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March 21, 2011

Ananda K. Radhakrishnan
Director
Division of Clearing & Intermediary Oversight
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Dear Ananda:

This is to follow up on our recent meeting with the Staff and prior correspondence on the Commission's recent rulemakings as to the use of shares of money market mutual funds ("money funds") for investment of customer cash and collateral posted to secure futures and swaps transactions. Again, we would like to thank you for meeting with us, and for the careful consideration that you and the staff have shown.

We understand the main concerns that the Commission seeks to address in these aspects of its proposed rulemakings center on liquidity and the risk of a "run" on a money fund. At the same time, we note that most, if not all, commenters have urged the Commission to preserve the ability to invest in money funds.[1] Below, we summarize the Commission's proposals, and then suggest standards that we believe would ensure liquidity while also allowing for the investment of collateral and customer funds.

I. Commission Proposals.

CFTC Rule 1.25 governs the investment of customer money deposited with FCMs and DCOs for the purpose of margining transactions in futures and other exchange-traded instruments. The Commission is considering amending Rule 1.25 so that no more than 10% of the total "assets held in segregation" (i.e., customer cash held by the FCM or DCO) could be

[1] *See* Letters from J. Charles Cardona, President, The Dreyfus Corporation (Dec. 3, 2010); Karrie McMillan, General Counsel, The Investment Company Institute (Dec. 3, 2010); Keith A. Weller, Executive Director & Senior Associate General Counsel, UBS Global Asset Management (Dec. 3, 2010); Gary DeWaal, Senior Managing Director and Group General Counsel, Newedge USA, LLC and Laurie Ferber, Executive Vice President and General Counsel, MF Global, Inc. (Dec. 2, 2010). Prior to the release of the pending proposals, Bank of New York Mellon submitted a comment opposing application of the proposed Rule 1.25 standards to swaps (Dec. 6, 2010).

invested in Money Funds, and no more than 2% of the total "assets held in segregation" could be invested in any one family of Money Funds.[2]

At the same time, in another proposed rulemaking related to uncleared swap transactions, the Commission is proposing standards as to the treatment of collateral posted by counterparties to swap dealers and major swap participants.[3] This proposed rulemaking is primarily concerned with the segregation of collateral and custody.[4] However, it also proposes new Rule 22.603, pursuant to which, notwithstanding any agreements by the parties, collateral could only be invested consistent with Rule 1.25.[5]

Finally, in an advance notice of proposed rulemaking related to cleared swap transactions,[6] the Commission solicits comment on potential methods for the protection of collateral for cleared swap transactions, including by applying the Rule 1.25 limitations on investment to such collateral.[7]

II. Alternative Approach.

Rather than simply establishing hard caps on investment as proposed, we suggest that the Commission instead adopt the following approach for futures contracts.

A. Rule 1.25: Government Funds.

First, Rule 1.25 should not limit the amount of assets that may be invested in money funds that invest exclusively in U.S. government securities (including U.S. government securities acquired through repurchase transactions). Investing funds in government securities directly, and investing those funds in money market funds that invest solely in government securities serves the same purpose — protection of customer funds by limiting investment to highly liquid,

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[2] *Investment of Customer Funds and Funds Held in an Account for Foreign Futures and Foreign Options Transactions,* 75 Fed. Reg. 67642 (Nov. 3, 2010).

[3] *Protection of Collateral of Counterparties to Uncleared Swaps*, 75 Fed. Reg. 75432 (Dec. 3, 2010).

[4] *See* 75 Fed. Reg. at 75433-75435.

[5] Proposed Rule 22.603; 75 Fed. Reg. at 75434; 75438.

[6] *Protection of Cleared Swaps Customers Before and After Commodity Broker Bankruptcies,* 75 Fed. Reg. 75162 (Dec. 2, 2010).

[7] *See* 75 Fed. Reg. at 75164. It is not clear how the Commission would apply such limitations when collateral for cleared and uncleared transactions is posted in kind. Indeed, Section 724 of the Dodd-Frank Act only appears to contemplate limitations on investment of "money" posted as margin for cleared swap transactions.

stable instruments.[8] Allowing FCMs and DCOs to invest freely in such funds would also eliminate the need for FCM or DCO staff to buy, sell, monitor the maturity of, and otherwise actively manage a portfolio of treasury instruments and thereby reduce operational risks and costs associated with that activity.

