

# Public Statements & Remarks

## Opening Statement of Commissioner Kristin N. Johnson before the Market Risk Advisory Committee

July 10, 2023

### Introduction

Good morning and welcome. Earlier this summer, I had the privilege of delivering a keynote address at the Salzburg Global Finance Forum.<sup>[1]</sup> As I noted in my remarks, it was thirteen years ago that I participated in my first Commodity Futures Trading Commission (CFTC or Commission) convening—a Joint Securities and Exchange Commission (SEC) and CFTC Staff Roundtable<sup>[2]</sup> on clearing of credit default swaps inspired by the Commissions' effort to work in collaboration to implement harmonized regulation anticipated by the Dodd-Frank Wall Street Reform and Consumer Protection Act adopted by Congress in July of 2010. I am hopeful that my opportunity to serve as an expert and my path to service as a Commissioner will inspire young professionals—economists, lawyers, and data analysts, among others—to consider public service or find opportunities to give of their time and talent to enhance regulatory oversight across the financial services sector of our economy.

I am also mindful that many who served as staff or participated as experts including senior professionals, trade association representatives, public interest advocates, and academics during that series of roundtable have continued to advocate for and advance effective regulation for more than a decade and some for several decades over the course of their careers.

During today's Market Risk Advisory Committee (MRAC)—our second meeting in 2023, the third meeting since I assumed sponsorship of the MRAC—the spirit of thoughtful engagement and collaboration that has characterized decades of Commission convenings continues.

At the outset of the meeting, allow me to thank our MRAC Chair and Chairman of the FIA Board, Alicia Crighton; MRAC Designated Federal Officer (DFO) Bruce Fekrat and Alternate DFO Marilee Dahlman. I also thank each of the ADFOs who support MRAC: Lillian Cardona, Daniel O'Connell, Parisa Nouri, and senior counsel on my staff Matt Rowland and Adrien Anderson.

As I have previously noted, the MRAC's productive subcommittees "have historically examined and proposed valuable interventions to the Commission addressing complex regulatory issues."<sup>[3]</sup> At today's meeting, MRAC Subcommittees and experts will share details on Subcommittee workstreams including the initiatives launched by the CCP Risk and Governance Subcommittee on CCP Recovery and Resolution; Margin and Collateral Guidelines; and Technology and Operations. The Market Structure Subcommittee will share updates regarding the Subcommittee's workstreams on block implementation rules, FCM concentration and capacity, U.S. Treasury market reform, and post-trade risk reduction. The Interest Rate Benchmark Reform Subcommittee will share a final report regarding the transition away from LIBOR.

Acknowledging the benefits that emerging technologies may offer, including reduced frictions, settlement timing, and costs as well as increased efficiency and access, an expert panel will examine the conflicts of interest that may arise when firms that employ centralized or decentralized infrastructure integrate diverse operational functions to enable trading in cryptocurrency transactions. This discussion draws on the history, implications, and lessons learned from vertical integration in traditional finance markets. I strongly support the anticipated discussion as well as the recent CFTC Staff Release Requesting Comment on the Impact of Affiliations of Certain CFTC-Regulated Entities.[4]

I applaud the efforts of the leadership and staff of the Divisions of Market Oversight, Clearing and Risk and Market Participants. Just a month prior to this release, on May 30, 2023, I repeated a call for Commission consideration of proposed rules that I began making not long after the onset of the crypto-winter last year.[5] Among other issues, I believe that it is imperative that the Commission understand the nature and implications of these affiliations in both traditional and innovative financial services markets.

This panel will explore both the promise and peril of the current market structures adopted in cryptocurrency or digital asset markets as well as traditional markets. The panel will focus on foundational issues such as custody policies and practices, segregation of customer assets or separation of customer property, and conflicts of interest that may arise as a result of vertical integration.

Finally, in anticipation of the Commission's Second Voluntary Carbon Market Convening scheduled for next week—July 19, 2023,[6] we will hear from experts regarding an update on domestic and international market, operational, and regulatory developments in the market for carbon offsets.

