CME Group

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

Re: Protection of Cleared Swaps Customers Before and After Commodity Broker Bankruptcies – 75 Fed. Reg. 75162 (Dec. 2, 2010), RIN 3038-AD99

Dear Mr. Stawick:

CME Group Inc. ("CME Group") appreciates the opportunity to comment on the Commodity Futures Trading Commission's ("CFTC" or the "Commission") advanced notice of proposed rulemaking ("ANPR") regarding potential models for implementing new provisions in the Commodity Exchange Act ("CEA"), enacted by Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank" or "DFA"), concerning segregation of collateral posted by customers in connection with cleared swaps. CME Group is the parent of Chicago Mercantile Exchange Inc. ("CME"). CME's clearing house division ("CME Clearing") offers clearing and settlement services for exchange-traded futures contracts, and for over-the-counter ("OTC") derivatives transactions through CME ClearPort. CME is registered with the CFTC as a derivatives clearing organization ("DCO"), and is one of the largest central counterparty clearing services in the world. As of December 31, 2010, customer-segregated assets on deposit at CME Clearing were in excess of $62 billion. In light of CME Clearing's significant role in providing clearing and settlement services for exchange-traded and OTC derivatives and collateral management services for customer funds, CME Group is particularly well-positioned to comment on issues presented in the ANPR.

A. Overview

The ANPR describes four potential models for segregation of collateral posted by customers to secure swaps that are cleared by a DCO. First is the "baseline" segregation model (the "Baseline Model"), which has been used for many years in accordance with the CEA and CFTC regulations for segregation of collateral posted by customers to secure exchange-traded futures and options on futures.[1] A hallmark of the Baseline Model is the strict requirement that customer collateral be kept separate from the FCM's property, and "[u]nder no circumstances" may such collateral be used "except to purchase, margin, guarantee, secure, transfer, adjust or settle trades, contracts or commodity option transactions of commodity or option customers."[2]

[1] A similar segregation model is used for customers' foreign futures and options, in accordance with CFTC Regulation 30.7. That model is not addressed in the ANPR, and we do not address it in this letter.

[2] CFTC Regulation 1.20(a).

Under the Baseline Model, collateral of multiple futures customers of a futures commission merchant ("FCM") is held in "commingled" or "omnibus" accounts at DCOs and other permitted depositories. If an FCM were to default to a DCO, and if the default were caused by failure of a futures customer to meet its financial obligations to the FCM, the DCO would be permitted (but not required), in accordance with the DCO's rules and CFTC regulations,[3] to use collateral of the FCM's other futures customers in the commingled account at the DCO to satisfy the FCM's net customer futures obligation to the DCO (referred to in the ANPR as "fellow-customer risk").[4] A DCO may not, however, use customer collateral to satisfy any obligations arising out of an FCM's "house" or "proprietary" account.

The Baseline Model has performed admirably over the years, with no futures customers suffering losses as a result of an FCM's bankruptcy or default. In October 2010, when CME Clearing put into effect its regime for pre-bankruptcy, substantive requirements for treatment of funds of cleared-swap customers (including but not limited to funds to margin interest rate swaps and credit default swaps) in conjunction with the CFTC's amendments to its Part 190 bankruptcy regulations, we adopted rules that follow the Baseline Model.[5] Furthermore, the Trustee under the Securities Investor Protection Act ("SIPA") for Lehman Brothers Inc. ("LBI") recently recommended that SIPA (and the SEC's segregation rules) be amended to establish sub-pools of customer property, citing "[t]he concept of separate estates or subpools of customer property ... embodied in the rules of the CFTC dealing with commodities brokerage."[6] LBI's SIPA Trustee noted that "[t]his approach could allow much more prompt ... distribution of property" and "could reduce much confusion and aid in the administration of these accounts."[7]

Each of the three remaining models in the ANPR diverges from the Baseline Model by proposing some form of actual or theoretical "individual segregation" for customer cleared-swap accounts. The first of these is Full Physical Segregation, which entails "[e]ach customer's cleared swaps account, and all property collateralizing that account, [being] kept separately for and on behalf of that cleared swaps customer at the FCM, at the DCO, and at each depository."[8]

The second has been christened Legal Segregation With Commingling ("Legal Segregation"). In this model, the collateral of cleared swaps customers would be kept in a commingled account at each DCO

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[3] Under CME rules, in an FCM default, CME Clearing will first utilize assets of the defaulting firm (memberships, performance bond and guaranty fund deposits) to cure the default. With regard to the use of customer collateral, CME Rule 802.G provides, in pertinent part:

> ....If a default occurs in a customer account, the Clearing House has the right to liquidate and apply toward the default all open positions and customer performance bond deposits in the associated customer account class. Accordingly, positions performance bonds deposited by customers not causing the default are at risk if there is a default in the applicable customer account class of their clearing member. If the Clearing House liquidates positions and/or collateral in a customer account class, any collateral remaining after application to Losses in respect of such account class shall be reserved to such customer account class in order to satisfy the claims of non-defaulting customers in accordance with applicable law.

[4] 75 Fed. Reg. 75162, 75163.

[5] *See generally* CME Rules 8F100 through 8F136.

[6] *In re Lehman Brothers Inc.*, No. 08-01420 (S.D.N.Y. Bankruptcy Court), Trustee's Preliminary Investigation Report and Recommendations, at 130 (Aug. 25, 2010).

[7] *Id.* at 131.

[8] 75 Fed. Reg. at 75164.

(and presumably at other depositories). However, "under this approach, every day every clearing member would need to send up to the [DCO] information on each customer's portfolio positions or rights and obligations at that [DCO]."[9] In the event that an FCM were to default to a DCO:

> ...the DCO must treat each customer's swaps positions, and related margin (based on the positions reported [to the DCO by the FCM] as of the day previous to the default) individually, debiting each customer's account with losses attributable to that customer's positions, and crediting each customer's account with gains attributable to that customer's positions. However, if the value of the margin account is reduced below the required level as a result of market fluctuations in the value of the collateral, the margin attributed to each customer would be adjusted accordingly on a pro rata basis.[10]

The third variant on individual segregation described in the ANPR is Moving Customers to the Back of the Waterfall (the "Waterfall Model"). In this context, the term "waterfall" refers to the financial resources available to a DCO to cure a default by a clearing member. The Waterfall Model is "similar to" Legal Segregation, with two modifications:

a. The DCO may use the remaining collateral attributable to each of the defaulting FCM's [cleared swaps] customers as a DCO default resource.
b. Before using the remaining collateral, the DCO must first apply (i) the DCO's contribution to its default resources from its own capital and (ii) the guarantee fund contributions of all members of the DCO.[11]