B. Rule 1.25: Other Money Funds.

As to investments in any other type of money fund, we believe the Commission could implement quantitative and prudential standards that would limit an FCM's or DCO's exposure to the risk of a run. These standards would limit the amounts of an FCM's or DCO's investment of segregated assets, establish qualifications for money funds that would be eligible for the investment of segregated assets, and require diligence by FCMs or DCOs before investing in a money fund.

Specifically, in order to limit the amount of an FCM's or DCO's investment of segregated assets, we suggest that, with respect to money funds that are not invested solely in U.S. government securities, Rule 1.25 be revised to:

(1) prohibit an FCM or DCO from investing more than 20% of its total assets held in segregation in any one family of money funds; and

(2) establish that an FCM's or DCO's investment of assets held in segregation could not represent more than 10% of any one money fund.

In addition, we suggest that the Commission set minimum qualification standards as to money funds in which customer funds are invested. We suggest that an FCM or DCO should not be permitted to invest in a money fund unless:

(1) the money fund is an established prime money fund with at least $10 billion in assets;

(2) the money fund's management company has at least $50 billion in money fund assets under management; and

(3) it agrees to redeem shares in cash not later than the business day following a redemption request.

Finally, Rule 1.25 should require an FCM or DCO, prior to investing customer funds in any money fund, and periodically thereafter, to complete a due diligence review of the money fund in question in order to determine that it presents minimal credit risks and has the capacity to

[8] Other financial regulators have taken the similar approach of treating as an eligible asset shares of a mutual fund that holds only assets eligible for the entity to own directly. *See., e.g.,* 12 C.F.R. 1.4(h) (shares of mutual funds that own only bank-eligible investments are themselves eligible for investment by a bank).

meet short-term redemption needs. For this purpose, the FCM or DCO should have to adopt written policies and procedures that require it to exercise due skill, care and diligence, and to consider, together with any other relevant factors:

- The need for diversification of risk;
- The diversification of the proposed money fund's investments;
- The quality of the proposed money fund's investments;
- Credit quality; and
- The percentage of the fund's shares that are owned by its largest shareholders.[9]

An FCM or DCO should have to keep, and periodically update, a record to reflect the basis for its determination that a given money fund was an appropriate investment.

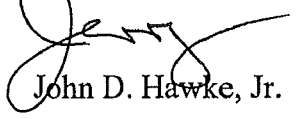
C. Swaps Collateral.

After additional consideration, we continue to believe that application of concentration limits to the investment of swaps collateral (whether in cleared or uncleared transactions) would be inappropriate and counterproductive. Swaps entities are sophisticated parties who are permitted to decide how collateral is to be handled. In general, they are given the right to choose whether to segregate their collateral at all, whether to hold those assets with a third party, whether to allow the collateral to be hypothecated, whether to permit those assets to be invested, whether they or their counterparty shall have the benefit of those investments, etc. Surely, they should have the right to agree to have that collateral invested in money funds that comply with SEC Rule 2a-7 without limitation. Accordingly, we suggest that the Commission not apply caps on the investment of swap collateral. On the other hand, we believe that the Commission could, if deemed necessary, require swap dealers and major swap participants to adopt policies and procedures for the investment of such funds, as described above.

[9] This approach is consistent with that employed by the Financial Services Authority of the United Kingdom (*see* FSA Handbook Chapter 7, *Client Money Rules*, Sections 7.4.7 – 7.4.10), and with the Securities and Exchange Commission's recent proposal to amend rules under the Investment Company Act of 1940 that refer to credit ratings. *References to Credit Ratings in Certain Investment Company Act Rules and Forms,* 76 Fed. Reg. 12896 (Mar. 9, 2011).

We appreciate the opportunity to provide you with these supplemental comments, and we look forward to working with you in the future.

Sincerely,



John D. Hawke, Jr.

cc: Gary Gensler, Chairman