### **CCP Risk and Governance Subcommittee**

Our agenda opens today with a presentation from the Central Counterparty Risk and Governance (CCP Risk and Governance) Subcommittee. One of the most recent successes of the CCP Risk and Governance Subcommittee that I would like to highlight is its recommendations on DCO governance. Our subcommittees gather input from diverse stakeholders on a variety of regulatory and market issues that affect the integrity and competitiveness of U.S. derivatives markets. The Subcommittee produced a discussion paper in February 2021[7] providing several recommendations on DCO governance standards. Last month, the Commission approved a final rule expanding DCO risk management regulations and creating additional opportunities to identify, mitigate, and manage DCO risks. These amendments adopt the MRAC CCP Risk and Governance Subcommittee's recommendations to enhance the Commission's DCO governance standards.[8] This is a great example of the type of efforts that advisory committees, through the workstreams of subcommittees may deliver.

Today, we will hear presentations from our CCP Risk and Governance Subcommittee Co-Chairs Alessandro Cocco, Vice President and the Head of Financial Markets Group at the Federal Reserve Bank of Chicago and Chris Edmonds, Chief Development Officer at the Intercontinental Exchange and Co-Chair Emeritus Alicia Crighton, Chairman of the FIA Board of Directors on the subcommittee's four workstreams: (1) Margin and Collateral Guidelines, (2) Recovery and Resolution, and (3) Technology and Operational Risk.

With respect to the first work stream, we anticipate discussions on a number of topics including model transparency for initial margin, anti-procyclicality, volatility parameter floors, model responsiveness for cleared and non-cleared initial margin models to market shocks, price volatility controls, and access to data for regulators. The subcommittee will evaluate timely questions in this area. Important topics that may be considered with respect to collateral guidelines include discussions on acceptable forms of collateral, liquidity profiles of accepted collateral, and liquidity implications of collateral calls for clearing members, clients, and the broader financial system.

The Recovery and Resolution workstream anticipates considering the Commission's proposed rules referenced in the Notice of Proposed Rule-Making on Recovery and Orderly Wind-Down Plans<sup>[9]</sup> for DCOs as well as public comments examining the rule-making. The Subcommittee will also evaluate and consider EMIR guidance including the EMIR 3.0 proposals.

Finally, the Technology and Operational Risk workstream will continue to examine a discussion started during the March 8, 2023 MRAC meeting exploring the current landscape of operational gaps identified by recent cyber incidents. This workstream will also explore cloud infrastructure vulnerabilities, cloud recovery issues, post-recovery reporting issues, and critical third and fourth-party vendors, among others. This workstream will seek to develop guidelines and consider where added guidance or regulation may be needed to increase resilience.

With sincerest gratitude, I am thankful for the leadership of Co-Chairs Cocco and Edmonds and Co-Chair Emeritus Crighton as well as each of the CCP Risk and Governance Subcommittee members. We look forward to your presentation and recommendations for the agency as we continue to evaluate and improve upon the regulatory framework for central counterparties.

### **Interest Rate Benchmark Subcommittee**

Next, Ann Battle, Senior Counsel, Market Transitions & Head of Benchmark Reform at the International Swaps and Derivatives Association, Inc. (ISDA), who served as co-chair of the Interest Rate Benchmark Reform (IRBR) subcommittee will present the key achievements of the IRBR's multi-year effort to support the transition away from the London Interbank Offered Rate (LIBOR) to risk-free rates, specifically in the United States to the Secured Overnight Financing Rate (SOFR).

Just one week ago, the remaining five USD LIBOR settings ceased to be published on a representative basis. I would like to recognize the significant work in the last few years by the IRBR to build momentum and liquidity for SOFR.

I would like to recognize Chair Behnam for his leadership in establishing the IRBR subcommittee under MRAC in July of 2018. Of course, so much of the IRBR's success was also due to Alicia Lewis, Special Counsel to Chair Behnam, who served as the Designated Federal Officer for IRBR under Chair Behnam's sponsorship.

