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Via Electronic Submission

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

Re: Request for Comment on the Direct Clearing of Derivatives by Retail Participants

Dear Mr. Kirkpatrick,

De Silva Law Offices submits this comment letter in response to the Commodity Futures Trading Commission staff's Request for Comment on the Direct Clearing of Derivatives by Retail Participants (the "RFC"). We regularly advise market participants on Commodity Exchange Act compliance, CFTC registration and regulatory obligations, and market structure questions involving designated contract markets, derivatives clearing organizations, and futures commission merchants.

The RFC correctly identifies an emerging market structure problem. Retail direct clearing models omit futures commission merchant intermediation and, with it, a set of customer protection, conduct, and risk management functions that the Commission's framework has historically placed on intermediaries. The RFC also correctly notes that the growth in retail direct clearing has been driven in significant part by prediction and other event-type markets, often through binary-outcome contracts cleared on a fully collateralized basis.

That fully collateralized structure is important. It reduces a particular risk category, namely the clearinghouse's counterparty credit exposure to the contract's maximum payout. It does not resolve the broader set of risks that matter most for retail customers, public confidence, and market integrity. Those risks include operational failures, misleading marketing, weak supervision of customer-facing activity, settlement and dispute governance, information asymmetries, and manipulation in thin markets.

This comment letter makes three points that run through our answers to Staff's questions.

First, the Commission should align regulatory duties with economic reality. If an entity is directly onboarding retail, holding retail collateral, setting retail access criteria, and servicing retail, it is performing functions the Commission has traditionally regulated through the FCM layer. Retail customers should receive substantively comparable protection whether access is intermediated or not. The simplest path to consistent outcomes is to require that retail clearing occur through an FCM, affiliated or non-affiliated. Where direct clearing is permitted, the Commission should require functional equivalents for the most consequential FCM protections.

Second, the Commission should protect the broader clearing ecosystem against unexpected risk transfer. The RFC correctly notes that hybrid structures can create paths by which unguaranteed losses associated with retail direct participants could be imposed on other clearing members through mutualized loss arrangements, even if the "product exposure" is fully collateralized. Risk transfer is not limited to price movement. It can arise from operational incidents, settlement disputes, custody events, cyber events, or liquidity stress that triggers extraordinary assessments or draws on shared resources.

Third, the Commission should account for the event-contract context that is driving these models. Retail-facing event contracts are often short-horizon, binary outcome instruments that can function as wagering substitutes for many users. That is not a moral characterization. It is a product-structure observation. When the product behaves that way, the most pressing regulatory questions shift from classic margin spiral concerns to customer conduct, marketing, and integrity controls. The CEA's "special rule" for event contracts, including its reference to "gaming," reinforces that the Commission is expected to make public-interest judgments in this overlap category.

We address the RFC's questions in order.

I. Question 1: Retail direct clearing and the absence of FCM intermediation

A. Question 1(a): Is there a need to ensure that all FCM duties with respect to customer clearing are fulfilled in a Retail DCO model?

Yes, for a core set of FCM duties that have a direct retail-protection or market-integrity function, and particularly for duties that turn on customer-facing solicitation, custody-like handling of funds, and supervision of retail activity. The Commission's framework has long relied on the FCM as the primary locus of retail protection.

It is also important to be precise about what "fully collateralized" does and does not do in this setting. In event-based models described in the RFC, the Retail DCO holds collateral equal to the contract's full value to protect the clearinghouse against the market and credit risk associated with the contract. That design addresses the risk that a participant cannot meet a loss obligation that exceeds posted margin. It does not address a different class of risks that the Commission and other regulators typically treat as retail-protection problems: misuse of funds, inadequate disclosures, operational outages, poor dispute handling, abusive marketing, and weak supervision of customer-facing activity.

The Commission's DCO rules and Core Principles are designed to protect the clearinghouse and the stability of clearing, not to supervise retail distribution in the manner contemplated by the FCM framework. DCO default procedures, for example, are built around the default of a clearing member as a unit, not around supervising large populations of small retail accounts that may behave in correlated ways during market stress or public events.

