. So thank you, people behind the black windows, appreciate it.

[Applause.]

MR. HUTCHISON: And lastly, but not least, the woman to my right has been key. It's a nice job that I have to call people up and say, how would you like to do this? And everybody says, yes, and thank you. But Alicia has done all the hard work of organizing all of this, getting all of your disclosures back to us. A little bit of a personal note. Of course, it happens today. Alicia is coming here early in the morning, as I did, and she has a flat tire. And I want to say that the woman in green with her pearls and everything else going to the gas station to pump up her tire in her high heels to get here on time, so, Alicia, thank you for also your hard work.

[Applause.]

MR. HUTCHISON: So with that, safe travels home, appreciate it, and look forward to doing this again sometime. Thank you.

[Whereupon, at 12:42 p.m. EDT, the meeting was adjourned.]