The success of the IRBR is also due to its leadership and membership. I would like to extend my appreciation to Tom Wipf, former Vice Chairman of Morgan Stanley who was central to guiding the work of the IRBR. In addition to his role with the IRBR, Tom also served as the Chair of the Alternative Reference Rate Committee ("ARRC"), a group of private-market participants convened by the Federal Reserve Board and the Federal Reserve Bank of New York. We also wish Co-Chair Wipf our very best as he transitions from Morgan Stanley where he served for nearly three decades. Similarly, I would like to recognize Co-Chair Ann Battle's work and leadership on the IRBR. I look forward to Co-Chair Battle's presentation today.

Finally, I would like to recognize all the CFTC staff across the Commission and several different divisions who supported the transition. In particular, CFTC staff have issued no-action letters and noticed proposed and final rulemakings to facilitate the market's transition to SOFR.

The multi-year global effort to transition away from LIBOR to SOFR will serve as a case study for successful public-private sector partnership to address an orderly transition away from LIBOR. The result of this exemplary public-private global effort has been an orderly transition from LIBOR. We have witnessed alignment across markets as over-the-counter uncleared and cleared markets as well as exchange-traded derivative contract markets to all transition away from LIBOR.

With my deepest appreciation, I want to recognize all the IRBR members and Commission staff who have contributed to this meaningful work.

### **Market Structure Subcommittee**

Following the IRBR Subcommittee, we will hear a presentation from Co-Chair Biswarup Chatterjee of the Market Structure Subcommittee. As we noted at the last MRAC meeting in March, the Commission has re-established this Subcommittee to fulfill the mission outlined in its charter. We are grateful for our newly appointed co-chairs, Ann Battle and Biswarup Chatterjee, Managing Director and Head of Innovation for the Global Markets Division at Citigroup, who are experts in this area and are very effective in driving the work of the Subcommittee forward.

Today, Co-Chair Chatterjee will address forthcoming Market Structure Subcommittee workstreams including concerns surrounding the block implementation rules set to take effect on December 4, 2023. The block thresholds may impact market participants' ability to efficiently execute large-sized swap transactions. In addition, Co-Chair Chatterjee will also describe the initiation of workstreams examining the concentration and capacity of Futures Commission Merchants (FCMs) in derivatives markets, U.S. Treasury market reform, and post-trade risk reduction.

I would like to express my appreciation to Co-Chairs Battle and Chatterjee as well as each of the Market Structure Subcommittee members.

### **Future of Finance Subcommittee**

From the beginning of my term as a Commissioner and for many years prior to my service, I have encouraged a comprehensive and thoughtful dialogue regarding emerging financial products, technology, and evolving market structures.[10] As a result of the rapid growth in digital asset markets as well as the increasing adoption of innovative technologies, it is imperative for the Commission to continue to foster a public conversation with diverse stakeholders as well as other federal and international regulators to coordinate and collaborate on the adoption of a harmonized set of effective regulations governing these new tools and technologies.

Today, the Future of Finance panel will examine the contours, implications, and consequences of vertical integration and its effect in both traditional financial markets and digital asset markets. Our panel of experts includes Rebecca Rettig, Chief Policy Officer, Polygon Labs; Yesha Yadav, Associate Dean and Robert Belton Director of Diversity, Equity and Community Milton R. Underwood Chair Professor of Law Faculty Co-Director, LL.M. Program, Vanderbilt University Law School; Steven Schwarcz, Stanely A. Star Distinguished Professor of Law, Duke University Law School; Jason Algrante, Chief Legal and Compliance Officer, Fireblocks; and Chen Arad, Chief External Affairs Officer, Solidus Labs.

