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**By Electronic Mail**

July 20, 2009

Mr. David A. Stawick  
Secretary  
Commodity Futures Trading Commission  
1155 21<sup>st</sup> Street NW  
Washington DC 20581

**Re: Investment of Customer Funds and Funds Held in an Account for Foreign Futures and Foreign Options Transactions, 74 Fed.Reg. 23962 (May 22, 2009)**

Dear Mr. Stawick:

The Futures Industry Association (“FIA”) welcomes the opportunity to submit this letter in response to the Commodity Futures Trading Commission’s (“Commission’s”) request for comment on possible revisions to Commission Rule 1.25, Investment of Customer Funds, and Rule 30.7, Treatment of Foreign Futures or Foreign Options Secured Amount.<sup>1</sup> FIA shares the Commission’s interest in assuring that the investment of customer assets be “consistent with the objectives of preserving principal and maintaining liquidity.” 74 Fed.Reg. 23962, 23963.

As the Commission is aware, FIA actively participated in the Commission’s consideration of the amendments to rule 1.25 adopted in 2000 and again in 2004-2005. Indeed, several provisions of the current rule were suggested by FIA in its written comments on the proposed amendments. FIA is particularly pleased, therefore, that the investment guidelines set out in Rule 1.25 generally weathered the financial turmoil of the past year.<sup>2</sup>

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<sup>1</sup> FIA is a principal spokesman for the commodity futures and options industry. FIA’s regular membership is comprised of approximately 30 of the largest futures commission merchants (“FCMs”) in the United States. Among FIA’s associate members are representatives from virtually all other segments of the futures industry, both national and international. Reflecting the scope and diversity of its membership, FIA estimates that its members effect more than eighty percent of all customer transactions executed on United States contract markets.

<sup>2</sup> For example, as reflected in the enclosed Excel spreadsheets prepared from publicly available data, from December 2007 through May 2009, firms experienced ample liquidity in the secondary markets for US Treasury securities and general obligations of government sponsored agencies. Although the markets experienced higher volatility levels in the fall of 2008, bid to offer spreads were always available.

To prepare this comment letter, FIA formed a committee comprised of individuals responsible for financial management at a significant number of member firms, who carefully reviewed the issues raised in the Federal Register release, as well as the provisions of Rule 1.25 and 30.7. The committee did not identify any changes to Rule 1.25 that it believes are essential to preserve the rule's primary objectives. Nonetheless, the committee has identified and set out below several modifications to the rule that should further reduce the exposure of customer funds to potential credit, liquidity and market risks. We encourage the Commission to include these recommendations in any proposal to amend Rules 1.25 and 30.7 that may hereafter be published for comment.

### **Permitted Investments**

FIA believes that all of the permitted investments described in Rule 1.25(a) are compatible with the Commission's objectives of preserving principal and maintaining liquidity.<sup>3</sup> In addition, we recommend that the Commission add to the list of permitted investments securities that are guaranteed as to principal and interest by an agency of the United States, such as securities issued by a bank and guaranteed by the Federal Deposit Insurance Corporation ("FDIC") in accordance with the FDIC's Temporary Liquidity Guarantee Program and any similar programs that may be created.<sup>4</sup> Further, we recommend that the Commission consider adding securities issued by foreign banks and guaranteed as to principal and interest by the relevant foreign government. These securities are highly liquid and trade in a manner similar to sovereign debt.<sup>5</sup>

We recognize that the Commission may want to require that, in order to be a permitted investment under Rule 1.25, securities issued by a particular bank, domestic or foreign, and guaranteed as to principal and interest as noted above, must be of sufficient size to assure liquidity, and suggest \$1 billion as an appropriate minimum size. For purposes of complying with the concentration limits discussed below, these securities would be included with all other securities issued by the relevant bank.

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<sup>3</sup> However, we understand there is some confusion regarding the ability of FCMs to invest customer segregated funds in securities offered in reliance on Securities and Exchange Commission ("SEC") Rule 144A under the Securities Act of 1933. We ask the Commission to clarify whether or under what circumstances FCMs may purchase Rule 144A securities.

