



December 2, 2011

Via Electronic Submission: <https://comments.cftc.gov>

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

Re: Notice of Proposed Rulemaking on Protection of Cleared Swap Customer Contracts and Collateral; Conforming Amendments to the Commodity Broker Bankruptcy Provisions: RIN 3038-AC99

Dear Mr. Stawick:

Managed Funds Association¹ is submitting this letter to supplement comments we previously submitted² to the Commodity Futures Trading Commission (the “**Commission**”) on its proposed rules on “Protection of Cleared Swap Customer Contracts and Collateral; Conforming Amendments to the Commodity Broker Bankruptcy Provisions” (the “**Proposed Rules**”). MFA is a strong supporter of efforts to reduce systemic risk, including by transitioning the over-the counter (“**OTC**”) derivatives markets to greater central clearing.³ In addition, MFA

¹ Managed Funds Association (“**MFA**”) represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent and fair capital markets. MFA, based in Washington, DC, is an advocacy, education and communications organization established to enable hedge fund and managed futures firms in the alternative investment industry to participate in public policy discourse, share best practices and learn from peers, and communicate the industry’s contributions to the global economy. MFA members help pension plans, university endowments, charitable organizations, qualified individuals and other institutional investors to diversify their investments, manage risk and generate attractive returns. MFA has cultivated a global membership and actively engages with regulators and policy makers in Asia, Europe, North and South America, and all other regions where MFA members are market participants.

² See MFA’s comments on the Commission’s Notice of Proposed Rulemaking on “Protection of Cleared Swap Customer Contracts and Collateral; Conforming Amendments to the Commodity Broker Bankruptcy Provisions”, 76 Fed. Reg. 33818 (Jun. 9, 2011) filed with the Commission on August 8, 2011, available at: <http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=48013&SearchText=> (“**MFA Proposed Rule Letter**”); see also MFA’s comments on the Commission’s Advanced Notice of Proposed Rulemaking on “Protection of Cleared Swap Customers Before and After Commodity Broker Bankruptcies”, 75 Fed. Reg. 75162 (Dec. 2, 2010) filed with the Commission on January 18, 2011, available at: <http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=27165&SearchText=>.

³ See MFA’s comments on the Commission’s Notice of Proposed Rulemaking on “Governance Requirements for Derivatives Clearing Organizations, Designated Contract Markets, and Swap Execution Facilities; Additional Requirements Regarding the Mitigation of Conflicts of Interest”, 76 Fed. Reg. 722 (January 6, 2011) filed with the Commission on March 7, 2011, available at: <http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=31117&SearchText=>; MFA’s comments on the Commission’s Notice of Proposed Rulemaking on “Risk Management Requirements for Derivatives Clearing

strongly supports the goals of Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act to enhance transparency and reduce risk in the swap markets, including the segregation of collateral for cleared swaps.⁴ Accordingly, like others in the industry, we are very troubled by the recent bankruptcy of, and other events related to, MF Global, Inc. (“**MF Global**”), which have resulted in a delay in the return of segregated customer assets, material concerns that customers have incurred associated losses, and allegations of misuse or misplacement of customer funds.⁵ Thus, in the context of the Commission’s overall reform efforts, we offer some additional thoughts on customer protection in the swaps and futures markets to assist the Commission in its consideration of the lessons learned from the MF Global situation.

I. General

MFA applauds the Commission’s prompt response to the MF Global matter and decision to open an investigation into whether the Commodity Exchange Act or Commission regulations were violated.⁶ These events have caused many market participants, including MFA’s members, to question what framework is best suited to prevent similar events from occurring in the future. In the absence of greater knowledge about what events precipitated the delayed return of, and potential losses associated with, MF Global’s segregated customer assets, our views are still evolving with respect to certain provisions within the Proposed Rules and other Commission regulations that may have a bearing on the MF Global matter. However, MFA members, which are significant participants in the OTC derivatives markets, are actively reviewing and evaluating these issues. We hope to be helpful to the Commission as it considers the Proposed Rules and other relevant rulemakings in light of the MF Global developments.

Organizations”, 76 Fed. Reg. 3698 (Jan. 20, 2011) filed with the Commission on March 21, 2011, available at: <http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=32003&SearchText=>; MFA’s comments on the Commission’s Notice of Proposed Rulemaking on “Requirements for Processing, Clearing, and Transfer of Customer Positions”, 76 Fed. Reg. 13101 (Mar. 10, 2011) filed with the Commission on April 11, 2011, available at: <http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=35520&SearchText=>; and MFA’s comments on the Commission’s Notice of Proposed Rulemaking on Customer Clearing Documentation and Timing of Acceptance for Clearing”, 76 Fed. Reg. 45730 (Aug. 1, 2011) and the Commission’s Notice of Proposed Rulemaking on “Clearing Member Risk Management”, 76 Fed. Reg. 45724 (Aug. 1, 2011) filed with the Commission on September 30, 2011, available at: <http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=48444&SearchText=>.

⁴ S. Rep. No. 111-176 at 32 (2010), available at <http://www.gpo.gov/fdsys/pkg/CRPT-111srpt176/pdf/CRPT-111srpt176.pdf>.

