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January 17, 2024

Mr. Christopher J. Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission
1155 21st Street NW
Washington DC 20581

Re: RIN 3038–AF24 – Investment of Customer Funds by Futures Commission Merchants and Derivatives Clearing Organizations – 88 Fed. Reg. 81236 (November 21, 2023)

Dear Mr. Kirkpatrick:

The Futures Industry Association[1] ("**FIA**") and CME Group Inc. ("**CME**") (collectively, "**we**") welcome the opportunity to comment on the Commodity Futures Trading Commission's ("**CFTC**" or "**Commission**") notice of proposed rulemaking regarding "Investment of Customer Funds by Futures Commission Merchants and Derivatives Clearing Organizations" (the "**Proposed Regulation**").[2] FIA and CME particularly appreciate the Commission's consideration of their petition (the "**Joint Petition**") in requesting an order under Section 4(c) of the Commodity Exchange Act (the "**Act**") to expand investments ("**Permitted Investments**") that futures commission merchants ("**FCMs**") and derivatives clearing organizations ("**DCOs**") may enter into with Customer Funds (as defined in the Proposed Regulation), as well as the petition from Invesco Capital Management LLC ("**Invesco**" and the "**Invesco Petition**" and together with the Joint Petition, the "**Petitions**") advocating for the addition of U.S. Treasury exchange-traded fund

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[1] FIA is the leading global trade organization for the futures, options, and centrally cleared derivatives markets, with offices in London, Brussels, Singapore, and Washington DC. FIA's mission is to support open, transparent, and competitive markets; protect and enhance the integrity of the financial system; and promote high standards of professional conduct. FIA's membership includes clearing firms, exchanges, clearinghouses, trading firms, and commodities specialists from more than 48 countries, as well as technology vendors, lawyers, and other professionals serving the industry. FIA's core constituency consists of firms that operate as clearing members in global derivatives markets.

[2] 88 Fed. Reg. 81236 (Nov. 21, 2023). The Proposed Regulation would: (i) amend the CFTC regulations governing the types of investments that futures commission merchants and derivatives clearing organizations may make with funds held for the benefit of customers trading and clearing futures, foreign futures, and cleared swaps transactions; (ii) specify market risk capital charges that a futures commission merchant would be required to take on such investments; (iii) adopt conforming amendments to regulations requiring each futures commission merchant to report such investments to the Commission to its designated self-regulatory organization; and (iv) revise the regulations to eliminate the requirement that a depository holding customer funds must provide the Commission with read-only electronic access to such accounts for the futures commission merchant to treat the funds held in the accounts as customer segregated fund accounts.

securities ("**ETFs**") to the list of Permitted Investments.[3] We fully support the Commission's action in response to the Petitions and in adopting the Proposed Regulation. We believe that the Commission's action will fortify and expand the tools available to FCMs and DCOs to manage risks associated with holding Customer Funds; mitigate foreign currency risk entailed by having to convert foreign currencies into U.S. dollars in order to invest in currently permitted, U.S. dollar-denominated investments; and, by providing safe alternative investment options to FCMs and DCOs, enable more diversified portfolios of such investments, with reduced concentration risk.

Before addressing the questions set forth in the Proposed Regulation, we briefly review the background to the Commission's consideration of foreign sovereign debt as a Permitted Investment. The topic has been a focal point of Commission deliberations and action four times in the last 23 years, and we believe that an understanding of this history is critical to a proper evaluation of the Proposed Regulation.

The Proposed Regulation's Recognition of the Specified Foreign Sovereign Debt as a Permissible Investment is Consistent with Prior Commission Action

The Commission initially included foreign sovereign debt as a Permitted Investment in response to a recommendation from the Federal Reserve Bank of Chicago ("**FRBC**"), set forth in a comment letter to a Commission release proposing a variety of new regulatory structures intended to adapt to "the changing needs of the modern marketplace."[4] The FRBC recommended that "CFTC rules permit the investment of customer funds held in a foreign currency in identically-denominated sovereign debt securities."[5] Noting that permitting such investments would mitigate "foreign currency fluctuation risk"[6] to which FCMs and DCOs are subject by having to convert foreign currency to USD-denominated assets before investing such FX balances, the Commission adopted the FRBC's suggestion, subject to two conditions: investments would be (i) permitted only in foreign sovereign debt rated in the highest category by a nationally-recognized statistical rating agency and (ii) limited to the extent of balances owed to customers (for FCMs) or clearing members (for DCOs).

In 2010, the Commission proposed removing foreign sovereign debt as a Permitted Investment entirely, citing "negligible investment" in such instruments by FCMs,[7] and "recent events [namely,

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3 See Proposed Regulation, 88 Fed. Reg. at 81239 (FN 45) (Joint Petition) and 81240 (FN 56) (Invesco Petition).

4 Rules Relating to Intermediaries of Commodity Interest Transactions, 65 Fed. Reg. 77993, 77994 (December 13, 2000) ("**2000 Permitted Investments Amendment**").

5 Id. at 78003.

6 Id.

7 Investment of Customer Funds and Funds Held in an Account for Foreign Futures and Foreign Options Transactions, 75 Fed. Reg. 67642, 67645 (November 3, 2010) ("**2010 Proposing Release**"). The Commission citeed a 2007 "review of the nature and extent of [Permitted Investments]" conducted by the Division of Clearing and Intermediary Oversight (the "**2007 Review**"), indicating that "out of 87 FCM respondents, only three held an

the 2008 financial crisis and its aftermath] undermining confidence in the solvency of a number of foreign countries."[8]

In 2011, the Commission adopted its proposal, thereby eliminating foreign sovereign debt as a Permitted Investment. Citing the "potential volatility" of such investments in the "current economic environment," and the "varying degrees of financial stability of different issuers," the Commission considered and rejected arguments from commenters, including FIA, CME and ISDA,[9] urging the Commission to retain foreign sovereign debt on the list of Permitted Investments.[10] Noting the FRBC's concern with the risks of foreign currency exposure, the Commission stated that "[r]ecent global and regional financial crises" had cast doubt on the proposition that foreign sovereign debt was a "sufficiently safe means for hedging such risk."[11] In addition, the Commission suggested that an FCM could avoid foreign currency risk by "not accepting [FX] collateral that is not accepted at the DCO or foreign board of trade" and by "providing in its customer agreement that the customer will bear any currency exposure." The Commission rejected the argument that foreign sovereign debt promoted diversification of customer funds, reiterating the finding of the 2007 Review that such investment "was minimal" and had not apparently increased since. On that basis as well, the Commission concluded, the elimination of foreign sovereign debt as a Permitted Investment "should not undermine" or "cause a disruption in" foreign sovereign debt markets.[12]

At the same time, the Commission recognized in the 2011 Permitted Investments Amendment that "the safety of sovereign debt issuances of one country may vary greatly from those of another, and that investment in certain sovereign debt might be consistent with the objectives of preserving principal and maintaining liquidity, as required by Regulation 1.25."[13] Accordingly, the Commission stated that it would be

> amenable to considering applications for exemptions with respect to investment in foreign sovereign debt by FCMs or DCOs upon a demonstration that the investment in the sovereign debt of one or more countries is appropriate in light of the

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investment in foreign sovereign debt at any time during that year," and "only one FCM invested in such debt under Regulation 30.7." Id. at FN 28.