Accordingly, the Commission should seek equivalent outcomes, not merely formal compliance with Part 39. At minimum, a Retail DCO model that directly onboards retail should be required to ensure functional equivalents for duties that include: (1) customer funds protection and segregation standards; (2) supervision of solicitation and account handling; (3) customer identification and AML; (4) antifraud and fair dealing obligations; and (5) dispute resolution and complaint handling processes that retail customers can realistically access.

In our view, the Commission should not attempt to transform DCOs into retail brokers by grafting the entire Part 1 and Part 166 framework onto Part 39 in one step. That path risks confusion, uneven application, and gaps. The Commission should instead identify a baseline set of retail outcomes that must be met and then determine whether those outcomes are best achieved through required FCM intermediation, through an FCM-equivalent rule set applied to the retail-facing entity, or through a hybrid.

B. Question 1(b): Should direct retail participants be required to become customers of the Retail DCO's affiliated FCM?

The Commission should strongly favor requiring that retail participants clear through an FCM in most cases. We agree with the central point made by Robinhood Derivatives in its comment letter and by the World Federation of Exchanges. FCM regulation is the Commission's most developed and time-tested retail customer protection regime.

Affiliation, however, should not be mandatory. A requirement that retail clear through an affiliated FCM can create a "captive" model that concentrates commercial incentives, customer-facing distribution, and clearing risk decisions within a single corporate group. The RFC itself highlights conflict-of-interest questions that arise in vertically integrated structures, and those conflicts are not theoretical.

The Commission can capture the main benefit of FCM intermediation without forcing a captive structure by requiring retail clearing through an FCM while allowing customers to clear through either an affiliated FCM or one or more non-affiliated FCMs. That approach has three advantages.

First, it preserves the retail protections embedded in the FCM and NFA frameworks.

Second, it promotes competitive discipline on fees, service quality, disclosures, and dispute resolution.

Third, it reduces the risk that a single corporate group's commercial incentives will erode market integrity or retail protections through subtle design choices.

This is also consistent with the WFE's view that conflicts are better addressed through governance, supervision, and transparency requirements than through restrictions on market participation.

C. Question 1(c): Should a Retail DCO that does not have an affiliated FCM be required to establish one?

The Commission should not require every Retail DCO to establish an affiliated FCM. A mandatory affiliate requirement may unintentionally incentivize vertical integration and increase conflicts that the Commission then needs to police.

The Commission should, however, require that retail participants clear through an FCM, either affiliated or non-affiliated, unless a Retail DCO can demonstrate that it has implemented functional equivalents for key FCM protections and is subject to a comparable supervisory regime for customer-facing conduct. In practice, that will be a high bar, and it should be. Retail direct clearing is not simply a different plumbing choice. It changes who owes duties to the retail participant and which regulator's tools apply.

Where a Retail DCO asserts that an FCM layer is too costly for fully collateralized products, the correct policy response is not to accept gaps in protections. The correct response is to require the Retail DCO and its corporate group to bear the cost of delivering comparable outcomes, because the alternative is regulatory arbitrage by structure.

D. Question 1(d): Conflicts of interest and risk transfer in vertically integrated structures

The RFC's conflict questions are well-framed. Retail direct clearing models often arise in corporate groups that may own or control the retail-facing platform, a DCM, a DCO, and potentially an affiliated FCM. The Commission should treat conflicts in these structures as a central risk, not a peripheral compliance issue.

We recommend four categories of mitigants.

First, legal and financial separateness must be real. The Commission should require that each regulated entity be separately capitalized at the legal entity level, with independent governance and clear allocation of liabilities.

Second, information barriers should be documented and tested. The Commission should require robust restrictions on customer-level data sharing and on trading and surveillance information between the affiliated FCM and the DCO or DCM, except as needed for risk management and regulatory compliance.