CME Group recognizes the critical nature of a strong and effective customer-protection model to CFTC-regulated markets, particularly in light of Dodd-Frank's expansion of the CFTC's jurisdiction over cleared swaps. We applaud the CFTC's past history of utilizing an effective regulatory regime in this regard, including development and enforcement of the Baseline Model. Under the CFTC's oversight, FCM insolvencies have been a rarity. LBI, of course, is the most recent instance of an FCM filing for bankruptcy (and the first instance of a joint FCM/broker-dealer insolvency). After LBI's parent company (Lehman Brothers Holdings Inc., or LBHI) filed for bankruptcy and before LBI's filing, LBI's futures customers either transferred their accounts to other FCMs of their own choosing or were part of a "bulk transfer" of customer accounts to another FCM, in accordance with CFTC regulations. None of LBI's futures customers suffered financial losses in connection with its insolvency.[12]

CME Group appreciates that recent events in the OTC markets and the expected growth in client clearing warrant further consideration of methods to enhance customer protections. To be effective, however, any new customer-protection mechanism must not create moral hazard or be cost prohibitive. In addition, any new model should provide a consistent framework across account classes, products and clearing relationships. Furthermore, achieving Dodd-Frank's goals of bringing additional clearing services to the

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[9] *Staff Roundtable on Individual Customer Collateral Protection* ("Roundtable"), at 35-36 (Statement of Robert Wasserman, CFTC Division of Clearing and Intermediary Oversight).

[10] 75 Fed. Reg. at 75164.

[11] *Id.*

[12] Counterparties of various LBHI subsidiaries in non-cleared OTC markets generally did not fare as well as LBI's futures customers, and have filed billions of dollars of claims in alleged losses on OTC derivative contracts in the Lehman bankruptcy cases.

OTC marketplace, increasing competition, and reducing the concentration of risk with a few institutions requires a regulatory system that not only provides appropriate measures to protect the safety of customer funds, but continues to ensure the existence of a well-capitalized and diversified set of FCMs. The FCM community plays an important role in risk management and systemic-risk containment. The objective of customer protection must therefore be balanced with the objective of incentivizing qualified firms to act as FCMs and positioning them to offer cost-effective intermediation services to their customers.

CME Group is very concerned that adopting an individual-segregation model for customer cleared swaps would undermine Dodd-Frank's key principles. Such models would impose significantly higher costs on customers and clearing members, and inject moral hazard into the system at the customer and FCM levels.[13] Depending on the particular characteristics of the proposed segregation model and the extent to which the model is implemented, the increased costs may decrease participation in the CFTC-regulated cleared-swaps market: customers may be unable or unwilling to satisfy substantially increased margin requirements; FCMs would face a variety of increased indirect costs (*e.g.*, staff overheads, new systems, compliance and legal costs) and direct costs (*e.g.*, banking and custodial fees) that they will be incented to pass along to customers. FCMs, however, may be unable to recoup a substantial portion of these costs from customers in the form of execution fees or investment management services (particularly considering the CFTC's proposal to amend Regulation 1.25).[14]

Consequently, smaller FCMs may be forced out of the business, larger FCMs may not be incented to stay in the business, and firms otherwise qualified to act as FCMs may be unwilling to do so if the risk and cost profile of the FCM model is adversely impacted by requirements of individual segregation. This may lead to a larger concentration of customer exposures at fewer FCMs, further increases to margin and guaranty fund requirements, and further increased costs to customers. As further explained below, CME Group believes that Dodd-Frank's statutory purposes can be best accomplished by continuing to utilize the time-tested Baseline Model and providing customers with certain additional disclosures to enable them to make better informed decisions regarding the credit and risk profile of their FCMs.

B. Congressional Intent Regarding Segregation of Customer Funds

Before delving further into potential segregation models, we will address the CFTC's query as to whether, in enacting Dodd-Frank, Congress evinced an intent to adopt a particular segregation model for customers' cleared swaps. Such an analysis begins, of course, with the statutory language.

For more than forty years, Section 4d of the CEA has governed the treatment by FCMs and clearing organizations of collateral received from customers to margin exchange-traded futures contracts. Dodd-Frank made no substantive amendments to these provisions, which are located in Sections 4d(a)(2) and 4d(b). Section 724 of Dodd-Frank did, however, add to the CEA new Section 4d(f), which governs the treatment by FCMs and DCOs of collateral received from customers to margin cleared swaps. As the enclosed chart illustrates, the language of Section 4d(f) parallels the language of Sections 4d(a)(2) and (b), with two exceptions where 4d(f) contains the word "customer", whereas 4d(a)(2) and 4d(b) contain the word "customers."

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[13] "Moral hazard" generally occurs when a party insulated from risk may behave differently than it would behave if it were fully exposed to the risk.

[14] *See* 75 Fed. Reg. 67642 (Nov. 3, 2010).

We think it unlikely that Congress would adopt such a subtle method of moving away from the Baseline Model and directing the use of individually segregated accounts for cleared swaps. In the prior instance when Congress wished to diverge from the Baseline Model, it enacted legislation squarely addressing the issue. Specifically, for derivatives transaction execution facilities (or DTEFs, a registrant category created by the Commodity Futures Modernization Act of 2000), Section 5a(f) of the CEA provides that, "consistent with regulations adopted by the [CFTC], a registered [DTEF] may authorize a [FCM] to offer any customer of the [FCM] that is an eligible contract participant the right to not segregate customer funds of the customer that are carried with the [FCM] for purposes of trading on or through the facilities of" the DTEF.[15]

Also, examination of statutory language is "guided not by a single sentence or member of a sentence, but looks to the provisions of the whole law, and to its object and policy." *Deal v. United States*, 508 U.S. 129, 132 (1993). Section 724 of Dodd-Frank not only added new Section 4d(f) to the CEA, it also amended the U.S. Bankruptcy Code's definition of "commodity contract" to include a swap that is cleared by a DCO, and its definition of "customer" to include an entity that holds a claim against an FCM arising out of the FCM's business for the "commodity contract" account of such entity.[16] Significantly, Dodd-Frank did not amend provisions in the Code that call for *pro rata* distribution to customers in an FCM bankruptcy,[17] a concept that many would contend is incongruous with a system of individually segregated customer accounts.[18] The CFTC's rulemaking authority can only be exercised within the bounds of the policies set in the commodity-broker subchapter of the Bankruptcy Code. See *In re Griffin Trading Co.*, 245 B.R. 291, 302 (Bankr. N.D. Ill. 2000) (finding invalid a CFTC regulation that expanded the Code's definition of "customer property" and changed the distribution priority scheme in the commodity-broker subchapter). Therefore, the fact that these amendments to the Code were made contemporaneously with the adoption of Section 4d(f) weighs against any view that Congress intended a regime of individually segregated accounts for customer cleared swaps.

