

From: Nikki G. Appel <Nikki.G.Appel@chase.com>
Sent: Friday, September 10, 2010 5:42 PM
To: acknowledgmentletter <acknowledgmentletter@CFTC.gov>
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Subject: RIN 3038-AC72
Attach: Final CFTC Comment Letter.doc

Nikki Appel | Managing Director & Associate General Counsel | JPMorgan Chase Bank, N.A.
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September 10, 2010

Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581
Attn.: Mr. David A. Stawick, Secretary of the Commission

Via email (acknowledgmentletter@cftc.gov)

Re: RIN Number 3038-AC72 Acknowledgment Letters for Customer Funds and Secured Amount Funds

Ladies and Gentlemen:

JPMorgan Chase Bank, N. A. (“J.P. Morgan”) appreciates this opportunity to comment on the Commodity Futures Trading Commission’s (the “Commission”) proposed amendments to its regulations (“Regulations”) regarding the required content of the acknowledgment letter that a registrant must obtain from a depository holding its segregated customer funds or funds of foreign futures or foreign options customers (the “Proposal”).¹

Role of Depository to Segregate Funds

Currently, in setting up and maintaining segregated and secured accounts (“Accounts”) on behalf of futures commission merchants (“FCMs”) and derivatives clearing organizations (“DCOs”) that accept customer funds, the depository’s role is to comply with certain contractual provisions that are consistent with elements of the Regulations through an acknowledgment letter (“Acknowledgment Letter”). Those provisions require a depository to (a) ensure that Accounts are clearly identified as such on its books and records and (b) agree that fully paid assets and cash in the Account(s) shall at no time secure, directly or indirectly, any loan made by the depository to the client nor shall any such assets be subject to any right, charge, security interest, lien or claim of any kind in favor of the depository or any person claiming through the depository. The depository also acknowledges and agrees that it has been informed that the funds in the Accounts are those of commodity customers and that such funds are being held in accordance with the provisions of the Commodity Exchange Act, as amended (the “Act”) and the rules and regulations promulgated by the Commodity Futures Trading Commission (the “CFTC”) thereunder.

The Depository, in providing the Acknowledgment Letter, has not undertaken to ensure that the FCMs or DCOs are managing funds deposited in or operating the Accounts in accordance with Act and regulations thereunder. While J.P. Morgan believes that it is correct for the depository to acknowledge that these are funds of commodity customers and as such also indicate how it has set up the Accounts on its books and records and how J.P. Morgan treats the funds from its

¹ 75 *Fed. Reg.* 47738 (August 9, 2010).

perspective, J.P. Morgan does not believe it is within the scope of the services offered by the Depository to monitor activity in the Account or otherwise ensure that FCMs or DCOs operate the Accounts in accordance with the Act and CFTC regulations.

We therefore request that the Proposal be amended to clarify this point. In particular, we note that the second paragraph of the letter requires us to “acknowledge and agree that ... the Funds must otherwise be treated in accordance with the provisions of the Act and CFTC regulations”. In addition, the proposed rule provides: “No person, including ... *any depository (emphasis added)* that has received customer funds for deposit in a segregated account . . . may hold, dispose of, or use any such funds as belonging to any person other than the option or commodity customers of the futures commission merchant which deposited such funds”. Each of the foregoing could be considered obligations of the depository to monitor the compliance of its customers. It does not appear that the CFTC wishes to impose any such unreasonable policing obligations on depositories since the letter states that a depository may conclusively presume that any withdrawal from the Account(s) and the balances maintained therein are in conformity with the Act and CFTC regulations without any further inquiry. We therefore request that the foregoing reference to the depository be removed and that the depository be required to acknowledge that the funds deposited by the FCMs or DCOs are funds held by such parties for or on behalf of its customers and to acknowledge how we will treat the funds but not to agree as to how our customers are treating the funds.

Audit of the Accounts

The CFTC has requested, and the Depository is comfortable providing, officers, agents and/or employees access to the Accounts from time to time in connection with any examination of an FCM or DCO. However, in order to not place an undue burden on our client service and operations teams we request that such information request be reasonable in frequency and scope and be upon reasonable notice and at a mutually agreed place and time.

Instructions from CFTC

The Proposal permits the Depository to act upon and rely upon instructions from the CFTC. J.P. Morgan suggests that the Acknowledgment Letter include a notice provision with contact information for the Depository so that the CFTC has information on how to best contact the Depository.

Fully Paid Securities

We also believe that the rule should distinguish between Accounts that hold cash from those that hold securities. With respect to Account(s) holding cash the proposed Acknowledgment Letter includes the right to charge back to the Account(s) checks or other deposits credited to the Account(s), which are subsequently dishonored, reversed or otherwise returned. Similarly, for Account(s) that hold securities, the depository should waive its lien and right of setoff only on fully

paid securities. Indeed, we believe that the rule should clarify that only fully paid securities should be deemed credited to such an Account. To the extent that it is determined that a depository has extended credit with respect to a security deposited into such an Account then the Uniform Commercial Code, Section 9-206 protects a securities custodian that settles a securities transaction in this regard by stating that “A security interest in favor of a securities intermediary attaches to a person’s security entitlement if (1) the person buys a financial asset through the securities intermediary in a transaction in which the person is obligated to pay the purchase price to the securities intermediary at the time of the purchase; and (2) the securities intermediary credits the financial asset to the buyer’s securities account before the buyer pays the securities intermediary.” No security agreement is required and the security interest is auto-perfected under 8-106. This is consistent with Rule 15c3-3 of the Securities Exchange Act of 1934, as amended, which explicitly excludes securities that are not fully paid securities. The Depository therefore requests that the Proposal be amended to reference fully paid securities.

Conclusion

While J.P. Morgan supports the aims of the section of the Proposal that is the subject of this letter, it believes that clarifications to the Acknowledgment Letter should be made that are consistent with the scope of services offered. Again, J.P. Morgan appreciates the opportunity to comment on this subject and would be pleased to discuss any of the points raised in this letter in more detail. Should you have any questions, please contact Jason Orben at 212-623-5419.