Third, governance should be designed to insulate risk decisions from commercial pressures. DCO and DCM risk committees that set participation criteria, collateral standards, and emergency procedures should include independent directors or independent committee members. Risk settings should not be subject to override by commercial leadership.

Fourth, the Commission should require transparency and enforceable allocation rules to reduce unanticipated risk transfer between affiliates. This is particularly important for stress events that do not look like classic market risk. In a fully collateralized, binary-outcome market, the stress event may be an operational outage during a major public event, a settlement dispute, a custody incident, or a cyber event. Those scenarios can create losses and liquidity demands that are not captured by "collateral equals max payout."

On the "captive" question, the Commission should be cautious about mandating captive affiliation. The WFE is correct that captivity is not a necessary or proportionate response. A better approach is to require open access for non-affiliated FCMs and to impose strong conflict governance and supervision on affiliated structures.

Retail direct clearing models also raise a distinct information-asymmetry risk that is not solved by full collateralization. *In a vertically integrated structure, the retail-facing platform, an affiliated FCM, or the corporate group's infrastructure entities may have access to nonpublic order and position information about retail participants. Where an affiliated market maker or proprietary trading desk provides liquidity in the same products, the incentive and ability to trade ahead of customers, or otherwise exploit retail flow, becomes a core conflict-of-interest and market integrity concern.*

The Commission should require clear prohibitions on the use of confidential retail order and position data for proprietary trading, robust information barriers with independent testing, and transparent disclosure of any economic arrangements that create incentives to route retail flow to affiliated liquidity providers

II. Question 2: Hybrid models combining direct and intermediated clearing

The RFC notes hybrid models where retail traders can choose direct clearing or intermediated clearing through an FCM. The RFC also recognizes that default management and collateral segregation can differ depending on that choice. That variability is itself a retail-protection concern. A retail customer's protections should not turn on a technical "membership" status that the customer does not understand.

A. Question 2(a): Are additional risk management protections needed to prevent undue risk transfer?

Yes. Hybrid models should be permitted only if the DCO can demonstrate that retail direct clearing activity cannot impose undue risk on intermediated clearing members and their customers, and vice versa. That demonstration should include stress scenarios where losses arise from operational failures, settlement disputes, or cyber incidents rather than from price movement.

The Commission should consider requiring a written "risk allocation framework" for hybrid models that addresses: (1) governance and decision-making authority in a stress event; (2) who funds extraordinary costs; and (3) how retail collateral is protected when the stress event is not a price-driven default.

B. Question 2(b): Is there a need to divide default-related resources or other protections?

Yes. A hybrid DCO should ring-fence default resources by clearing model and, where appropriate, by product class. Retail direct clearing should not be permitted to draw on default resources funded by intermediated clearing members unless those members have explicitly consented and the Commission has assessed the fairness and incentives created by that mutualization.

This is not only about protecting FCM clearing members from subsidizing retail. It is also about preserving confidence in cleared markets. Traditional clearing members will reassess participation if they perceive they are being exposed to retail-driven operational or conduct risks they did not bargain for.

C. Question 2(c): Might certain default events result in unexpected or undue risk transfer?

Yes. The RFC correctly identifies this concern. Risk transfer can occur through shared liquidity facilities, shared operational resources, shared insurance, or corporate group decision-making during stress. It can also occur through bankruptcy dynamics if multiple service lines sit in one legal entity.

The Commission should require clear rulebook provisions that define whether and how losses from retail direct clearing can be imposed on other clearing members, including through assessments. The Commission should also require plain-English disclosures to retail participants describing what happens if the DCO faces an operational crisis or a settlement dispute.

D. Question 2(d): Are there circumstances where hybrid models should not be permitted?

Yes. Hybrid models should not be permitted where ring-fencing is not legally robust or where corporate-group incentives make cross-subsidization likely. The Commission should be particularly cautious where a single corporate group controls product design, retail distribution, clearing parameters, and default management. In that structure, growth incentives can overwhelm risk discipline.