We are also mindful that statutes should not be applied in ways that would "yield patent absurdity." *Dunn v. Commodity Futures Trading Comm'n*, 519 U.S. 465, 470 (1997). CME Group expects that a significant number of customers with cleared swaps in their account at an FCM will also clear exchange-traded futures and/or options on futures through the same FCM. It is possible, therefore, that an FCM could default to a DCO as a result of a default by a customer in both the cleared-swaps origin and the futures origin. If the CFTC were to adopt an individual-segregation regime for cleared swaps while retaining the Baseline Model for futures, the FCM's cleared swaps customers (who must be eligible contract participants or ECPs,[19] a category that includes financial institutions and investment companies) may

[15] The CFTC did not adopt regulations allowing DTEF customers to opt out of segregation, "in part due to the need to consider related bankruptcy distribution issues." Susan C. Ervin, *The Griffin Trading Case: A Challenge to the CFTC's Bankruptcy Regime*, at p. 5 (Jan. 2001), American Bar Association, Section of Business Law, Committee on Regulation of Futures and Derivatives Instruments, 2000 Annual Winter Meeting.

[16] Section 724(b) of DFA (amending 11 U.S.C. § 761).

[17] 11 U.S.C. § 766(h).

[18] *See, e.g.*, Roundtable at 151-53 (Statement of Ed Rosen, Cleary Gottlieb Steen & Hamilton).

[19] The definition of "eligible contract participant" is in Section 1(a) of the CEA.

receive preferential financial treatment in comparison to its futures customers (which includes non-ECPs who are individual or "retail" customers). We do not believe that Congress intended such anomaly.[20]

C. Costs Arising From "Individual Segregation" Models

The ANPR propounds a litany of questions regarding specific costs and moral hazards that would be imposed on customers, FCMs and DCOs under each individual-segregation model described in the ANPR. As a preliminary matter, we urge the CFTC to consider other viable alternatives that may avoid the costs and moral hazards associated with Full Physical Segregation, Legal Segregation and the Waterfall Model. One alternative worthy of further exploration is an insurance vehicle, similar in concept to the additional account protection beyond SIPC's limits (commonly referred to as "Excess SIPC") offered by broker-dealer firms. We understand that firms have arranged for various types of Excess SIPC coverage, including: (1) "net equity" insurance, which covers each eligible customer account up to the account's total value or net equity; and (2) "aggregate limit" insurance, which is similar to net equity insurance but has a coverage limit per customer account and/or an aggregate limit per firm on the total amount payable for all accounts.

With regard to costs arising from use of Full Physical Segregation, Legal Segregation and the Waterfall Model, many key components of the required analyses are presently unknown (*e.g.*, which cleared-swap customers will qualify for an "end user" exemption from mandatory clearing; the number of customer cleared-swaps accounts that will exist; how the CFTC's proposed individual-segregation models will address customer omnibus accounts of non-clearing FCMs; the number of FCMs that will carry customer cleared-swap accounts). Furthermore, the CFTC is proposing myriad other regulations under Dodd-Frank that may impact costs arising from an individual-segregation regime, but none of those regulations is yet in final form. Calculating costs associated with individual segregation of customer cleared-swaps accounts is, therefore, an exercise in rough approximation.

We do know that cleared swaps will not be limited to asset classes such as interest rate swaps and credit default swaps in which the FCM constituency is largely comprised of firms with large bank affiliates. Rather, cleared swaps will incorporate asset classes such as energy, agricultural and, potentially, foreign exchange, in which all manner of FCMs will participate. We therefore assume that any individual-segregation model for customer cleared swaps will involve a large number of customer accounts, and that most of our FCM clearing members will carry at least some customer cleared-swap accounts.

1. *Impacts to Guaranty Fund and Customer Margin Requirements Common to Full Physical Segregation, Legal Segregation and the Waterfall Model*

All three of the proposed models for individual segregation would have major impacts to DCOs' financial resources packages. A strong financial resources package is essential to a DCO's ability to fulfill its role as risk-bearer of last resort in times of extreme market stress. Financial resources packages generally have two key components: initial margin requirements and guaranty fund deposits. Initial margin is the

[20] *See* Allen & Overy Client Alert, *CFTC Roundtable on Client Collateral Segregation: Does Removing Client Loss Mutualization Make Us Any Safer?* (Oct. 27, 2010) (under the CFTC's proposal for individual segregation for accounts of cleared-swap customers, "in the event of an FCM default, and assuming that the existing collateral protection framework would continue to apply to futures, swap customers would be accorded preferential treatment when compared to other customers of such FCM, a result which may not be entirely consistent with the intentions of Congress in the Act").

first line of defense for the guarantor of an account's performance.[21] Initial margin is a powerful tool in minimizing moral hazard (discussed in Section G below) because it causes the parties that contribute risk to the system to bear most of the costs associated with such risk. Initial margin helps to absorb (i) potential losses an FCM may incur in the event of a customer default, and (ii) potential losses a DCO may face in the event of a clearing member default.

A DCO's guaranty fund is designed to prevent a clearing-member default from posing systemic risk to the DCO's markets. Guaranty fund deposits are required of all clearing members, and generally are calculated based upon each member firm's proportionate share of the risk pool. The balance between the initial margin and guaranty fund components of a DCO's financial resources package can vary, although typically DCOs use very conservative coverage standards for initial margin in order to cover tail events associated with normal market conditions. The guaranty fund is then designed to cover potential risks that exist beyond the coverage of initial margin, which typically arise from extreme tail events associated with extreme but plausible market conditions. CME Clearing presently maintains two separate guaranty funds: one for cleared-only interest rate swaps (the "IRS Guaranty Fund"), and one for all other products and asset classes (the "Base Guaranty Fund").

Full Physical Segregation, Legal Segregation and the Waterfall Model share certain attributes that would create similar impacts to guaranty-fund sizing and customer margin requirements. For purposes of this letter, we use the following assumptions for the mature state of a centrally cleared IRS market and the current state of CME Clearing's other markets:

IRS Guaranty Fund and Initial Margin:

- Estimated cleared notional of $200 trillion
- Estimated initial margin of $500 billion
- Estimated guaranty fund deposits of $50 billion[22]

Base Guaranty Fund and Initial Margin:

- Total initial margin of $80 billion
- Guaranty fund deposits of $2 billion

a. *Guaranty Fund*

Under the Baseline Model, CME Clearing establishes the size of our Base Guaranty Fund by stress testing clearing member's clearing accounts to establish "worst loss" amounts. Each clearing member's clearing accounts are treated as diversified, unitary pools. Because clearing-level customer accounts in this model are generally comprised of multiple underlying customers with diversified exposures, the loss profiles resulting from these stress tests benefit from a diversified portfolio profile.