Reflecting on the history of the vertical integration in the residential mortgage-backed securities markets, panelists will describe the epistemological challenges of defining and deconstructing the term “vertical integration.” In addition, panelists will distinguish the use of vertical integration in traditional financial markets from digital asset or cryptoasset markets and further distinguish between centralized and decentralized financial (or defi) operational infrastructure including as relates to self-custody. The panelists will explore risks and mitigation initiatives as well as recommendations.

A vertical integration model leads to a wide variety of questions and concerns around effective governance, conflicts of interest, lack of transparency, and supervisory responsibilities in traditional and digital asset markets. Customer protection is a foundational and core principle of the CFTC’s regulatory framework. It is important to consider these concerns arising where retail customers may be a significant demographic and there may be a lack of parallel customer protections in intermediated and non-intermediated markets.

As I have previously noted, there is an “increasingly urgent need for the Commission to initiate a formal rulemaking process that invites a comprehensive evaluation of ‘heightened’ risks associated with certain crypto clearing activities to ensure parallel customer protections apply across our markets for similar clearing activities.”[11]

I look forward to the panel’s presentation and to the discussion that their comments will engender.

### **Climate-Related Market Risk Subcommittee**

Finally, anticipating the Commission’s Second Voluntary Carbon Market Convening next week, a panel will explore recent trends in environmental commodity markets, both voluntary and compliance, as well as the jurisdictional challenges that arise in the context of regulating the markets for underlying carbon offsets. Tyson Slocum, Director Public Citizen Energy Program and Peter Malyshev, Partner, Cadwalader, Wickersham & Taft LLP; Adjunct Professor Georgetown University Law Center and George Washington University Law School will present as part of this panel followed by MRAC member discussion.

I am looking forward to both the panel and subsequent discussion.

## Conclusion

This meeting is an opportunity to roll up our sleeves and begin to chart a course for the development and completion of the important work that the MRAC Subcommittees will explore. I am hopeful for an open and meaningful discussion among MRAC members regarding the critical issues facing our markets.

Thank you so much for joining us today.

Before we move into the substance of today's meeting, I want to thank our Chairman and my fellow Commissioners for their participation today and for their service sponsoring the Agricultural, Energy and Environmental, Global, and Technology Advisory Committees. I want to acknowledge the hard work of my fellow Commissioners and the membership of the committees they sponsor which produce knowledge, expertise, and recommendations that are critical to the development of regulations and policies, industry best practices, and compliance and control systems.

We welcome collaboration with our other CFTC advisory committees—AAC, EEMAC, TAC, and GMAC. We will seek out opportunities to connect with the Chair and Commissioners who sponsor these advisory committees and the leadership of relevant subcommittees as we work in tandem on the issues deeply affecting our markets.

With that, I will turn it over to my fellow commissioners who are joining us virtually today for their remarks. I look forward to a robust and informative discussion.

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[1] Commodity Future Trading Commissioner Kristin N. Johnson, *Future-Proofing Financial Markets Regulation*, Salzburg Global Finance Forum (June 29, 2023) <https://www.cftc.gov/PressRoom/SpeechesTestimony/opajohnson4> (<https://www.cftc.gov/PressRoom/SpeechesTestimony/opajohnson4>).

[2] Securities and Exchange Commission and Commodity Futures Trading Commission Joint Roundtable, *Issues Related to Clearing Credit Default Swaps* (Oct. 22, 2010) [https://www.cftc.gov/sites/default/files/idc/groups/public/@swaps/documents/dfssubmission/dfssubmission7\\_102210-transcrip.pdf](https://www.cftc.gov/sites/default/files/idc/groups/public/@swaps/documents/dfssubmission/dfssubmission7_102210-transcrip.pdf) ([https://www.cftc.gov/sites/default/files/idc/groups/public/@swaps/documents/dfssubmission/dfssubmission7\\_102210-transcrip.pdf](https://www.cftc.gov/sites/default/files/idc/groups/public/@swaps/documents/dfssubmission/dfssubmission7_102210-transcrip.pdf)).

[3] Market Risk Advisory Committee Press Release, Commissioner Kristin N. Johnson Announces Agenda for the July 10 Market Risk Advisory Committee (June 16, 2023).