III. Question 3: Multiple product classes within the same legal entity

The RFC describes a model where a single legal entity clears fully collateralized retail direct products and also clears leveraged or margined products in an intermediated model.[11] This structure increases complexity and creates obvious channels for contagion.

A. Question 3(a): Are additional protections needed to prevent undue risk transfer across service lines?

Yes. The Commission should require service-line-by-service-line risk management plans, including separate stress tests, separate operational resilience measures, and separate default management procedures calibrated to the different product types.

It is not enough to say the fully collateralized line is "safe" because payouts are capped. Operational and governance failures can create uncollateralized losses.

B. Question 3(b): Is there a need to divide default-related resources by product type?

Yes. Default resources and financial safeguards should be segregated by product type and clearing model. This includes default funds, assessment powers, liquidity resources, and any shared insurance or guarantees.

The Commission should require a clear demonstration that the fully collateralized retail direct product line cannot impose losses on the leveraged or margined line, and vice versa, except under a disclosed and Commission-reviewed loss-allocation framework.

C. Question 3(c): Might certain default events result in unexpected or undue risk transfer between collateral pools?

Yes. Even in a fully collateralized model, collateral can be exposed to custody risk, investment risk, and operational error. If the same legal entity also clears margined products, stress can create incentives, or legal necessities, to draw across resources. The Commission should require strict limits on cross-use of collateral and should evaluate whether bankruptcy-remote structures or separate legal entities are needed for meaningful protection.

D. Question 3(d): Are there circumstances where this model should not be permitted?

Yes. Where ring-fencing cannot be made legally robust, the Commission should consider requiring separate legal entities for the distinct service lines, or prohibiting retail direct clearing in the same entity that clears leveraged or margined products.

The burden should be on the Retail DCO to demonstrate that risk transfer is not merely unlikely, but structurally constrained.

IV. Question 4: Separate DCO registration sub-category for Retail DCOs

A separate Retail DCO registration sub-category is warranted, or at least a set of enhanced, tailored conditions that apply to Retail DCOs, because the retail direct model introduces distinct retail conduct and market integrity risks that are not central to Part 39's design.

A. Question 4(a): How should a sub-category be tailored?

A Retail DCO sub-category should address three areas.

First, retail conduct and distribution. Retail direct clearing is, in practice, retail onboarding and distribution. It should trigger retail-facing supervision obligations comparable in substance to those imposed on FCMs, including marketing standards, supervision of customer-facing personnel and communications, complaint handling, and accessible dispute mechanisms.

Second, conflicts and vertical integration. Retail DCOs should be subject to explicit governance requirements addressing corporate group conflicts, including independent oversight, information barriers, and transparent governance arrangements.

Third, market conduct and integrity. Retail event markets can be thin and can trade on events susceptible to information asymmetry. These characteristics require enhanced surveillance, clear prohibited practice rules, and reliable escalation pathways for suspected manipulation.

B. Question 4(b): Other factors for a sub-category

The Commission should consider how the sub-category interacts with incentives. If retail direct clearing offers a path to avoid the FCM framework, the market will predictably migrate toward that path. That is not a criticism of innovation. It is a standard regulatory arbitrage dynamic. The sub-category should be designed to eliminate that incentive by requiring equivalent outcomes.

V. Question 5: Reporting requirements

The RFC asks whether Regulation 39.19 reporting is sufficient given the differences between intermediated and direct clearing. We recommend enhanced reporting for Retail DCOs in two respects.

First, the Commission should require reporting that separates direct retail clearing activity from intermediated clearing activity, including concentration metrics, activity levels, and liquidity measures. Retail event products can experience sharp, correlated surges around public events. The Commission should see those dynamics clearly.

Second, reporting should be designed to detect the risks that collateralization does not address. Retail DCOs should report operational incidents, settlement disputes, error rates, and complaint volumes in a standardized way. These are leading indicators of retail harm and market integrity problems.