Switching to Full Physical Segregation, Legal Segregation or the Waterfall Model would cause CME Clearing's approach towards sizing the guaranty fund to lose the benefit of treating each clearing member's clearing-level accounts as diversified, unitary pools. As a result, CME Clearing would likely

[21] The CFTC has issued a proposal to define initial margin as "money, securities, or property posted by a party to a futures, option, or swap as performance bond to cover potential future exposures arising from changes in the market value of the position." 75 Fed. Reg. 77576, 77585 (Dec. 13, 2010).

[22] The estimated size of the IRS guaranty fund will vary depending upon the distribution of customer business at various FCMs. However, $50 billion is a reasonable estimate, with a potential range from approximately $20 billion to approximately $100 billion for an IRS guaranty fund under the Baseline Model.

change to an approach geared toward assessing the largest loss associated with a certain number of the largest individual customer accounts. Currently, we presume that five such customer accounts would be our target, although experience and prudence would be our guide. In any event, our stress-test loss profile of the largest customer accounts would almost certainly generate larger "worst loss" results than under the Baseline Model.

In making this calculation, we utilized the existing CME Clearing risk pool. Based on that assessment, we determined that the Base Guaranty Fund would need to at least double in size (*i.e.*, from approximately $2 billion, to at least $4 billion). All else being equal in the swaps market (*e.g.*, the same distribution of customer exposures across FCMs), this would mean a doubling of the IRS Guaranty Fund from $50 billion to $100 billion.

b. Customer Margin

Adoption of Full Physical Segregation, Legal Segregation or the Waterfall Model would have a broadly similar impact to a DCO's financial resources package in the event of a clearing member default originating in the customer cleared-swap origin. Under the Baseline Model, if such an event were to occur, a DCO would be entitled to use as part of its financial resources package the collateral of the FCM's other futures customers in the commingled account at the DCO to satisfy the FCM's net customer futures obligation to the DCO. Each of the proposed models for individual segregation would change that to a degree. Generally, a DCO would be required to utilize the collateral of the defaulting customer (to the extent determinable) and defaulting clearing member available to the DCO, the DCO's own capital contribution, and the guaranty-fund capital of non-defaulting clearing firms to cure the default. As a result, guaranty-fund capital of all clearing members would bear greater risk than under the Baseline Model. This would create a powerful incentive to rebalance the relative risks that clearing members and customers bear in the financial-resources package by increasing customer margin requirements.

Rebalancing the risks and costs between the guaranty fund and initial margin could be accomplished in two ways. In order to reduce the stress-testing shortfall for any given customer, a DCO could increase initial margins for all cleared-swap customers to indicative stress-test levels, where stress tests are defined as "extreme but plausible" market conditions. In particular, CME Clearing's stress tests go further into the tail of a portfolio's distribution and increase the assumed liquidation horizon for the portfolio. For IRS portfolios, the methodology employed covers extreme, theoretical market moves based on historic data (*e.g.*, those occurring during the market turmoil of late 2008 and early 2009) aimed at capturing extreme tail events specific to a portfolio.[23] The stress-testing methodology has been thoroughly vetted by early adopters of Dodd-Frank's clearing mandate, various buy-side and sell-side participants and clearing members, and was tested on dealer portfolios, customer portfolios and synthetically generated portfolios. With respect to large buy-side portfolios, the shortfall between initial margin and the stress-test results range from 60 to 90 percent. For IRS, this would mean an increase in initial margin from $500 billion to as high as $800 to $900 billion. This approach would allow the IRS Guaranty Fund to be sized as it would be under the Baseline Model, albeit at a significant cost.

Alternatively, a DCO could implement what is traditionally called "concentration" margin, whereby the DCO sets a level of risk at which it would begin to charge higher margins based on indicative stress-test levels. This is a more targeted approach that would seek to redirect the increase in the guaranty fund

[23] While historic data are utilized to gauge the magnitude of stress tests, the stress tests employed for a given portfolio will be based on the risk profile specific to the portfolio (*e.g.*, directional, curve, butterfly).

back to the customer cleared-swap accounts in the clearing system with the largest potential shortfalls. While we currently lack sufficient information to precisely assess an appropriate methodology to incorporate concentration margin into a potential financial-safeguards regime, likely concentration charges would fall in the range of $50 billion to $250 billion. We would make the observation, however, that customers most likely to use cleared swaps to hedge exposures in other markets may bear the brunt of a concentration-margin approach. Any such methodology would need to be appropriately balanced to address concentrated risks, together with risks of other customer-exposure profiles in the clearing system.

2. <u>*Additional Costs of Full Physical Segregation*</u>

   a. *Banking and Settlements*

One key advantage of the Baseline Model is the efficiencies that are derived from a pooled-account structure for the customer origin. This enables a DCO to net all pays and collects across all accounts of an FCM in the customer origin into one net pay or collect amount. CME Clearing relies on this structure to facilitate financial stability in large part by removing debt obligations among market participants as they occur. This is accomplished by independently determining a marking price at the close of each settlement cycle daily for each contract and marking all open positions to that price. Each business day, CME Clearing performs two full settlement cycles, marking to the market once in the late morning (for futures) and once in the late afternoon. Actual settlement of the late morning mark-to-market occurs at mid-day and actual settlement of the late afternoon mark-to-market occurs in the early morning hours of the next day.

Two distinct processes occur during a settlement cycle. Initially, at each settlement cycle, all new trades are captured, cleared and marked-to-market. All open positions are also marked-to-market at this time. Cash settlement occurs for the mark-to-market on open futures positions and the option premium associated with new options positions, known as settlement variation. Simultaneously, forward looking collateral requirements are re-evaluated for all open positions. The combination of these two processes – the cash payments that move between CME Clearing and our clearing members and the resetting of performance bond (or margin) coverage – ensure that all accumulated debt obligations are removed from the system, and that CME Clearing holds sufficient collateral to protect against anticipated losses that clearing members and their customers may accumulate before the next settlement cycle. In times of extreme price volatility, CME Clearing has the authority to perform additional mark-to-market calculations on open positions and call for immediate payment of settlement variation. CME Clearing's mark-to-market settlement system stands in direct contrast to traditional settlement systems implemented by many other financial markets which are not centrally cleared, including OTC markets in which participants regularly assume credit exposure to each other.

CME Clearing has worked with the industry over time to develop a cost-effective, flexible collateral program. Our current collateral program presumes, of course, the existing pooled account structure associated with the Baseline Model. Full Physical Segregation would destroy that structure and require the establishment of a multiplicity of customer accounts at each FCM, DCO, bank, and other depository of customer funds, across asset types. At a minimum, this would involve a substantial increase in customer banking and custody fees.