<sup>4</sup> Under the Temporary Liquidity Guarantee Program, the FDIC guarantees the payment of all unpaid principal and contract interest on newly-issued senior unsecured debt of an insured depository institution, if the depository fails or if a bankruptcy petition is filed by the depository's parent holding company. The guarantee applies to debt issued on or before October 31, 2009 and extends to December 31, 2012. Enclosed with this letter is a presentation prepared by Bank of America Merrill Lynch earlier this year that provides support that the securities issued under the Temporary Liquidity Guarantee Program have a liquidity profile comparable to the profile for government sponsored agencies.

<sup>5</sup> Securities issued by foreign banks and guaranteed as to principal and interest by the relevant foreign government should be required to have the same ratings as sovereign debt, discussed below.

## **Limitations and Safeguards**

### **1. Marketability**

We have not identified any reason to alter the requirement that investments purchased with customer funds be “readily marketable” as defined in SEC Regulation 15c3-1.

### **2. Ratings**

Rules 1.25(b)(2)(B) and (E) currently provide that the instruments described must have the highest short-term rating of an NRSRO or one of the two highest long-term ratings of an NRSRO. FIA recommends that these provisions of the rule be revised to require that the listed instruments must have the highest short-term rating or one of the two highest long-term rating of at least two NRSROs. Similarly, Rule 1.25(b)(2)(D) should be amended to require that foreign sovereign debt also have the highest rating of at least two NRSROs.

### **3. Concentration**

FIA believes that the concentration limits set out in Rule 1.25(b)(4) are generally appropriate insofar as they set limits on the amount of securities of any one issuer that an FCM may purchase. One exception would be money market mutual funds. The rule currently sets no limit on the amount of customer funds that may be used to purchase interests in any money market mutual funds. We recommend that the rule be amended to provide (i) that an FCM’s investment in any one money market mutual fund may not exceed 5 percent of assets under management in that fund and (ii) that no more than 25 percent of invested customer funds may be invested in any one money market mutual fund.<sup>6</sup>

Separately, FIA believes it would be appropriate to adopt concentration limits for different product types in addition to issuer limits. That is, the Commission should amend Rule 1.25 to provide that no more than a fixed percentage of customer funds could be invested in any one product type. Thus, for example, although 100 percent of customer funds could be invested in US government securities or money market funds, FIA recommends that no more than 75 percent of customer funds be invested in securities of government sponsored enterprises, and no more than 25 percent of customer funds be invested in each of (i) securities issued pursuant to the Temporary Liquidity Guaranteed Program and similar government programs, (ii) municipal securities, (iii) certificates of deposit, (iv) commercial paper, and (v) corporate securities.<sup>7</sup>

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<sup>6</sup> As the Commission is aware, the SEC recently proposed for comment certain amendments to its rules governing money market mutual funds. 74 Fed.Reg. 32688 (July 8, 2009). Any amendments that the SEC may adopt may cause us to take a different position with respect to the use of money market funds under Rule 1.25.

<sup>7</sup> For purposes of Rule 1.25, foreign sovereign debt would continue to be limited to the amount of the balances in that country’s currency held in the FCM’s customer segregated account. As discussed below, however, the ability of an FCM to invest in foreign sovereign debt should not be so limited in the foreign futures and foreign options secured amount.

FIA believes it is appropriate to exempt from both the issuer concentration limits currently in the rule and the sector concentration limits proposed above those securities held either in connection with reverse repurchase transactions or in accordance with the procedures set out in Rule 1.25(e).<sup>8</sup> The risk of holding such securities, therefore, is significantly less than holding those same securities as a result of a direct investment. These transactions are generally over-collateralized, subject to daily mark-to-market margin requirements, and must be reversed within one business day or on demand. As such, they are comparable to the programs offered by derivatives clearing organizations and referenced in Rule 1.25(b)(5).