The Commission should also consider a limited public transparency layer. Retail participants should be able to understand how collateral is held, what happens in a dispute, and how losses are allocated in extraordinary events.

VI. Question 6: Other requirements, including manipulation and the event-contract context

The RFC invites comment on additional requirements relating to retail protection, governance and risk management, market conduct and integrity, and transparency. We recommend three.

First, minimum retail disclosures tailored to binary and event-type products. The RFC notes that these markets often involve binary-outcome contracts. Binary design is simple to explain, but it is easy to market in ways that minimize risk. The Commission should require prominent disclosure that the contract payoff is step-function and that the ability to exit depends on liquidity. Retail customers should be told, in plain language, that "offsetting" is not a guaranteed right. It is a separate trade that requires a counterparty and a market that functions during stress.

Second, manipulation and integrity controls that match the product. Manipulation risk in retail event markets has two forms.

One is microstructure manipulation in thin markets, including wash trading and strategies designed to move a price that the public may interpret as a probability signal. The other is event manipulation or trading on nonpublic information about the underlying event. The Commission should require enhanced surveillance and rules on prohibited trading by persons with direct influence over outcomes, as well as protocols for cooperation with relevant integrity bodies where appropriate.

This is also where the FCM layer matters. Robust KYC, supervision, and surveillance escalation are historically performed at the intermediary level. Retail direct clearing should not be allowed to dilute those capabilities.

Third, product governance in light of the CEA's event contract "special rule." Retail direct clearing has expanded alongside event-type markets. Congress also gave the Commission authority to prohibit certain event contracts, including those involving gaming, if contrary to the public interest. This statutory structure signals that the Commission's work is not purely mechanical. The retail access model chosen by the Commission will shape the real-world scale of gaming-adjacent event trading under federal supervision.

Accordingly, if the Commission permits retail direct clearing for event contracts, it should require clear settlement sources, dispute escalation, and the ability to suspend trading for integrity reasons. Those safeguards are not optional in a retail-facing product that can resemble wagering.

The RFC is asking exactly the right questions. Retail direct clearing can create gaps in customer protection and can introduce new conflict and risk-transfer pathways. The Commission

should strongly favor FCM intermediation as the default mechanism for retail access, whether through affiliated or non-affiliated FCMs, because that framework is comprehensive and well understood. Where retail direct clearing is permitted, the Commission should require functional equivalents of key FCM protections, impose strong governance and conflict mitigants on vertically integrated structures, ring-fence default resources to prevent unexpected mutualization of retail-direct losses, and adopt enhanced reporting and market integrity requirements calibrated to event-type markets.

We appreciate the opportunity to comment and would welcome further dialogue with the Commission and Staff.

Respectfully submitted,

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Sources:

1. Commodity Futures Trading Comm'n, *Request for Comment on the Direct Clearing of Derivatives by Retail Participants* (Dec. 2025).
2. Letter from J.B. Mackenzie, President, Robinhood Derivatives, LLC, to Christopher J. Kirkpatrick, Sec'y, Commodity Futures Trading Comm'n (Jan. 16, 2026).
3. Commodity Futures Trading Comm'n, *Request for Comment on the Direct Clearing of Derivatives by Retail Participants* (Dec. 2025).
4. 7 U.S.C. § 7a-2(c)(5)(C)(i) (2022); 17 C.F.R. § 40.11 (2025).
5. 17 C.F.R. § 39.16 (2025).
6. World Fed'n of Exchanges, *WFE Response to the CFTC's Request for Comment on the Direct Clearing of Derivatives by Retail Participants* (Jan. 19, 2026).
7. Commodity Futures Trading Comm'n, *Request for Comment on the Direct Clearing of Derivatives by Retail Participants* (Dec. 2025).
8. 17 C.F.R. § 39.19 (2025).
9. Commodity Futures Trading Comm'n, *Request for Comment on the Direct Clearing of Derivatives by Retail Participants* (Dec. 2025).

cc. The Hon. Michael Selig, Chairman