Consider a scenario where each of 10,000 active cleared-swap customer accounts pledges the following currently accepted asset types, necessitating approximately 10 accounts per customer: cash, U.S.

Treasuries, European Sovereigns, high-grade corporate bonds, foreign exchange, equities and various money-market funds. In order to replicate existing functionality, CME Clearing would have to assess the staffing, systems, and compliance work necessary to support the establishment and maintenance of approximately 100,000 separate customer custody accounts. In assessing these implications, CME Clearing would have to consider issues such as standard operational account maintenance, daily reconciliations, coupon interest and dividend processing, daily deposits and withdrawals, and the potential for different obligations associated with tax reporting. These overheads would likely drive the CFTC-regulated cleared derivatives industry to a "cash with interest and U.S. Treasuries only" model. This would have a profoundly negative impact to the standard revenue model of most FCMs.

Also, the CFTC has indicated its intent to propose regulations in connection with DCO Core Principle D (Risk Management) that provide a mechanism for customer futures to be moved into the customer cleared-swaps origin (and vice versa) for purposes of obtaining margin offsets where available.[24] Under Full Physical Segregation, CME Clearing would be unable to net pay and collect amounts across all accounts in an FCM clearing firm's customer cleared-swaps origin into a single net pay or collect. This would likely undermine certain aspects of CME Clearing's current settlement system. At present, settlement banks approve payments based on the clearing member's status with the bank. Under Full Physical Segregation, however, approval of settlement payments may no longer remain among the settlement bank, clearing member and DCO, but may shift to being among the settlement bank, DCO and each of the clearing member's cleared-swap customers. We believe this would substantially delay the settlement process and may eliminate the ability to perform intra-day settlements for any customer futures positions that have been moved into the customer cleared-swap origin, thereby introducing significant operational risk into the system. Foregoing an intra-day mark-to-market process for futures contracts in the customer cleared-swap origin may also necessitate moving to 2-day margin rather than 1-day margin coverage for such products, which would increase margins by approximately 40 percent.

b. *Financial Reporting and Audits/Compliance*

The CFTC asks for comment regarding additional "compliance activities" that would have to be performed under Full Physical Segregation. At CME Clearing, compliance activities in connection with customer protections and financial oversight of our clearing-member firms are performed primarily by the Audit Department. CME Clearing auditors spend a significant amount of time auditing each of our clearing members, a group that presently includes 53 FCMs.

In general, the Audit Department's current procedures under the Baseline Model are to review all customer-segregated bank accounts to ensure they are properly titled and covered by the requisite segregation acknowledgement letter. Auditors "tie out" every line item included on FCMs' month-end financial computations, as of the audit date. This includes tracing balances to third-party documents such as bank accounts, trade registers, carrying-broker statements and equity runs. CME Clearing auditors reconcile FCMs' daily segregation computations as of the audit date to the official month-end financial statement submitted to CME Clearing to ensure that each FCM has appropriate daily procedures and internal controls. They also review sampling of daily customer-segregation statements to ensure the statements are being completed in a timely fashion, to check for any significant variances, and to ensure that excess segregation is maintained.

[24] *Staff Roundtable on Proposed Rule for Risk Management Requirements for Derivative Clearing Organizations* (Dec. 16, 2010).

Adopting a Full Physical Segregation model would have a dramatic impact on CME Clearing's Audit Department and the financial and regulatory oversight functions they perform (with parallel impacts on our FCM member firms). In Full Physical Segregation, each customer cleared-swap account at each FCM would be required to have its own segregation computation (rather than a "pooled" computation under the Baseline Model); its own account at each DCO, bank and other depository; and its own acknowledgement letter from each depository. Consequently, CME Clearing would have to perform the steps noted above under the Baseline Model separately for each of the thousands of customer cleared-swaps accounts, rather than reviewing 53 customer-segregation computations and 53 bank and DCO reconciliations under the Baseline Model (*i.e.*, one for each FCM clearing member).

This would place a severe burden on the Audit Department's resources and engender delays in completing financial reviews and audits of our FCM member firms. Furthermore, the CFTC would have to rewrite its 1-FR-FCM to provide for separate segregation computations for each customer-cleared swap account. On a related note, FCMs would be required to work with firms that furnish their back-office accounting software to make system changes necessary to support separate segregation statements for each customer cleared-swap account, which we expect would be a costly and time-intensive endeavor.

c. *Increased Staffing, Systems and Related Resource Requirements*

In order to deal with the multiplicity of separate customer accounts created under Full Physical Segregation, CME Clearing would be required to rebuild many of its existing systems and increase staff in all departments, including but not limited to the Financial Unit, the Audit Department and Risk Management. We cannot estimate these cost increases with any precision without more precise factual information regarding the number and nature of separate customer cleared-swap accounts that would exist, but we anticipate that they would be material.

3. *Additional Costs of Legal Segregation*

Because Legal Segregation would not require separately segregated customer accounts, it would not entail the type of additional banking, settlement, financial reporting and audit costs created by Full Physical Segregation. Legal Segregation, however, would require FCMs to report to each DCO on a daily basis information on each cleared-swap customer's portfolio positions or rights and obligations at the DCO. This would require the creation of a new reporting system. As the CFTC is aware, "Large Trader" reports provide information based on account *controller* rather than account *owner* (thereby consolidating many separate accounts into one in the case, for example, of accounts controlled by an investment adviser). The CFTC recently issued a separate proposal that would require the reporting of certain information at the account level (called the Ownership and Control Report, or OCR),[25] and held a roundtable to discuss the OCR proposal and associated costs. We expect that information gleaned by the CFTC in connection with the OCR proposal may be indicative of costs associated with creating a system for FCMs to report account-level data to DCOs on a daily basis.

Moreover, we seriously question the assumption that an FCM will have the wherewithal to provide accurate customer account-level data to DCOs on the eve of its own bankruptcy filing (*i.e.*, the time at which such data would be most critical). The Preliminary Investigation Report and Recommendations of LBI's SIPA Trustee (the "LBI Report") is instructive in this regard. It describes various aspects of the

[25] 75 Fed. Reg. 41775 (July 19, 2010).

"rushed, confused, uncertain and near-panic atmosphere" that engulfed LBI shortly before its bankruptcy filing on September 19, 2008, including but not limited to the following factors:

- After LBHI filed for bankruptcy on September 15, 2008, some employees "simply did not show up for work, or showed up without any incentive" to do work required to wind down LBI's business; and even if the employees had been available, "they would have encountered little direction from management, which was distracted" by other aspects of the insolvency proceedings. (Lehman Report at 65-66.)
- LBI's settlement bank "shut off access to information systems that LBI ... used to monitor account activity." (*Id.* at 60).
- An increasing number of customers were removing their assets and accounts from LBI, particularly in connection with the insolvency proceedings of Lehman Brothers International Europe (or LBIE, LBI's principal European broker-dealer affiliate), and "last minute attempts to move customer accounts...further clouded the picture between LBIE and LBI...." (*Id.* at 34.)