8 Id. at 67645.

9 See Joint Comment Letter of FIA and ISDA on 2010 Proposing Release, and Comment Letter of CME Group, dated December 2, 2010.

10 Investment of Customer Funds and Funds Held in an Account for Foreign Futures and Foreign Options Transactions, 76 Fed. Reg. 78776, 78781 (Dec. 19, 2011) ("**2011 Permitted Investments Amendment**").

11 Id.

12 Id. at 78781-82.

13 Id. at 78782.

> objectives of Regulation 1.25 and that the issuance of an exemption satisfies the criteria set forth in Section 4(c) of the Act.[14]

That is, the 2011 Permitted Investments Amendment invites FCMs and DCOs "that seek to invest customer funds in foreign sovereign debt to petition the Commission" and specifically contemplates that the Commission will "consider permitting investments (1) to the extent that the FCM or DCO has balances in segregated accounts owed to its customers (or clearing member FCMs, as the case may be) in that country's currency and (2) to the extent that such sovereign debt serves to preserve principal and maintain liquidity of customer funds as required for all other [Permitted Investments]."[15]

In 2018, the Commission considered precisely such a request from ICE Clear Credit LLC, ICE Clear US, Inc., and ICE Clear Europe Limited (collectively, the "**ICE DCOs**") and in response issued an order pursuant to Section 4(c) of the Act conditionally permitting all DCOs to invest futures customer funds and Cleared Swaps Customer Collateral (as defined in the Proposed Regulation)[16] in the foreign sovereign debt of France and Germany.[17] The Commission issued that order on the basis of a showing that the foreign sovereign debt of France and Germany "has credit, liquidity, and volatility characteristics that are comparable to U.S. Government Securities."[18] In addition, the Commission observed that investing in foreign sovereign debt "poses less risk to customer funds than the current alternative of holding the funds at a commercial bank, on the basis that exposure to high-quality sovereign debt is preferable to facing the credit risk of commercial banks through unsecured bank demand deposit accounts."[19]

Viewed in this context, the Commission's proposal to amend the list of Permitted Investments to include the sovereign debt of Canada, France, Germany, Japan, and the United Kingdom ("**Specified Foreign Sovereign Debt**") is entirely consistent with the "overall objectives of Regulation 1.25 of preserving principal and maintaining liquidity of Customer Funds"[20] as well as

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[14] Id.

[15] Id. See also Proposed Regulation, 88 Fed. Reg. at 81243 (FN 100).

[16] *See* 88 Fed. Reg. at 81237.

[17] The Commission included all DCOs in scope of the exemption in response to a request from CME. FIA recommended including all DCOs and their FCM clearing members in scope of the order. The Commission declined at the time to expand the exemption to FCMs, noting that FCMs "are a separate class of registrants subject to differing regulatory obligations that the Commission would need to carefully consider on their own terms." Order Granting Exemption from Certain Provisions of the Commodity Exchange Act Regarding Investment of Customer Funds and from Certain Related Commission Regulations, 83 Fed. Reg. 35241, 35244 (July 25, 2018) ("**2018 Order**").

[18] Id. at 35242.

[19] Id. See also Proposed Regulation 88 Fed. Reg. at 81244 (FN 113).

[20] Proposed Regulation, 88 Fed. Reg. at 81244.

the Commission's broader responsibilities to protect customer funds and avoid systemic risk and "ensure that its regulations are robust and responsive to our evolving market structure."[21]

Comments on Provisions of the Proposed Regulation Relating to Specified Foreign Sovereign Debt

The Specified Foreign Sovereign Debt Has Comparable Credit, Liquidity and Volatility Characteristics to U.S. Treasuries

The Commission notes that two-year debt instruments in the Specified Foreign Sovereign Debt have credit, liquidity and volatility characteristics that are consistent with two-year U.S. Treasury securities.[22] As evidenced by the data set forth in Appendix 1 to the Joint Petition, we submit that the Commission's observation regarding two-year instruments is generalizable to shorter tenors as well.[23]

The Commission also observes that the Specified Foreign Sovereign Debt instruments may be "less liquid than U.S. government securities."[24] Measured by bid-ask spread (that is, the difference between the lowest ask price and the highest bid price, which is a widely used measure of liquidity), the short-term Specified Foreign Sovereign Debt instruments in scope of the Proposed Regulation all demonstrate abundant market liquidity; they are comparable to, if not identical with, bid-ask spreads in U.S. government securities for the same tenors.[25]

All fixed income markets become more volatile in the face of uncertainties in macroeconomic outlook and the expected path of interest rates, and as a result, markets in Specified Foreign Sovereign Debt as well as in U.S. government securities have seen elevated volatility in the last

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21 Id. at 81287 (Appendix 3—Statement of Commissioner Kristin N. Johnson).

22 Id. at 81258.

23 See Joint Petition, Appendix 1, Support for Rule 1.25 Specified Sovereign Debt Expansion ("**Appendix 1**"). See also FIA's Supplement to Petition for Order under Section 4(c) of the Commodity Exchange Act, September 22, 2023.

24 Proposed Order, 88 Fed. Reg. at 81247.

25 See Appendix 1. Although bid-ask spreads for Japan's sovereign debt have been higher in recent years, the Japanese sovereign debt market remains one of the world's largest at 1,230 trillion yen (USD 8.16 trillion). The recent higher spreads are [an historical outlier] caused by the Bank of Japan's yield-curve control policy. Notably, though, the BOJ's actions in 2023 to implement changes to that policy have resulted in a tightening of bid-ask spreads and a diminishment in yield-curve dislocations – indications of a return to market functioning and liquidity more in line with historical benchmarks. See Liquidity Indicators in the JGB Markets, Financial Markets Department, Bank of Japan (September 28, 2023); see also Foreigners hold more JGBs than Japan banks for first time, Nikkei Asia (November 15, 2023); Masaki Kondo & Yumi Teso, Yen Replaces Bonds in Driving Speculation of a BOJ Policy Change, Bloomberg (August 24, 2023); Junoko Fujita, Explainer: What is happening in Japan's bond market? Reuters (January 16, 2023). In a recent interview with Securities Finance Times, a senior manager at Euroclear noted several "intrinsic qualities" of JGBs "that make them particularly suitable" as collateral, citing Japan's trusted status as a sovereign issuer, and the size and liquidity of the market. See Changing Perceptions in JGBs, March 3, 2023 (available here).

year. Volatility causes spikes in bid-ask spreads and less market depth – which is to say, it erodes liquidity. But generally, where elevated volatility affects Specified Foreign Sovereign Debt liquidity, it does so in ways that are comparable to what is likewise observable in markets for U.S. government securities.[26]

The Specified Foreign Sovereign Debt Complements Risk Management Processes of FCMs and DCOs