[4] CFTC Staff Releases Request for Comment on the Impact of Affiliations of Certain CFTC-Regulated Entities (June 28, 2023) <https://www.cftc.gov/PressRoom/PressReleases/8734-23> (<https://www.cftc.gov/PressRoom/PressReleases/8734-23>).

[5] Statement of Commissioner Kristin N. Johnson Calling for the CFTC to Initiate A Rulemaking Process for CFTC-Registered DCOs Engaged in Crypto or Digital Asset Clearing Activities (May 30, 2023) <https://www.cftc.gov/PressRoom/SpeechesTestimony/johnsonstatement053023> (<https://www.cftc.gov/PressRoom/SpeechesTestimony/johnsonstatement053023>).

[6] CFTC Announces Second Voluntary Carbon Markets Convening on July 19, 2023, <https://www.cftc.gov/PressRoom/Events/opaeventvoluntarycarbonmarkets071923> (<https://www.cftc.gov/PressRoom/Events/opaeventvoluntarycarbonmarkets071923>) (The purpose of the second convening will be to “recent private sector initiatives for high quality carbon credits; current trends and developments in the cash and derivatives markets for carbon credits; public sector initiatives related to carbon markets; and market participants’ perspectives on how the CFTC can promote integrity for high quality carbon credit derivatives.”)

[7] [https://www.cftc.gov/media/6201/MRAC\\_CCPRGS\\_RCCOG022321/download](https://www.cftc.gov/media/6201/MRAC_CCPRGS_RCCOG022321/download) ([https://www.cftc.gov/media/6201/MRAC\\_CCPRGS\\_RCCOG022321/download](https://www.cftc.gov/media/6201/MRAC_CCPRGS_RCCOG022321/download))

[8] <https://www.cftc.gov/sites/default/files/2022/08/2022-16683a.pdf> (<https://www.cftc.gov/sites/default/files/2022/08/2022-16683a.pdf>)

[9] Commodity Futures Trading Commission, Notice of Proposed Rulemaking on Derivatives Clearing Organizations Recovery and Orderly Wind-Down Plans; Information for Resolution Planning, p. 5-6 (Jun. 7, 2023), available at [https://www.cftc.gov/media/8711/votingdraft060723\\_17CFRPart39b/download](https://www.cftc.gov/media/8711/votingdraft060723_17CFRPart39b/download) ([https://www.cftc.gov/media/8711/votingdraft060723\\_17CFRPart39b/download](https://www.cftc.gov/media/8711/votingdraft060723_17CFRPart39b/download)).

[10] See, e.g., Keynote Address of Commissioner Kristin Johnson at Digital Assets @ Duke Conference, Duke’s Pratt School of Engineering and Duke Financial Economics Center: *Mitigating Crypto-Crises: Applying Lessons Learned in Governance, Risk Management, and Compliance*, Jan. 26, 2023, <https://www.cftc.gov/PressRoom/SpeechesTestimony/opajohnson2> (<https://www.cftc.gov/PressRoom/SpeechesTestimony/opajohnson2>); Keynote Address of Commissioner Kristin Johnson at UC Berkeley Law Crypto Regulation Virtual Conference, *Post Crypto-Crises: Pathways for Protecting Customers and Preserving Market Integrity*, Feb. 8, 2023, <https://www.cftc.gov/PressRoom/SpeechesTestimony/opajohnson3> (<https://www.cftc.gov/PressRoom/SpeechesTestimony/opajohnson3>).

[11] Statement of Commissioner Kristin N. Johnson Calling for the CFTC to Initiate A Rulemaking Process for CFTC-Registered DCOs Engaged in Crypto or Digital Asset Clearing Activities, May 30, 2023, <https://www.cftc.gov/PressRoom/SpeechesTestimony/johnsonstatement053023> (<https://www.cftc.gov/PressRoom/SpeechesTestimony/johnsonstatement053023>).

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