Additionally, CME Group is very concerned that Legal Segregation would adversely impact the ability of DCOs (and bankruptcy trustees) to effect an orderly wind-down process in the event of an FCM default originating from the customer cleared-swap origin. In such circumstances, a DCO would be faced with the operational burdens of disaggregating the customer cleared-swap pooled account into separate accounts for each customer of the defaulting FCM (assuming the DCO could obtain sufficient account-level information from the defaulting FCM), and calculating variation margin payments on a customer-by-customer basis. This would likely delay the transfer or liquidation of positions of non-defaulting customers, whereas current CFTC regulations under the Baseline Model contemplate actions being taken without delay. Such increased operational burdens may adversely impact the proper functioning of DCOs' default-management procedures and thereby increase systemic risk, particularly in times of extreme market turmoil when a DCO may be faced with multiple defaults.

4. *Additional Costs of the Waterfall Model*

The Waterfall Model is the same as Legal Segregation, except that a DCO could in theory use customer cleared-swap collateral to cure a default originating in that customer origin, but only after the DCO exhausted its own capital contribution to the waterfall along with the guaranty-fund deposits of its clearing members. We expect that the Waterfall Model would create the same additional costs and risks as Legal Segregation.

In addition, to preserve its right under the Waterfall Model to use collateral in the customer cleared-swap account of the defaulting FCM to cure a default, a DCO would need to retain such collateral until such time as (i) the defaulting customer is identified, and (ii) losses created by the default are crystallized. This could result in a situation similar to that which occurred in the insolvency proceedings of Lehman Brothers International Europe, where customer collateral was frozen while complex legal and operational issues were sorted through, and customers were forced to deposit additional collateral with their new clearing firms to meet margin requirements associated with transferred positions, in effect having to pay double margins for an extended period of time.

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5. *Optional Models*

Some parties have suggested that customers should be allowed to "opt out" of the baseline model and "opt in" to an individually segregated account. This would be similar to non-cleared OTC markets, where certain participants have negotiated agreements with their counterparties to hold their collateral in segregated accounts at third-party custodians. Use of custodial accounts enables such participants to "substantially reduce or even eliminate credit exposure to [their] swap counterparties,"[26] while paying the extra costs associated with this structure. Counterparties that elect to use third-party custodial accounts in bilateral OTC markets include investment advisers with fiduciary duties to their clients.[27]

The CFTC has also permitted certain institutional customers to use third-party custodial accounts, subject to standards designed to ensure the carrying FCM's access to customer funds in such accounts.[28] This resulted from an SEC interpretation of Section 17(f) of the Investment Company Act of 1940 as barring registered investment companies ("RICs") from using FCMs and futures clearing houses as custodians of fund assets. In 1996, the SEC adopted Rule 17f-6, which permits RICs (with limited exceptions) to deposit customer margin directly with FCMs and DCOs to effect transactions in exchange-traded futures contracts and commodity options. Thereafter, because most RICs no longer were required to use custodial accounts to engage in futures transactions, the CFTC determined that "the use of third-party custodial accounts is no longer justified or appropriate, except in limited cases where the FCM is precluded from holding RIC assets."[29]

Significantly, the SEC has not amended Rule 17f-6 to permit RICs to deposit customer margin directly with FCMs and DCOs to secure transactions in cleared-only derivatives, which are not traded on an exchange.[30] Until such time as the SEC makes such amendments (which would align with Dodd-Frank's purpose of encouraging the clearing of OTC swaps), CME Group suggests that the CFTC consider allowing RICs (and any other fiduciaries not permitted by their regulators to deposit customer margin for cleared-only swaps with FCMs or DCOs) to use third-party custodial accounts for swaps cleared by a DCO, subject to standards designed to ensure the carrying FCM's access to customer funds in such accounts in appropriate circumstances.[31] If the CFTC were to promulgate regulations allowing RICs or other fiduciaries to utilize third-party custodial accounts, we believe those regulations should govern and that DCOs should not be permitted to adopt their own models. This would eliminate the need to address

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[26] Letter from Tudor Investment Corporation (John G. Macfarlane, Vice Chairman, and Stephen N. Waldman, Managing Director and Deputy General Counsel) to the CFTC (Dec. 22, 2010).

[27] *See, e.g.*, Roundtable at 17-19 (Statement of Mark Szycher, General Motors Asset Management).

[28] Financial and Segregation Interpretation No. 10, Treatment of Funds Deposited in Safekeeping Accounts, Comm Fut. L. Rep. (CCH) 7120 (May 23, 1984).

[29] 70 Fed. Reg. 24768 (May 11, 2005).

[30] CME recently obtained no-action relief from the SEC's Division of Investment Management to enable RICs to place and maintain assets with CME or CME clearing members that are FCMs for purposes of meeting margin requirements for certain credit default swaps cleared by CME.

[31] We note that, as the CFTC has observed, "the holding of customer margin in any [third-party custodial] account has and continues to present ... some uncertainty as to the treatment of funds in the event of an FCM insolvency...." 70 Fed. Reg. 5417, 5418 (Feb. 2, 2005). CFTC staff expressed similar concerns during the Roundtable. *See* Roundtable at 155 (Statement of Robert Wasserman) ("What would be non-ratable [under the Bankruptcy Code] is if we endeavored to do [individual segregation] on a voluntary basis, with some customers being protected and some customers not").

questions posed in the ANPR based on the premise of different DCOs adopting different "optional" models.

Costs to any customer electing to use a third-party custodial account would likely be significant. As noted in prior comment letters to the CFTC, the use of such accounts requires the customer to "establish[] procedures and software programs to incorporate these arrangements in their back office systems," and may necessitate "incorporating a 'cushion' in margin levels" to address certain risks unique to third-party custodial accounts.[32] In addition, from the FCM's perspective:

> Third party accounts impose significant costs and expenses, including financing and potential opportunity costs, relative to regular customer accounts. Most notably, these include financing costs associated with covering initial margin requirements for third party account customers at the clearing house level. In addition, there can be increased personnel and legal costs and regulatory exposure associated with maintaining third party accounts relative to regular customer accounts. In this regard, because they require negotiation with both the customer and the custodian, third party accounts generally require a significant amount of additional resources from in-house counsel and typically take a longer period of time to conclude. While the time to negotiate and implement varies, in some circumstances, such negotiations can take weeks or months to complete.[33]

Some categories of costs arising from a customer's election of a third-party custodial account – such as higher margin requirements, wire-transfer fees and certain other operational and administrative costs – could be passed directly through to the customer. Other costs associated with this approach could be subject to negotiation between the customer and its FCM, just as they are now subject to negotiation between counterparties in non-cleared OTC markets that choose to use third-party custodial accounts.