Adding Specified Foreign Sovereign Debt to the list of Permitted Investments for FCMs and DCOs augments the capacity of each to manage the risks associated with holding Customer Funds denominated in the applicable foreign currencies. First, as the Commission notes, "holding high-quality foreign sovereign debt may pose less risk to Customer Funds than the credit risk of commercial banks through unsecured bank demand deposit accounts" located outside the U.S. (typically the only alternative available).[27] To be sure, CFTC regulations require the risk management policies and procedures of an FCM and a DCO to include evaluation and diligence processes for assessing any depository of Customer Funds for adequate capitalization, creditworthiness, operational reliability, and access to liquidity. That assessment must also address risks associated with concentration of Customer Funds in any depository or group of depositories, the availability of deposit insurance, and the regulation and supervision of depositories.[28] But even the most meticulous and thorough diligence cannot detect the (often unforeseeable) risk of contagion in financial networks through debt and collateral markets.[29] In the event of a foreign depository's insolvency, claims to uninsured cash balances are at greater risk of being treated as unsecured claims against the depository estate than claims to specific securities held in custody. This is to say that FCMs, DCOs, and customers alike are in a better risk posture when FCMs and DCOs are able to diversify non-USD exposures by leveraging both permitted non-U.S. depositories as well as Permitted Investments in Specified Foreign Sovereign Debt instruments.[30]

The Commission has long recognized that investments of Customer Funds denominated in foreign currencies in foreign sovereign debt enhance the ability of FCMs and DCOs to manage foreign

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[26] See Proposed Regulation, 88 Fed. Reg. at 81244 ("The Commission also analyzed the volatility of the Specified Foreign Sovereign Debt and observed, based on the available data, that the price risk of the relevant foreign sovereign debt is comparable to that of U.S. Treasury securities."); see also Michael Fleming, "How Has Treasury Market Liquidity Evolved in 2023?", Liberty Street Economics, Federal Reserve Bank of New York (October 17, 2023); Market Operations in Fiscal 2022, Financial Markets Department, Bank of Japan (September 2023); Pablo Anaya Longaric et al., Sovereign bond markets and financial stability: examining the risk to absorption capacity Financial Stability Review, European Central Bank (November 2023).

[27] Proposed Regulation, 88 Fed. Reg. at 81244 (FN 113); see also 2018 Order, 83 Fed. Reg. at 35242.

[28] CFTC Regulations 1.11(e)(3)(i); 39.14(c).

[29] Jin-Wook Chang & Grace Chuan, Contagion in Debt and Collateral Markets, Finance and Economics Discussion Series 2023-016, Federal Reserve Board (April 2023).

[30] See ICE Clearing House Application for an Exemptive Order Under Section 4(c) of the Commodity Exchange Act: Investment in Foreign Sovereign Debt Under Regulation 1.25, June 22, 2017, page 7; see also 2018 Order, 83 Fed. Reg. at 32542 (FN 10).

currency fluctuation risk.[31] An FCM that holds non-USD Customer Funds in excess of what it is required, or permitted (due, for example, to DCO concentration limits[32]), to deposit with the DCO may wish to invest such Customer Funds in a Permitted Investment. Currently, any such FCM must first convert such non-USD Customer Fund balances into USD – thus incurring foreign currency risk.[33]

The FCM could, by contract, attempt to mitigate that risk, either by refusing to accept such deposits, or by requiring the customer to assume the FX risk – as the Commission suggested when it eliminated foreign sovereign debt as a Permitted Investment in 2011.[34] The Commission made that suggestion on the basis of a finding (relying on the 2007 Review) that investment by FCMs in foreign sovereign debt was "minimal" – presumably because FCMs at the time were holding comparably "minimal" levels of Customer Funds denominated in foreign currency.[35] Fast-forward to the present: the level of Customer Funds held in the denominations of the Specified Foreign Sovereign Debt has increased significantly since the 2007 Review and the 2011 Permitted Investments Amendment. The Commission takes note of this change in the Proposed Regulation: "FCMs collectively held an aggregate of a U.S. dollar equivalent of $51 billion of Customer Funds denominated in Canadian dollars, ("**CAD**"), euros ("**EUR**"), Japanese yen ("**JPY**"), and British pounds ("**GBP**") on August 15, 2023. The $51 billion represented approximately 10 percent of the total $490 billion of Customer Funds held by FCMs in segregated accounts on August 15, 2023."[36] In short, there is now compelling evidence demonstrating the risk management rationale for expanding the list of Permitted Investments to include Specified Foreign Sovereign Debt.

Notably, the growth in FX-denominated Customer Funds derives primarily from growth in the cleared swaps customer business, which was still in its infancy in 2011. Cleared swaps customers deposit initial margin in foreign currency to a much greater extent than do futures or foreign futures customers.[37] It would be impractical – and unfair to cleared swap customers – to continue

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[31] Proposed Regulation at 88 Fed. Reg. at 81244 (FN 114); see also 2000 Permitted Investments Amendment at 65 Fed. Reg. at 78003; 2011 Permitted Investments Amendment, 76 Fed. Reg. at 78780.

[32] For example, the CME imposes a $250 million USD-equivalent limit across any group of clearing member and its affiliates for meeting requirements in a currency different from the contract currency (although clearing members may, on request, deposit additional CAD, EUR, GBP, and JPY cash up to a $500 million USD-equivalent FX cash mismatch limit). See Summary of Acceptable Collateral, CME Group website (available here: https://www.cmegroup.com/clearing/financial-and-collateral-management/summary-of-collateral.html) (accessed 24 November 2023).

[33] Proposed Regulation, 88 Fed. Reg. at 81267.

[34] 2011 Permitted Investment Amendment, 76 Fed. Reg. at 78781.

[35] Id.; see also 2010 Proposing Release, 75 Fed. Reg. at 67645.

[36] See Proposed Regulation, 88 Fed. Reg at 81243-44. The data is sourced from the Segregation Investment Detail Reports filed by FCMs as of August 15, 2023. Id. at 81244 (FN 118).

[37] A survey of FIA members conducted in preparing this comment letter shows that the growth of CAD/EUR/GBP/JPY customer balances (measured by the total equity value of accounts holding cash, securities, and positions denominated in those currencies, expressed on a USD-equivalent basis) between 11/30/2018 and 11/30/2023

incentivizing FCMs to refuse margin deposits not denominated in USD (to the extent that such deposits cannot be transferred to DCOs) or to require customers depositing such balances to assume the foreign currency risk.

The growth in non-USD Customer Fund balances has corresponded with rising customer demand for FCM flexibility in servicing multi-currency accounts. Many customers, particularly customers that clear swaps, seek non-USD single-currency margining services from their FCMs – meaning that they deposit non-USD cash and rely on FCMs to manage those deposits to satisfy margin calls on their behalf denominated in one or more other currencies. Since several of the DCOs that clear swaps are located in the United Kingdom and the European Union, the complexity of single-currency margining processes are compounded by the complexity of LSOC residual interest processes (that is, the need to source non-USD residual interest amounts to cover LSOC deficits in advance of settlement with DCOs outside of U.S. banking hours or on U.S. bank holidays).[38]

Single-currency margining and LSOC compliance processes make for higher levels of operational risk; having the ability to convert non-cash balances into Specified Foreign Sovereign Debt will help FCMs control that risk by giving them risk management optionality that they do not have today (e.g., using Specified Foreign Sovereign Debt instruments held in FCM proprietary accounts to cover LSOC deficits incurred outside of U.S. banking hours).[39]

The Proposed Conditions on Permitted Investments in Specified Foreign Sovereign Debt Help to Ensure their Safety for FCMs, DCOs and Customers

The Commission proposes to permit investment by FCMs and DCOs in Specified Foreign Sovereign Debt subject to conditions consistent with the criteria specified in the 2011 Permitted Investments Amendment and the 2018 Order[40]:

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has been most pronounced for the customer cleared swaps origin. For the members surveyed, CAD/EUR/GBP/JPY cleared swap customer balances totaled USD 1.6 billion in 2018 and USD 9.8 billion in 2023 – a six-fold increase.