#### **4. Liquidity**

FIA recommends that the Commission consider requiring FCMs to hold a certain percentage of total invested customer funds, *e.g.*, 10 percent, in more highly liquid investments. Such highly liquid investments would include US Treasury securities, bank deposits,<sup>9</sup> money market funds, reverse repurchase agreements and transactions permitted under Rule 1.25(e).

#### **5. Weighted Average Maturity**

Rule 1.25(b)(5) provides that, except for investments in money market mutual funds, the dollar-weighted average of the time-to-maturity of the investment portfolio may not exceed 24 months. The Commission imposed this requirement to minimize credit risk, volatility risk, and liquidity risk in the FCM's investment portfolio. To further protect against these risks, FIA believes that the dollar-weighted average of the time-to-maturity of the investment portfolio should be reduced to not to exceed 18 months. In calculating the weighted average of the time to maturity, however, FIA recommends that securities held in a reverse repurchase agreement or in accordance with the procedures of Rule 1.25(e) be deemed to have a maturity of one day. As noted above, securities held pursuant to reverse repurchase agreements are generally over-collateralized, subject to daily mark-to-market margin requirements, held under a tri-party agreement with a permitted depository, and must be reversed within one business day or on demand. Therefore, we believe it is more appropriate to treat securities held through such transactions as having a one day maturity.

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<sup>8</sup> Rule 1.25(e) authorizes an FCM that is also registered with the Securities and Exchange Commission as a broker-dealer, in connection with its activities as a broker-dealer, to exchange securities to which it has an unqualified right to pledge for customer money or securities held in the customer segregated account. Among other requirements, in addition to those noted above, the rule provides that the securities transferred into the customer segregated account must be held in a safekeeping account, *i.e.*, through a tri-party agreement, with a bank, a derivatives clearing organization or the Depository Trust Company in an account that complies with Commission Rule 1.26.

<sup>9</sup> Bank deposits include those customer funds held in bank trust accounts, as described in CFTC Letter No. 03-31, [2003-2004 transfer Binder] Comm.Fut.L.Rep. (CCH) ¶29,576 (August 25, 2003).

### **Foreign Futures and Foreign Options Secured Amount**

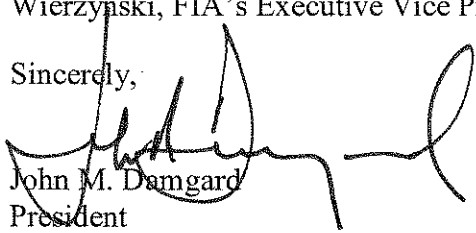
As a general matter, FIA would support an amendment to Commission Rule 30.7, which would require FCMs to follow Rule 1.25 in investing the foreign futures and foreign options secured amount. Our member firms generally follow the Rule 1.25 investment guidelines in any event. However, FCMs should have greater latitude in investing the secured amount in relevant sovereign debt and should not be subject to the provisions of Rule 1.25, which limit the amount an FCM may invest in sovereign debt to the extent of its liabilities to its clients in that country's currency. Often, FCMs have customers that use a single currency margining arrangement and the FCM may still have an obligation to margin the clients' positions with their clearing organizations in multiple currencies.

In addition, we reiterate our recommendation that Commission consider adding securities issued by foreign banks and guaranteed as to principal and interest by the relevant foreign government. As noted, these securities are highly liquid and trade in a manner similar to sovereign debt.

### **Conclusion**

We trust the Commission will find these comments in response to the advance notice of proposed rulemaking with respect to Commission Rules 1.25 and 30.7 helpful. We would be pleased to meet with the staff to discuss these issues in greater detail. If the Commission has any questions concerning the matters discussed in this letter, please contact Barbara Wierzynski, FIA's Executive Vice President and General Counsel, at (202) 466-5460.

Sincerely,

  
John M. Damgard  
President

cc: Honorable Gary Gensler, Chairman  
Honorable Michael Dunn, Commissioner  
Honorable Jill E. Sommers, Commissioner  
Honorable Bart Chilton, Commissioner  
Division of Clearing and Intermediary Oversight  
Ananda Radhakrishnan, Director  
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