⁵ On October 31, 2011, MF Global Holdings Ltd. filed for bankruptcy. During the due diligence process by a potential acquirer, where the acquisition would have averted the bankruptcy filing, it was discovered that significant amounts of customer assets were missing from MF Global’s segregated customer accounts. The exact amount of customer assets allegedly lost or misplaced is unknown, but current estimates are \$1.2 billion.

⁶ Commission Press Release “CFTC Commissioner Jill E. Sommers to Act as Senior Commissioner for the Agency in Any Matters Relating to the Bankruptcy of MF Global, Inc.” dated November 10, 2011.

II. Reevaluating Segregation Models for Cleared Swaps

MFA previously submitted a comment letter in response to the Proposed Rules,⁷ in which we supported the proposed Complete Legal Segregation Model.⁸ In that letter, we agreed with the Commission that the Complete Legal Segregation Model provided superior protections when compared to the Legal Segregation with Recourse Model and the Futures Model.⁹ Although MFA still believes that the Complete Legal Segregation Model has more robust segregation protections and may facilitate portability better than the other two models, in light of the emerging facts surrounding MF Global, we intend to reexamine this model as well as other alternatives, including the full physical segregation model,¹⁰ for the protection of customer assets for cleared swaps.

In addition, MFA strongly urges the Commission to retain the flexibility to consider each of the following options: (1) adopting the full physical segregation model for cleared swaps; (2) adopting the Complete Legal Segregation Model;¹¹ or (3) conducting an impartial study of the additional costs and the benefits provided to customers associated with the Complete Legal Segregation Model as compared to the full physical segregation model to determine which model is more suitable. MFA will continue to monitor the MF Global developments, and we hope to maintain an open dialogue with the Commission about these issues. As appropriate, MFA will provide updated views on the Proposed Rules, once more information is known.

MFA recognizes that the fact-finding related to MF Global has just begun and that it may be many months before the Commission can make a final determination as to whether violations occurred. We urge the Commission to wait until the facts are clearer and there has been sufficient policy debate before proceeding with rules related to segregation of collateral for cleared swaps. However, we also are not suggesting that the Commission wait for definitive answers on every aspect of the MF Global failure before proceeding with rulemakings related to the protection of customer collateral. Rather, we are suggesting that given the unprecedented

⁷ *Supra* note 2.

⁸ See MFA Proposed Rule Letter at 2, where we stated our belief that the Complete Legal Segregation Model provided “a proper level of protection for customers’ assets should another customer of an FCM default” and allowed for “efficient portability of customer positions and related collateral in the event of a default by an FCM or one of its customers”.

⁹ *Id.*

¹⁰ By “full physical segregation”, we mean that an independent third party custodian holds the collateral of each individual customer in an account separate from the assets of a futures commission merchant’s (“FCM”) other customers, and the relevant FCM is prohibited from accessing the segregated customer assets, except under very limited circumstances (*e.g.*, the customer’s default), such circumstances to be set forth in a tri-party account control agreement (or similar document with equal effect). Perhaps, this model may be further strengthened by requiring the separate accounts to be in the name of the individual customer, and not the FCM, while still giving the FCM full rights to access the account in the event of a customer default.

As the Commission is aware, full physical segregation would afford cleared swaps customer a level of protection and transparency with respect to collateral posted by such customer that is similar to those of collateral posted with respect to uncleared swaps at a third party custodian.

¹¹ The Complete Legal Segregation Model may expedite the move to central clearing.

nature of the events surrounding MF Global and the renewed significance of the segregation rules, it is critical that the Commission evaluate the swap collateral rules in light of the new information. Once the Commission knows more facts, it can determine more conclusively the relative merits of adopting the Complete Legal Segregation Model, the full physical segregation model or protections in other areas.

In addition, MFA is not suggesting that the Commission delay other rulemakings. In particular, we wholeheartedly encourage the Commission to continue adopting and implementing other important final rules that are unrelated to the segregation of customer collateral for cleared swaps.

III. Examine Customer Protections for Futures

In light of the MF Global situation, we feel it is also appropriate to re-examine the protections available to participants in the futures market, and to assess the appropriate balance between the costs of enhanced protections versus the costs to investors and the market as a whole of a segregation failure. Once the Commission has more information about the events that led to the MF Global failure, we would recommend that as the Commission did when considering segregation rules for swaps, they hold one or more roundtables to ensure full consideration of the lessons learned, and to assess whether further protections of the collateral of futures customers are appropriate.

MFA members believe that the events of MF Global warrant careful analysis and should inform future regulatory decisions. MFA appreciates the Commission's consideration of these supplemental comments on the Proposed Rules. We would be pleased to meet with the Commission members or staff to discuss our comments. If the Commission members or staff have any questions, please do not hesitate to call Carlotta King or the undersigned at (202) 730-2600.

Respectfully submitted,

/s/ Stuart J. Kaswell

Stuart J. Kaswell
Executive Vice President, Managing Director &
General Counsel

cc: The Hon. Gary Gensler, Chairman
The Hon. Jill E. Sommers, Commissioner
The Hon. Bart Chilton, Commissioner
The Hon. Scott D. O'Malia, Commissioner
The Hon. Mark P. Wetjen, Commissioner