38 "LSOC" is the abbreviation for "legal segregation with operational commingling" – coined by the Commission in its proposal to adopt Part 22 of the CFTC Regulations. See also Notice of Proposed Rulemaking on the Protection of Cleared Swaps Customer Contracts and Collateral; Conforming Amendments to the Commodity Broker Bankruptcy Provisions, 76 Fed. Reg. 33818, 33822 (June 9, 2011); CFTC Regulation 22.2(f)(4) (providing that an FCM "must, at all times, maintain in segregation … an amount equal to the sum of any credit balances that the Cleared Swaps Customers of the [FCM] have in their accounts. This balance may not be reduced by any debit balances that the Cleared Swaps Customers of the [FCM] have in their accounts"). The operational complexity of cleared swap LSOC processes are summarized by the Joint Audit Committee's Regulatory Alert 12-03 (October 18, 2012).

39 See CFTC Regulation 22.2(e)(3)(i) (permitting FCMs to satisfy residual interest obligations by depositing Permitted Investments in the cleared swaps customer account; see also CFTC Regulation 1.23(a)(1) (same rule for segregated futures account); CFTC Regulation 30.7(g)(1) (same rule for the secured amount account).

40 Proposed Regulation at 81243.

- investments would be permitted only to the extent of balances owed to customers (or clearing members, as applicable) denominated in the applicable currency, and provided that the two-year credit default spread of the issuing sovereign is 45 BPS or less;[41]

- if the credit default spread of a subject country exceeds the 45 BPS cap, new investments (both direct and by repurchase transactions) would be prohibited;[42]

- The dollar-weighted average time-to-maturity of investment portfolios in Specified Foreign Sovereign Debt[43] must not exceed 60 calendar days;

- Direct investments in a Specified Foreign Sovereign Debt instrument must not have a remaining maturity greater than 180 calendar days;

- The list of counterparties to permitted repurchase transactions involving Specified Foreign Sovereign Debt would be expanded to include foreign banks qualifying as a depository under CFTC Regulation 1.49(d)(3)[44] and located in a money center country (or in another jurisdiction that has adopted the currency of the permitted sovereign debt);[45]

- Similarly, the list of permitted depositories for Specified Foreign Sovereign Debt instruments transferred to an FCM or DCO under a reverse repurchase agreement would be expanded to include foreign banks qualifying as permitted depositories under CFTC Regulation 1.49.

We believe that, as a general matter, the proposed conditions are appropriately tailored to the proposed inclusion of Specified Foreign Sovereign Debt instruments as Permitted Investments, and to the overall objectives of Regulation 1.25 that such Permitted Investments preserve principal and maintain liquidity of Customer Funds. We offer the following specific comments in response to the Commission's questions regarding the proposed conditions.

- As noted in the Joint Petition, we continue to believe that a dollar-weighted average of the time-to-maturity of six months would better promote liquidity than the proposed 60 days.[46] A dollar-weighted average of the time-to-maturity of six months, computed on a currency-

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41 Id. at 81244-45.

42 Id. at 81245.

43 As computed under Rule 2a-7 under the Investment Company Act of 1940, on a country-by-country basis; securities acquired under reverse repurchase transactions or sold under repurchase transactions would count toward this WAM computation.

44 A bank or trust company located outside the United States must have in excess of USD 1 billion in regulatory capital to qualify under CFTC Regulation 1.49(d)(3)(i).

45 Proposed Regulation, 88 Fed. Reg. at 81246-47. "Money center country" means Canada, France, Italy, Germany, Japan, and the United Kingdom. CFTC Regulation 1.49(a)(1).

46 Joint Petition at page 5.

by-currency basis, would make optimally liquid markets available to FCMs and DCOs. Likewise, we ask that the final rule provide that a DCO or FCM may make direct investments in Specified Foreign Sovereign Debt with a remaining maturity up to two years, thereby, again, assuring optimally liquid markets for such investments.[47] While we agree with the Commission's observation that the time-to-maturity requirements as set forth in the Proposed Rule are "adequate to satisfy the demand for investment of Customer Funds in the relevant instruments,"[48] we also believe that those requirements may be safely expanded, thereby enhancing liquidity (with the attendant additional benefit of enhanced price stability and diversification across currencies and tenors), without increasing credit risk.

- The Proposed Regulation does not indicate whether the calculation of the 45 BPS credit default spread condition on the eligibility of Specified Foreign Sovereign Debt should be based on the bid, offer or mid-level. We propose that the basis point spread be determined using the mid-level.[49] Mid-level pricing is a widely accepted pricing convention for a wide range of asset classes including sovereign debt (as the Commission recognized in requiring swap dealers to disclose the mid-market mark to counterparties when disclosing the price of a swap).[50]

- We agree with the Commission that, where the two-year credit default spread on Specified Foreign Sovereign Debt exceeds 45 BPS, FCMs and DCOs should not be required to immediately divest current investments. Since proposing the condition in 2017, the Commission has recognized the "risks associated with selling assets into a potentially volatile market."[51] Moreover, we do not believe that a "cooling-off" period is necessary before Specified Foreign Sovereign Debt may be used again after breaching the 45 BPS threshold. The Commission's historical analysis[52] shows that exceedances of that threshold by issuers of Specified Foreign Sovereign Debt have been relatively rare, and

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[47] Id. at pages 5-6. We note that a two-year remaining maturity standard is consistent with CFTC Regulation 1.25(b)(4).

[48] 88 Fed. Reg. at 81246 at FN 140.

[49] See Joint Petition at FN 19.

[50] See Business Conduct Standards for Swap Dealers and Major Swap Participants With Counterparties, 77 Fed. Reg. 9734, 9765 (February 17, 2012) (noting that that "information about the spread between the quote and mid-market mark is relevant to disclosures regarding material incentives and provides the counterparty with pricing information that facilitates negotiations and balances historical information asymmetry regarding swap pricing").

[51] Proposed Order and Request for Comment on Application for Exemption From Certain Provisions of the Commodity Exchange Act Regarding Investment of Customer Funds and From Certain Related Commission Regulations, 82 Fed. Reg. 59586, 59589 (December 15, 2017); see also 2018 Order, 83 Fed. Reg. at 35243; Proposed Regulation, 88 Fed. Reg. at 81245.

[52] Proposed Regulation, 88 Fed. Reg. at 81245.

where they have occurred the causes may be traced to broader market volatility conditions, the melioration of which itself constitutes such a "cooling-off" period.