G. Moral Hazard Concerns and Customers Risk-Managing Their FCMs

Adopting Full Physical Segregation, Legal Segregation or the Waterfall Model also creates moral-hazard concerns at the FCM level. In particular, use of these models "could create a disincentive for an FCM to (1) offer the highest level of risk management to its customers if the oversight and management of individual customer risk were to be shifted to the clearing house and (2) continue to carry the amount of excess capital that they do today."[34] It also has been observed that "customers should risk-manage their FCMs, and provide market discipline by doing business with FCMs that pose less risk."[35] Adoption of Full Physical Segregation, Legal Segregation or the Waterfall Model would engender moral hazard at the customer level by isolating them from the credit risk of their FCM, thereby reducing their incentives to perform due diligence when selecting an FCM. The ANPR poses various questions designed to address moral-hazard concerns at the FCM level, and to assist customers in risk managing their FCMs on an initial and ongoing basis.

[32] Letter from Investment Company Institute (Frances M. Stadler, Deputy Senior Counsel) to the Commission (Apr. 4, 2005).

[33] Letter from Futures Industry Association (John M. Damgard, President) to the Commission (Apr. 4, 2005).

[34] Letter from Commissioner Scott D. O'Malia to Thomas Donohue, President of the U.S. Chamber of Commerce (Nov. 3, 2010).

[35] 75 Fed. Reg. at 75165.

1. *FCM Capital Requirements and Risk Management*

The CFTC requests comment on whether current FCM capital requirements are sufficient. The CFTC raised minimum capital requirements for FCMs less than one year ago. In particular, Regulation 1.17 was amended to increase the required minimum dollar amount of adjusted net capital that an FCM must maintain; require the computation of an FCM's margin-based minimum adjusted net capital requirement to incorporate customer and noncustomer positions in OTC derivative instruments submitted for clearing by the FCM to DCOs or other clearing organizations; specify capital deductions for FCM proprietary cleared OTC derivative positions based on deductions required by CFTC regulations for FCM proprietary positions in exchange-traded futures and options contracts; and change the FCM capital computation to increase the applicable percentage of the total margin-based requirement for futures, options and cleared OTC derivative positions in noncustomer accounts from four percent to eight percent.[36] Those measures were appropriate to ensure that FCMs can continue to meet their financial obligations in light of developments in the cleared derivatives markets, including the growing demand for cleared OTC derivative instruments. CME Group does not believe that further mandatory increases to FCM capital requirements are warranted at this time, and we caution against an indiscriminate, broad-brush approach to increased capital requirements that may have the undesirable effects of concentrating customer accounts among fewer FCMs, decreasing competition and further increasing customer costs.

The CFTC also requests comment on whether it or DCOs should take steps to further mitigate the risk of clearing member defaults. We understand that the CFTC's forthcoming rulemaking proposal regarding DCO Core Principles D (Risk Management) and G (Default Rules and Procedures) will address this subject.[37] Also, the types of disclosures described below may provide FCMs with additional incentives to enhance their customer risk-management policies.

2. *Disclosures Regarding "Fellow Customer Risk"*

The CFTC seeks comment on disclosures that may enable customers to better gauge fellow-customer risk at an FCM. CME Group agrees that it is critical to provide customers with the incentive and the ability to make informed decisions regarding the credit and risk profile of their FCMs. Unlike each of the proposed individual-segregation models, the Baseline Model would continue to incentivize customers to select FCMs with strong capital and risk-management practices. With respect to FCM capital, under Regulation 1.10(g)(2), certain information from FCM financial filings (*i.e.*, 1-FR-FCM or FOCUS reports) is

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[36] 74 Fed. Reg. 69279 (Dec. 31, 2009).

[37] Although the CFTC's Proposed Rulemaking for Risk Management Requirements for DCOs has not yet appeared in the Federal Register, the Fact Sheet published by the CFTC regarding that rulemaking proposal contains the following information:

> Proposed Rule 39.13 sets forth the requirements that a DCO would have to meet to comply with Core Principle D (risk management). The proposed rule addresses requirements for a DCO's risk management framework, chief risk officer, measurement of credit exposure (mark to market), margins (including methodology and coverage, independent validation, spread margins, price data, daily review and periodic back tests, and customer margin), and other risk control mechanisms (including risk limits, review of large trader reports, stress tests, swaps portfolio compression, and reviews of clearing members' risk management policies and procedures).
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> ....
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> Proposed Rule 39.16 sets forth the requirements that a DCO would have to meet to comply with Core Principle G (default rules and procedures), including default management plans, default procedures, and actions in the event of a clearing member insolvency.

already publicly available, including the FCM's adjusted net capital, minimum capital requirement under Regulation 1.17, and the amount of its adjusted net capital in excess of minimum net capital requirements.

With respect to fellow-customer risk, the risk that one customer of an FCM will suffer losses because of another customer defaulting to that FCM would come to fruition only if the defaulting customer created a loss of such magnitude that (i) the FCM could not fully satisfy its financial obligations to the DCO as the customer's guarantor, and (ii) the FCM's assets held by the DCO were insufficient to cover the shortfall. CME Group believes that the likelihood of such an event occurring can be measured in large part through disclosure of certain information designed to reveal customer risk in general at an FCM, without disseminating non-public information about individual customers. In that regard, we suggest that the CFTC work with the FCM community to determine the feasibility of, and costs associated with, requiring disclosures by FCMs on a regular basis (perhaps quarterly) as to: (a) whether the FCM was required during the disclosure period to provide notice to the CFTC under Regulation 1.12(f)(3) in connection with a customer or customer omnibus account;[38] and (b) the aggregate dollar amount of any debit balances in customer cleared-swap accounts (or that would be in such accounts but for any credit extended to the defaulting customers by the FCM or its affiliate) above a pre-determined threshold level tied to the FCM's adjusted net capital.

We further suggest that the CFTC consider designing and implementing a mandatory, FCM stress-testing regime for customer accounts, with transparent standards. FCMs would be required to share with each customer the FCM-calculated stress tests result for that particular customer, and FCMs and customers alike would be able to execute the stress tests. At the outset, stress test results could be deemed non-public for a defined period in order to give FCMs and customers an opportunity to verify the data. If certain threshold levels were reached or exceeded, however, the stress test results may be required to be publicly disclosed on a "no names" basis. For example, stress test criteria could be configured such that results would be material and disclosable if they exceeded a pre-defined, threshold percentage of the FCM's adjusted net capital. To avoid (or minimize the likelihood of) such mandatory-disclosure situations, FCMs could request more margin from particular customers. If customers did not want to pay additional margin or have stress-test results from their account made public (even on a no-names basis), they could diversify their FCM relationships and establish an account at an additional FCM. The system would then have more margin and/or more diverse FCM-customer relationships, each of which would be a beneficial outcome.

