



1901 N. FORT MYER DRIVE • SUITE 500 • ARLINGTON, VA 22209-1604 • 703-351-8000 • FAX 703-351-9160



November 17, 2010

Mr. David A. Stawick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

**RE: RIN 3038 AD01, Proposed Rule 75 FR 63732 - 17 CFR Parts 1, 37, 38, 39, and 40
Requirements for Derivatives Clearing Organizations, Designated Contract Markets, and Swap
Execution Facilities Regarding the Mitigation of Conflicts of Interest**

Dear Mr. Stawick,

The Petroleum Marketers Association of America [PMAA] ⁱ and the New England Fuel Institute [NEFI] ⁱⁱ are pleased to respond to the Commodity Futures Trading Commission's (the "CFTC") and the Securities and Exchange Commission's (the "SEC"; the CFTC and the SEC are referred to collectively as "Commissions") proposed rules limiting conflicts of interest in the ownership, financial interest in and control over derivatives clearing organizations ("DCOs"), designated contract markets, swap execution facilities, clearing agencies that clear security-based swaps ("Clearing Agencies"), security-based swap execution facilities and national securities exchanges that post or make available for trading security-based swaps.

PMAA and NEFI were involved in the activities in the Congress that gave rise to the presentation of the "Lynch Amendment," ⁱⁱⁱ adopted in the U.S. House of Representatives and in the final version of the Dodd-Frank legislation ^{iv} that serves as the legislative underpinning of the proposed rule. What is clear from the actions of the Congress on this issue is that the Congress' foremost desire is to encourage meaningful and transparent competition in the ownership of the financial clearinghouses that are subject to this rule. As Representative Lynch ^v has stated in the U.S. House of Representatives during the Congress' work on the Dodd-Frank legislation and again before the Commissions, "The Office of the Comptroller of the Currency has estimated that upwards of 95 percent of the order flow in the existing over the counter derivatives market is controlled by only five banks." We wish to strongly associate ourselves with the comments provided by Representative Lynch to the Commissions.

While the intent of the proposed rule is admirable, one provision contains a flaw that would not prevent the concentration of ownership of a clearinghouse by dealer banks, nor would it go far enough in reversing the anti-competitive circumstances that exist today and that the Comptroller of the Currency has identified.

Specifically, one of the proposed models of governance contains a provision by which a clearing facility may choose to limit the ownership voting interest of any participant, such as a dealer bank, to no more than 5 percent of the total, with no limitation on aggregate ownership by banks. This is the alternative to a limitation of 20 percent of voting interest by any single institution and 40 percent of voting interest owned collectively by all institutions.

While the 20/40 rule seems to be effective in capping improper ownership interests, the 5 percent limitation would still allow a group of dealer banks to gain control of a clearing facility. A minimum of 11 banks, owning 5 percent each, could attain majority voting ownership and continuing to pose the obstacles to increased clearing that Dodd-Frank is intended to overcome. It is likely that banks will try to exploit such a loophole to continue their cartel-like control of the derivatives market.

We have seen that such concentrated ownership can lead to derivatives transactions not being cleared, meaning increased fees paid to the owner banks and little transparency and competition. The same principle of limited conflicts of interest applies to swap execution facilities, the exchanges that are the heart of the derivatives reform envisioned by Dodd-Frank. But the ownership restriction deals with clearinghouses only, remaining silent on any similar limits on exchange ownership. This loophole, coupled with the 5 percent alternative limit for clearinghouses, endangers the true intent of the Dodd-Frank derivative reforms.

We urge the commission to eliminate the 5 percent alternative, to ensure that banks cannot use it as back door to continue their dominance of clearing facilities, continuing their high profits in an anticompetitive market. We also ask that you consider a rule extending the 20 percent/40 percent ownership limitations to exchanges as well as clearinghouses. Without such steps, we run the danger of seeing banks continue to control and exploit an uncompetitive market. The result would be a lack of transparency and accountability would run counter to the spirit and objectives of Dodd-Frank and prolong the danger of economic crisis in the future.

Congress' concern throughout the work on Dodd-Frank was that, with derivatives trading required to be conducted through clearinghouses, a small handful of large financial institutions would own and/or control the clearinghouses and effectively set rules for their own transactions. The Lynch Amendment specifically provided that these restricted owners, which are defined as swap dealers, security-based swap dealers, major swap participants and major security-based swap participants, cannot own more than a 20 percent voting stake in derivatives-clearing organization, a swap-execution facility, or a board of trade. Further, the rules of the clearing organization, swap-execution facility and board of trade must provide that a majority of the directors cannot be associated with a restricted owner.

While the Lynch Amendment was not in the final legislation, in sections 726 and 765 of the final legislation, state that the CFTC and SEC must adopt rules on conflicts of interest. Specifically, for example, the SEC may include numerical limits on the control of clearing agencies and security-based swap execution facilities. In addition, in a colloquy with Rep. Lynch on the day the House passed the conference bill, Financial Services Chair Barney Frank (D-MA) ***agreed that sections 726 and 765 of the Dodd-Frank Act require the SEC and CFTC to adopt rules eliminating the conflicts of interest arising from the control of clearing and trading facilities by entities such as swap dealers, security-based swap dealers, and major swap and security-based swap participants.*** The Commissions' adoption of strong conflict of interest rules on control and governance of clearing and trading facilities is mandatory.^{vi}

We do recognize that due to the specialized functions of risk analysis that would be required of the board of directors for clearing institutions, it would be appropriate for the directors of these boards to be a compensated position. The success of these boards will be directly related to the technical expertise of the individual members, and as such, would not be the typical makeup that you would see on most public boards of directors.

PMAA and NEFI urge the Commissions to adopt the strongest possible rule, applicable to **all trading facilities**, eliminate the 5 percent alternative which will eliminate conflicts of interest. In this manner, the Commissions would reflect a rejection of the status quo and work toward ensuring open, transparent and competitive markets.

Thank you for your consideration.



Sean Cota
PMAA Chairman-Elect
sean.cota@cotaoil.com
(802) 463-0000



Shane Sweet
President & CEO of NEFI
shane@nefi.com
(617) 924-1000 x211

ⁱ The Petroleum Marketers Association of America (PMAA) is a federation of 47 state and regional trade associations representing approximately 8,000 independent petroleum marketers nationwide.

ⁱⁱ The New England Fuel Institute (NEFI) is a member of PMAA, and an independent trade association representing the home heating industry since 1950. NEFI represents over 1,000 home heating oil and propane retailers and related service companies in New England and throughout the northeastern United States.

ⁱⁱⁱ Section 726(a) of the Dodd-Frank Act specifically empowers the Commission to adopt rules mitigating conflicts of interest with respect to any Derivatives Clearing Organization (“DCO”) that clears Swaps. These rules may include numerical limits on the control of, or the voting rights with respect to, such a DCO by one of several specified market participants. These participants include a Swap dealer, a major Swap participant, and a large bank holding company or non-bank financial company regulated by the Federal Reserve.

^{iv} **Dodd-Frank Wall Street Reform and Consumer Protection Act** (Pub.L. 111-203)

^v Representative Stephen F. Lynch, Member of Congress, [MA-9th CD]

^{vi} Cong. Record, June 30, 2010, H5217