Comments on Other Provisions of the Proposed Regulation[53]

Clarification of the Scope of Permitted Exchange-Traded Funds

We welcome the Commission's proposal to include interests in certain exchange-traded funds as Permitted Investments. We urge the Commission, however, to simplify and clarify the concept of "Qualified ETF" (as discussed in the Preamble and substantively reflected in the Proposed Rule text). Such simplification and clarification will better align the proposed conditions on the eligibility of Qualified ETF with (i) the definition of "government money market fund" (drawn from Rule 2a-7, as defined below), (ii) the Securities and Exchange Commission's ("**SEC**") proposed guidance on capital charges applicable to investments in U.S. Treasury ETFs, and (iii) market practice among the managers of eligible MMFs and ETFs.[54]

Specifically, we believe that the proposed condition on holdings of a Qualified ETF is unduly restrictive. The Commission proposes that holdings of a Qualified ETF be limited to "short-term U.S. Treasury securities that are bonds, notes, and bills with a remaining maturity of 12 months or less, issued by, or unconditionally guaranteed as to the timely payment of principal and interest by, the U.S. Department of the Treasury"[55] – to the exclusion, apparently, of short-term securities issued by U.S. government agencies that are guaranteed as to principal and interest by the U.S. government. The prospectus for a leading short-term U.S. Treasury index fund makes clear that securities issued by the U.S. Treasury and securities issued by U.S. government agencies are eligible fund instruments, so long as they "are backed by the full faith and credit of the U.S. government."[56]

To that end, we propose that an ETF that qualifies as a Permitted Investment (i.e., a Qualified ETF) should instead be subject to the following requirements:

i. an open-ended management company registered with the SEC under the Investment Company Act of 1940, as amended ("1940 Act") that holds itself out to investors as an exchange-traded fund in accordance with Rule 6c-11 under the 1940 Act and that issues securities redeemable at net asset value on a delivery versus payment basis[57]; and

[53] Except as provided herein, we support and have no additional comment on the Commission's proposals as set forth in the Proposed Regulation.

[54] Proposed Regulation, 88 Fed. Reg. at 81260 n. 262.

[55] Id. at 81249.

[56] Prospectus Supplement dated June 20, 2023, Vanguard Short-Term Treasury Index Fund at 45.

[57] This condition aligns with proposed regulations 1.25(c)(1) and 1.25(c)(8)(i).

ii. which invests at least 80 percent of its total assets in securities with a maximum remaining maturity of 12 months or less issued or guaranteed by the U.S. Treasury (where the payment of principal and interest is backed by the full faith and credit of the U.S. government) ("short-term securities"), including short-term securities issued by U.S. government agencies that are backed by the full faith and credit of the U.S. government, as well as government money market funds as defined in Rule 2a-7, and/or repurchase and reverse repurchase agreements with a remaining term to final maturity of 12 months or less collateralized by U.S. Treasury securities or other government securities (as defined under Rule 2a-7 and section 2(a)(16) of the 1940 Act) with a remaining term to final maturity of 12 months or less.[58]

The foregoing revision would amend the composition requirement (by including short-term securities both issued and guaranteed by the U.S. Treasury, and by revising the percentage of total assets threshold), remove the authorized participant requirement (as further discussed herein), and remove the condition that DCOs accept the interest in the Qualified ETF as performance bond. With respect to the percentage of total assets standard, the revised formulation would retain the benefits and protections noted by the Commission, while providing ETFs with flexibility to manage their portfolios in times of stress without introducing undue risk. Indeed, we believe that these conditions on eligibility are more conducive to management of portfolio risk by giving managers greater flexibility to rotate out of securities into cash during periods of stress and volatility. Further, we note that the 80% requirement, as distinct from a 95% requirement, aligns with current industry practice, as reflected in industry-standard prospectus terms for short-term Treasury ETFs.[59] By codifying a 95% requirement, the Commission risks creating optionality for FCMs and DCOs that will be impracticable to implement. FCMs and DCOs rely on the composition thresholds stated in funds' prospectus terms to diligence investments, and there may not be industry-wide amendments to prospectus terms in response to the final version of the Proposed Regulation.

Further, we do not support the requirement that the interests be redeemable in cash only. Limiting redemptions to cash could cause unintended impacts. Specifically, there may be instances in which it would be more advantageous to receive a vertical allocation of the underlying securities than cash as the U.S. Treasuries themselves are highly liquid. We also believe that limiting FCMs and DCOs to cash redemptions could potentially cause an inequitable first-mover advantage;

[58] This condition (ii) is intended to amend proposed Regulations 1.25(c)(8)(ii) and (iii). See Letter from Michael A. Macchiaroli, Associate Director, Division of Trading and Markets, to Kris Dailey, Vice President, Risk Oversight & Operational Regulation, Financial Industry Regulatory Authority ("FINRA"), dated June 2, 2022, cited in the Proposed Regulation, 88 Fed. Reg. at 81260 (FN 262). Alternatively, we would propose the following formulation for condition (ii): "at least 95 percent of its assets in cash and "government securities" that are "eligible securities," each as defined in paragraph (a) of Rule 2a-7 under the 1940 Act ("Rule 2a-7"), with a maximum remaining maturity of 12 months or less."

[59] See., e.g., the short-term U.S. Treasury ETFs acceptable at CME, all of which point to a standard of 80% of total assets being invested in securities comprising the index (available here).

liquidation of a significant portion of the fund to meet a redemption could cause a drop in the value of the underlying assets and in turn of the shares of the fund.

Regarding the proposed requirement that the interests in U.S. Treasury ETFs be acceptable as performance bond by a DCO, we appreciate the Commission's position that CME's acceptance of U.S. Treasury ETFs represents an important consideration.[60] However, we would caution the Commission against codifying this requirement. CME is currently the only DCO that accepts U.S. Treasury ETFs as collateral and should it choose for any reason to modify or cease its acceptance of such ETFs, it would be disruptive for FCMs. Further, as the Commission is aware, there is a separate standard governing collateral acceptability at DCOs.[61] The Commission should not conflate these distinct requirements and standards; a DCO may reasonably use different criteria for determining collateral acceptability than those established for Qualified ETFs in the Proposed Regulation.

FCMs Should be Permitted to Purchase and Redeem Qualified ETF Shares Through Agency Transactions

The Proposed Regulation requires an FCM or DCO that invests customer funds in the shares of a Qualified ETF to be an authorized participant.[62] The Commission cites three concerns with agency transactions. First, such investments may require taking customer funds out of segregated custody in order to settle purchases.[63] Second, transfers of customer funds to an authorized affiliate "may be in contravention of Commission regulations that provide that Customer Funds may only be deposited with a bank or trust company, a DCO, or another FCM."[64] Finally, where an FCM or DCO "uses an unaffiliated authorized participant to redeem its Qualified ETF shares, the redemption of the ETF shares may be protracted, preventing the redemption and liquidation of the shares to occur within one business day, as required by Regulation 1.25."[65]

We agree unreservedly that these are critical concerns, and if they could not be convincingly addressed, the Commission's proposed prohibition of agency transactions in Qualified ETF shares would be well-founded. We note that these concerns appear to stem, in part, from a perception that delivery-versus-payment ("**DVP**") settlement is generally unavailable for agency transactions

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60 Proposed Regulation at 81249.

61 See CFTC Regulation 39.13(g)(10) (DCOs must limit the assets they accept as initial margin to those that have minimal credit, market, and liquidity risk); CFTC Regulation 39.33 (DCOs financial resources may include highly marketable collateral, including high quality, liquid, general obligations of a sovereign nation so long as these assets are readily available and convertible into cash pursuant to prearranged and highly reliable funding arrangements under extreme but plausible market conditions).