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[38] Regulation 1.12(f)(3) states, in pertinent part:

> (3) Whenever a registered futures commission merchant determines that an account which it is carrying is undermargined by an amount which exceeds the futures commission merchant's adjusted net capital determined in accordance with §1.17, the futures commission merchant must immediately give telephonic notice, confirmed in writing immediately by facsimile notice, of such a determination to the designated self-regulatory organization and the principal office of the Commission at Washington, DC. This paragraph (f)(3) shall apply to any account carried by the futures commission merchant, whether a customer, noncustomer, omnibus or proprietary account....

CME Group thanks the CFTC for the opportunity to comment on this matter. We would be happy to discuss any of these issues with CFTC staff. If you have any comments or questions, please feel free to contact me at (312) 930-8275 or Craig.Donohue@cmegroup.com; or Lisa Dunsky, Director and Associate General Counsel, at (312) 338-2483 or Lisa.Dunsky@cmegroup.com.

Sincerely,

Craig S. Donohue

Craig S. Donohue

cc: Chairman Gary Gensler (via e-mail)
Commissioner Michael Dunn (via e-mail)
Commissioner Bart Chilton (via e-mail)
Commissioner Jill Sommers (via e-mail)
Commissioner Scott O'Malia (via e-mail)
Ananda Radakrishnan (via e-mail)
Robert Wasserman (via e-mail)
Martin White (via e-mail)
Nancy Liao Schnabel (via e-mail)

Enclosure

CEA § 4d(f): Cleared Swaps

(2) CLEARED SWAPS.—
(A) SEGREGATION REQUIRED.—A [FCM] shall treat and deal with all money, securities, and property of any swaps customer received to margin, guarantee, or secure a swap cleared by or though a [DCO] (including money, securities, or property accruing to the swaps customer as the result of such a swap) as belonging to the swaps customer.
(B) COMMINGLING PROHIBITED.—Money, securities, and property of a swaps customer described in subparagraph (A) shall be separately accounted for and shall not be commingled with the funds of the [FCM] or be used to margin, secure, or guarantee any trades or contracts of any swaps customer or person other than the person for whom the same are held.

(3) EXCEPTIONS.—
(A) USE OF FUNDS.—
(i) IN GENERAL.—Notwithstanding paragraph (2), money, securities, and property of swap customers of a [FCM] described in paragraph (2) may, for convenience, be commingled and deposited in the same account or accounts with any bank or trust company or with a [DCO].
(ii) WITHDRAWAL.—Notwithstanding paragraph (2), such share of the money, securities, and property described in clause (i) as in the normal course of business shall be necessary to margin, guarantee, secure, transfer, adjust, or settle a cleared swap with a [DCO], or with any member of the [DCO], may be withdrawn and applied to such purposes, including the payment of commissions, brokerage, interest, taxes, storage, and other charges, lawfully accruing in connection with the cleared swap.

(B) COMMISSION ACTION.—Notwithstanding paragraph (2), in accordance with such terms and conditions as the Commission may prescribe by rule, regulation, or order, any money, securities, or property of the swaps customers of a [FCM] described in paragraph (2) may be commingled and deposited in customer accounts with any other money, securities, or property received by the [FCM] and required by the Commission to be separately accounted for and treated and dealt with as belonging to the swaps ***customer*** of the [FCM].

CEA §§ 4d(a)(2) and 4d(b): Exchange-Traded Futures

(2) [A FCM] shall, whether a member or nonmember of a contract market ..., treat and deal with all money, securities, and property received by such [FCM] to margin, guarantee, or secure the trades or contracts of any customer of such [FCM], or accruing to such customer as the result of such trades or contracts, as belonging to such customer.

Such money, securities, and property shall be separately accounted for and shall not be commingled with the funds of such [FCM] or be used to margin or guarantee the trades or contracts, or to secure or extend the credit, of any customer or person other than the one for whom the same are held:

Provided, however, That such money, securities, and property of the customers of such [FCM] may, for convenience, be commingled and deposited in the same account or accounts with any bank or trust company or with the clearing house organization of such contract market ..., and that such share thereof as in the normal course of business shall be necessary to margin, guarantee, secure, transfer, adjust, or settle the contracts or trades of such customers, or resulting market positions, with the clearing-house organization of such contract market ... or with any member of such contract market or derivatives transaction execution facility, may be withdrawn and applied to such purposes, including the payment of commissions, brokerage, interest, taxes, storage, and other charges, lawfully accruing in connection with such contracts and trades:

Provided further, That in accordance with such terms and conditions as the Commission may prescribe by rule, regulation, or order, such money, securities, and property of the customers of such [FCM] may be commingled and deposited as provided in this section with any other money, securities, and property received by such [FCM] and required by the Commission to be separately accounted for and treated and dealt with as belonging to the ***customers*** of such [FCM]:

(4) PERMITTED INVESTMENTS.—Money described in paragraph (2) may be invested in obligations of the United States, in general obligations of any State or of any political subdivision of a State, and in obligations fully guaranteed as to principal and interest by the United States, or in any other investment that the Commission may by rule or regulation prescribe, and such investments shall be made in accordance with such rules and regulations and subject to such conditions as the Commission may prescribe.	*Provided further*, That such money may be invested in obligations of the United States, in general obligations of any State or of any political subdivision thereof, and in obligations fully guaranteed as to principal and interest by the United States, such investments to be made in accordance with such rules and regulations and subject to such conditions as the Commission may prescribe.
(5) COMMODITY CONTRACT.—A swap cleared by or through a [DCO] shall be considered to be a commodity contract as such term is defined in section 761 of title 11, United States Code, with regard to all money, securities, and property of any swaps customer received by a [FCM] or a [DCO] to margin, guarantee, or secure the swap (including money, securities, or property accruing to the customer as the result of the swap).	
(6) PROHIBITION.—It shall be unlawful for any person, including any [DCO] and any depository institution, that has received any money, securities, or property for deposit in a separate account or accounts as provided in paragraph (2) to hold, dispose of, or use any such money, securities, or property as belonging to the depositing [FCM] or any person other than the swaps ***customer*** of the [FCM].	(b) It shall be unlawful for any person, including but not limited to any clearing agency of a contract market … and any depository, that has received any money, securities, or property for deposit in a separate account as provided in paragraph (2) of this section, to hold, dispose of, or use any such money, securities, or property as belonging to the depositing [FCM] or any person other than the ***customers*** of such [FCM].