62 Proposed Regulation at 81251. See proposed paragraph (c)(8)(i) of Regulation 1.25.

63 Id.

64 Id. at 81252.

65 Id.

in Qualified ETF shares.[66] In fact, as set forth in more detail in the Invesco comment letter on the Proposed Regulation, FCMs and DCOs may transact with authorized participants in Qualified ETFs on a DVP basis. Accordingly, in lieu of a prohibition on agency transactions, we recommend that the Commission subject such transactions to the condition that agency purchase/redemption/transfer transactions in Qualified ETFs be settled on a DVP basis. So amended, we believe that the proposed prohibition may be reformulated as a condition that will not unfairly discriminate against FCMs that are not authorized participants.

Addressing the Commission's concerns in turn:

- As noted, we believe that there is functionality available to investors that are not authorized participants to settle purchase/redemption/transfer transactions in Qualified ETFs on a DVP basis.[67] An FCM or DCO that is not an authorized participant would, of course, have first to confirm that such DVP settlement was available before initiating a secondary market transaction; but having done so, it should be permitted to execute that transaction, on the same terms and subject to the same requirements as an FCM or DCO that is an authorized participant. To the extent that a transaction could not be settled DVP, it would not be eligible under Regulation 1.25.

- We respectfully disagree that settling an agency transaction in Qualified ETF shares entails the establishment of a depository relationship with the ETF's authorized participant. Indeed, if that were the case then FCMs that are themselves authorized participants would not be able to settle such primary market transactions in compliance with the CFTC's regulatory requirements. The authorized participant account for such FCMs will be maintained on its books and records in its capacity as a registered broker-dealer – which is not a permitted depository account location under CFTC Regulations 1.20(b), 22.2(b), or 30.7(b).

- As a threshold matter, we believe that given the highly liquid nature of the underlying assets of a Qualified ETF, delayed redemption arising from liquidity risk is unlikely. And, as further discussed below,[68] the tail risk of a delayed redemption would constitute a risk event for which an FCM or DCO has the obligation already to take remedial measures.

[66] Id. at 81251.

[67] DVP settlement entails cash and shares being exchanged at the same time. The Commission conditioned Permitted Investments in the form of repo and reverse repo transactions on transfer of securities to a customer segregated custodial account being made on a DVP basis in immediately available funds. See Regulation 1.25(d)(9). Thus, there should be no issue with under-funding in the customer segregated account where DVP settlement of is available.

[68] See below at FNs 74-76. The FCM or DCO might, for example, be required to carry the Qualified ETF shares at a higher haircut pending resolution of the delay and be obliged to increase levels of residual interest to cover any resulting deficit in the affected segregated origin.

The Commission states that FCMs and DCOs are likely to purchase and redeem shares of a Qualified ETF through primary market transactions intermediated by authorized participants rather than purchasing and selling the ETF shares in the secondary market.[69] The rationale for this view is that the price of the shares in the secondary market may differ from the ETF's share price (as determined by the fund's net asset value), and the sale of the shares in the secondary market may delay the liquidation of the instruments.[70] However, we note that there has in fact been substantial growth in the U.S. Treasury ETF secondary market as measured by shares traded daily. Additionally, it is reasonable to expect that a substantial number of shares of a fund could be liquidated in the secondary market with minimal impact on price due to market conventions such as primary market versus secondary market arbitrages. Finally, as noted, from a timing perspective secondary market trading would allow FCMs and DCOs to liquidate shares on a DVP basis. While standard secondary market ETF settlement is currently T+2, short settlement is available on a T+1 basis, which aligns with a T+1 primary market settlement requirement, as well as the standard settlement for the purchase and sale of U.S. Treasuries.

Accordingly, we believe the concerns raised by the Commission may be effectively mitigated and controlled by conditioning agency transactions on the requirement that purchases and redemptions settle DVP, as well as on risk mitigation that the Commission's regulations already require FCMs and DCOs to plan for and implement as needed. On that basis, an outright prohibition of agency transactions to purchase or redeem Qualified ETF shares unfairly burdens and discriminates against FCMs that are not authorized participants. We urge the Commission to take a more flexible approach in the final rule that can serve all FCMs' collateral management needs.

Clarification of the Acknowledgment Letter Requirement Relating to Permitted Investments in Qualified ETFs

The Commission notes in connection with Permitted Investments in Qualified ETFs that FCMs and DCOs "would be required to obtain the acknowledgment letter required by Regulation 1.26 from an entity that has substantial control over the ETF interests purchased with Customer Funds and that has the knowledge and authority to facilitate redemption and payment or transfer of the Customer Funds. Such entity may be the sponsor of the Qualified ETF or a depository acting as custodian for the ETF interests."[71]

We think further consideration and clarification may be needed to identify the "entity with substantial control over" the Qualified ETF interests and thus the appropriate signatory to the acknowledgment letter required under Regulation 1.26. We expect the entity with substantial control and appropriate signatory may differ depending on whether the final rule will require FCMs and DCOs to be authorized participants. If the CFTC intends for the "depository acting as

69 Proposed Regulation, 88 Fed. Reg. at 81250.

70 Id.

71 Id.

custodian for the ETF interests" to refer to the custodian of the Qualified ETF,[72] such depository is likely not the entity with substantial control over the Qualified ETF interests given that it will not have a record of the FCM/DCO's interests in the Qualified ETF and the depository's role, including in effecting purchase/redemption/transfer transactions, will be at the direction of the Qualified ETF.

Revised Concentration Limits for Permitted Government MMFs and Qualified ETFs

Citing "certain recent marketplace events," and the risk of "cyber-attacks and operational incidents,"[73] the Commission proposes to (i) establish a single concentration of 50 percent for all Permitted Government MMFs with at least $1 billion in assets and whose management company manages at least $25 billion in assets; and (ii) limit investments in any individual government MMF or U.S. Treasury ETF to 5 percent of total assets held in segregation in each of the segregated, secured amount, or customer cleared swap account origins, while retaining the 25 percent limit on investments in any single family of such government MMFs or U.S. Treasury ETFs.[74]

We understand that financial institutions, including FCMs and DCOs, like all commercial entities, could be targets for cyber-attacks that may adversely impact normal operating capabilities. It is certainly conceivable that such an incident could impair an FCM's or DCO's ability to redeem, promptly on demand, interests in permitted MMFs or ETFs. We note, however, that FCMs and DCOs are subject to comprehensive regulatory requirements to implement policies, procedures, and controls to detect, prevent, monitor, and mitigate operational risk, including cybersecurity risk.[75] Indeed, the CFTC has recently proposed to augment and reinforce these required policies, procedures, and controls with a new requirement that FCMs establish an "operational resilience framework."[76] In short, FCMs and DCOs are already required, upon the occurrence of any such incident, to take action to control and mitigate its effects (including, as necessary for FCMs, maintaining residual interest sufficient to cover any haircut imposed on collateral subject to

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[72] As distinct from a depository who acts as custodian for the FCM/DCO in respect of Customer Funds.

[73] Id. at 81256.

[74] See proposed amendments at CFTC Regulation 1.25(b)(3)(ii)(C) and (D).

[75] See, e.g., CFTC Regulations 160.30 and 162.21 (requiring FCMs to adopt policies and procedures that address administrative, technical and physical safeguards to protect customer information); CFTC Regulation 1.11 (requiring FCMs to adopt risk management policies and procedures addressing operational risk); CFTC Regulation 39.13 (requiring DCOs to establish and maintain a program of risk analysis and oversight with respect to its operations and automated systems to identify and minimize sources of operational risk); CFTC 39.18(b) (requiring DCOs "to establish and maintain a program of risk analysis and oversight with respect to its operations and automated systems to identify and minimize sources of operational risk"). See also NFA Interpretive Notice 9070 (establishing general requirements relating to NFA members' information systems security programs) and NFA Interpretive Notice 9079 (requiring FCMs to adopt and implement a supervisory framework relating to risks involved in outsourcing of any regulatory or operational function to a third-party service provider).

[76] See CFTC, Operational Resilience Framework for Futures Commission Merchants, Swap Dealers, and Major Swap Participants, 6351-01, RIN 3038-AF23 (December 13, 2023).

delayed redemption).[77] Accordingly, we respectfully submit that the proposed concentration limits are not well-tailored to the regulatory objective, which is already well-served by existing requirements (as supplemented, in due course, by the proposed Operational Resilience Framework rulemaking).

We believe that the Commission should continue to allow investment without asset-based concentration limits in the Permitted Government MMFs that would not be subject to concentration limits under the CFTC's current rules. As noted by the Commission in the 2011 Permitted Investment Amendment,

> [i]ndirect investment in Treasuries via a Treasury-only MMMF is essentially the risk equivalent of a direct investment in Treasuries, while allowing an FCM or DCO the administrative ease of delegating the management of its portfolio to a MMMF.[78]

This statement, we submit, is no less true today than it was in 2011, particularly for large Government MMFs.[79] Notably, large Government MMFs (i) invest in high-quality securities, (ii) have stable market value NAVs, (iii) have robust liquidity profiles, (iv) have implemented significant cybersecurity safeguards intended to protect the fund itself as well as its investors from cyber-attacks and other security incidents, and (v) operate in a manner that is consistent with the CFTC's customer asset protection regime. Moreover, Government MMFs arguably present greater diversification and more resiliency for investors than government securities themselves in rare instances of volatility or stress in the government securities market. For instance, funds that have the option to utilize repo or other security types (e.g., agency securities) can avoid mark to market deterioration that would occur in owning the single security itself.

Ultimately, we do not see a reasonable basis for imposing asset-based concentration limits in the Permitted Government MMFs that are not currently subject to concentration limits and, in any event, do not believe that the Commission has demonstrated that Government MMFs are more susceptible to cyber-attacks or other operational incidents than the financial services sector more broadly.[80]

In lieu of the proposed concentration limits, we respectfully propose that investments in government MMFs or U.S. Treasury ETFs that invest in U.S. government securities and that have

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77 See, e.g., JAC Regulatory Alerts 08-05, 09-03, and 09-05 (requiring FCMs to haircut the value of permitted investments in Reserve Primary Fund shares for purposes of their customer segregation, Part 30 secured amount and adjusted net capital computations).

78 2011 Permitted Investment Amendment, 76 Fed. Reg. at 78796.

79 The Commission may wish to increase the threshold for what constitutes a "large" Government MMF – from $1 billion in assets to $5 billion in assets.

80 Indeed, the single example of a cyber-attack cited in the Proposed Regulation relates to an entity that is not an MMF. See Proposed Regulation, 88 Fed. Reg at 81256 (FN 238) (referring to cyber-attack against ION Cleared Derivatives, a third-party provider of cleared derivatives order management, order execution, trading, and trade processing).

$1 billion or more in assets[81] and whose management company manages $25 billion or more in assets not be subject to an asset-based concentration limit (since these investments are proxies for, and not subject to investment risk materially different from, investments in U.S. government securities[82]). In addition, the proposed issuer-based concentration limits of 5 percent on individual eligible MMFs and ETFs and 25 percent on families thereof are not well calibrated relative to each other, since there are few, if any, families of eligible MMFs and ETFs that include more than two individual eligible funds. On that basis, the current concentration limit thresholds of 10 percent and 25 percent have proven to align better with current market structure.

Finally, in light of the obligations of FCMs investing in eligible MMFs and ETFs to monitor both the substantive eligibility of any fund as a Permitted Investment, and the level of any such investment relative to its related concentration limit, we urge the Commission to provide for a brief grace period (of no more than 3 business days) within which an FCM in breach of either condition may cure such breach without being deemed to have invested in an instrument that is not a Permitted Investment under Regulation 1.25 for purposes of the notification requirement under CFTC Regulation 1.12(l).

The Commission Should Align the Treatment under Regulation 1.25 of Qualified ETFs and Permitted Government MMFs in Extraordinary Circumstances

The Commission requests comment on whether there are "any extraordinary circumstances, similar to the events listed in Regulation 1.25(c)(5)(ii) with respect to MMFs, that may justify an exception to the proposed next-day redemption requirement?"

Given the "comparable credit, market, and liquidity risk" profiles of Qualified ETFs and Permitted Government MMFs,[83] we urge the Commission to harmonize the regulatory treatment of extraordinary circumstances in which, for the reasons enumerated in Regulation 1.25(c)(5)(ii), redemption requests from investors must be postponed.

Permitted Investments in Affiliated Eligible MMFs or ETFs

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[81] As noted, we would not oppose increasing the financial assets threshold for a large Government MMF under proposed Regulation 1.25(b)(3)(i)(E) to $5 billion or more in assets.

[82] Alternatively, the Commission may wish to impose an asset-based concentration limit at a level higher than 50 percent, for example, 75-80 percent. Notably, investments in government MMFs are subject to the safeguards required under Investment Company Act Rule 2a-7, 17 CFR 270.2a-7, including the portfolio maturity, quality, diversification, and liquidity conditions set forth in paragraph (d) thereof.

[83] Proposed Regulation, 88 Fed. Reg. at 81257.

Regulation 1.25(b)(5)(ii) currently provides that an FCM or a DCO may invest Customer Funds in a fund affiliated with that FCM or DCO. We believe that no change to this provision is warranted and urge the Commission not to prohibit such investments.

We note that "risks posed by affiliates" are a component of the Risk Management Program that FCMs are required to adopt under Regulation 1.11.[84] In adopting that requirement the Commission recognized that "many FCMs are part of a larger holding company structure that may include affiliates that are engaged in a wide array of business activities," and that the "top level company" in such a structure "is in the best position to evaluate the risks that an affiliate of an FCM may pose to the enterprise, as it has the benefit of an organization-wide view and because an affiliate's business may be wholly unrelated to an FCM's activities."[85] Accordingly, the Commission concluded, "to the extent an FCM is part of a holding company with an integrated risk management program, the Commission would allow an FCM to address affiliate risks and comply with [Regulation] 1.11(e)(1)(ii) through its participation in a consolidated entity risk management program."[86]

Last month, the Divisions of Clearing and Risk, Market Oversight, and Market Participants issued a Staff Advisory reminding DCOs "of their obligations to ensure compliance with existing statutory and regulatory requirements" relating to affiliate relationships with intermediaries and other market participants, including trading entities.[87]

We submit that, because Permitted Investments involving FCM affiliates are already subject to the policies, procedures, and controls of consolidated risk management programs,[88] as well as existing statutory and regulatory requirements, and further subject to examination and audit for compliance with the foregoing requirements, there is no reason to revisit the Commission's previous consideration of this issue (as supplemented by "further action" that Staff may recommend in light of Letter 23-16).[89]

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84 See CFTC Regulation 1.11(e)(1)(ii).

85 Enhancing Protections Afforded Customers and Customer Funds Held by Futures Commission Merchants and Derivatives Clearing Organizations, 78 Fed. Reg. 68506, 68519 (November 14, 2013).

86 Id.

87 See CFTC Staff Advisory on Affiliations Among CFTC-Regulated Entities, CFTC Letter No. 23-16 (December 18, 2023 ("**Letter 23-16**").

88 78 Fed. Reg. at 68520 (noting that an FCM's risk management policies and procedures under Regulation 1.11 must include procedures for assessing the appropriateness of investing customer funds in accordance with [Regulation] 1.25, and "must take into consideration the market, credit, counterparty, operational, and liquidity risks associated with the investments").

89 Notably, FCMs are expressly permitted to deposit Customer Funds with affiliated banks or brokers, provided that they disclose such arrangements, and of course, subject to their obligations to monitor and control the risks related to such arrangements, pursuant to CFTC Regulation 1.11. See paragraph (7) of the Risk Disclosure Statement required under CFTC Regulation 1.55(a) ("Futures commission merchants are permitted to deposit customer funds with affiliated entities, such as affiliated banks, securities brokers or dealers, or foreign brokers. You should inquire as to

Investments in Permitted Investments With Adjustable Rates of Interest and Investments in Commercial Paper and Corporate Notes or Bonds

For the reasons set forth in the Proposed Regulation,[90] we support the Commission's proposal to amend CFTC Regulation 1.25(b)(2)(iv)(A) by replacing LIBOR with the Secured Overnight Financing Rate ("**SOFR**") as a permitted benchmark for Permitted Investments that contain an adjustable rate of interest and to remove commercial paper, corporate notes, and corporate bonds from the list of Permitted Investments.

The Commission seeks comment on whether it should consider other interest rates beyond SOFR as permitted benchmarks for adjustable rate securities under Regulation 1.25.[91] We believe that FCMs and DCOs should also be permitted to invest Customer Funds in adjustable rate securities that reference SONIA, €STR, TONAR, and CORRA, to the extent that the FCM or DCO has balances owed to customers denominated in GBP, EUR, JPY or CAD, respectively. As the Commission is aware, these alternative reference rates have been selected by public/private-sector working groups, similar to the Alternative Reference Rates Committee, formed by the Bank of England (SONIA), the European Central Bank (€STR), the Bank of Japan (TONAR) and the Bank of Canada (CORRA), in connection with the transition away from LIBOR rates in these other currencies. As is the case with respect to the replacement of USD LIBOR with SOFR, the replacement of GBP, EUR, JPY, and CAD LIBOR with the risk-free rates by the central banks, as noted, advances the objective of Regulation 1.25 by promoting the use of reliable benchmarks as a condition on an instrument's eligibility as a Permitted Investment.[92] Accordingly, we believe that it is appropriate to include these other benchmark rates for Permitted Investments that contain an adjustable rate of interest, to the extent of an FCM's or DCO's Customer Funds held in the relevant corresponding currency.

Investments in Certificates of Deposit Issued by Banks

We believe that bank CDs should be removed from the list of Permitted Investments. We are not aware of a recent use of bank CDs for a Permitted Investment under Regulation 1.25, and no FIA member has said it foresees using bank CDs for that purpose.

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whether your futures commission merchant deposits funds with affiliates and assess whether such deposits by the futures commission merchant with its affiliates increases the risks to your funds.").

90 88 Fed. Reg. at 81253-54.

91 Id. at 81254.

92 Id.

Technical Corrections and Amendments

In light of the removal of commercial paper and corporate notes or bonds from the list of Permitted Investments, the current text of Regulation 1.25(b)(2)(vi) (setting forth conditions on such investments) should also be deleted.

The Forms of Government Money Market Fund Account acknowledgment letters should each be amended such that the Government Money Market Fund represents as follows, reflecting the proposed revisions to CFTC Regulations 1.25(a)(1)(v) and (c)(1):

"Furthermore, you acknowledge and agree that the Shares are in a fund that holds itself out to investors as a government money market fund, in accordance with 17 C.F.R. § 270.2a-7. In addition, the Shares are in a fund that does not choose to rely on the ability to impose discretionary liquidity fees consistent with the requirements of 17 C.F.R. § 270.2a-7(c)(2)(i)."

We suggest inserting this text following the second full paragraph of the letter (between "thereunder" and "Furthermore").

Comments on the SEC's Final Rule on Standards for Covered Clearing Agencies for U.S. Treasury Securities

During the comment period for the Proposed Regulation the SEC adopted a final rule requiring covered clearing agencies for U.S Treasury securities to adopt policies and procedures requiring their direct participants to submit for clearance and settlement all repurchase or reverse repurchase agreements collateralized by U.S. Treasury securities, as well as certain secondary cash market transactions (the "**Treasury Clearing Rule**").[93]

In response to the SEC's proposal of the Treasury Clearing Rule, FIA requested an exemption for FCMs from the clearing requirement when transacting in U.S. Treasury securities (including direct purchases, repos, and reverse repos conducted in compliance with Regulation 1.25) and acting in their capacity as an FCM, citing conflicts between the proposed clearing mandate and the customer asset protection regime under the Commodity Exchange Act and the CFTC's regulations thereunder. In the Treasury Clearing Rule, the SEC determined that such an exemption is unnecessary.[94] The SEC cited the availability of the "Sponsored Service" and the "Prime Broker and Correspondent Clearing" models at the Fixed Income Clearing Corporation ("**FICC**") (the sole provider of clearing and settlement services for U.S. Treasury securities) as potentially compatible with, or at least adaptable to, the requirements of CFTC Regulations, and urged FCMs

[93] Standards for Covered Clearing Agencies for U.S. Treasury Securities and Application of the Broker-Dealer Customer Protection Rule With Respect to U.S. Treasury Securities, Release No. 34-99149 (Final Rule Voting Draft, December 13, 2023).

[94] Id. at 80.

to "work with [FICC] to identify any modifications to its client clearing models to better allow FCMs to access central clearing."[95]

We believe that the Treasury Clearing Rule presents numerous material issues for FCMs engaging in Permitted Investments involving U.S. Treasury securities, and we anticipate having to engage with the Commission and Commission staff to vet and work through those issues, which may ultimately necessitate further changes to, or Staff no-action relief under, Regulation 1.25.

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Thank you for your consideration of these comments. If the Commission or any member of the staff have any questions regarding the matters discussed herein or need any additional information, please contact me at alurton@fia.org or 202.772.3057, or Michael Kobida, Executive Director, Collateral Services, at michael.kobida@cmegroup.com or 312.45.8961.

Respectfully submitted,

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95 Id. at 78.

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