clear to trade

January 16, 2018

Submitted via: CFTC website: http://comments.cftc.gov

Christopher Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafeyette Centre
1151 21st St., N.W.
Washington, D.C. 20581

Re: "Proposed Order and Request for Comment on Application for Exemption From Certain Provisions of the Commodity Exchange Act Regarding Investment of Customer Funds and From Certain Related Commission Requirements," 82 *Fed. Reg.* 59586 (December 15, 2017).

Dear Mr. Kirkpatrick:

Eurex Clearing AG ("Eurex Clearing") appreciates the opportunity to comment on the Commodity Futures Trading Commission's ("Commission") notice in the *Federal Register*, entitled, "Proposed Order and Request for Comment on Application for Exemption From Certain Provisions of the Commodity Exchange Act Regarding Investment of Customer Funds and From Certain Related Commission Requirements," 82 *Fed. Reg.* 59586 (December 15, 2017) ("Notice"). The Notice proposes to grant an exemption to the requesting derivatives clearing organizations ("DCOs") to permit them to invest futures and swap customer funds in certain categories of euro-denominated sovereign debt and to expand the categories of counterparties and depositories that may be used in connection with those investments. Eurex Clearing supports granting the proposed relief, and requests that it be included within the class of DCOs being granted the proposed exemptive relief.

I. Eurex Clearing

Eurex Clearing is one of the world's largest clearinghouses for euro-denominated instruments.[1] Eurex Clearing was formed in 1998 as the clearinghouse for the Eurex Deutschland and Eurex Zürich AG exchanges. Eurex Clearing acts as the central counterparty ("CCP") for all Eurex transactions as well as for the Frankfurter Wertpapierbörse (the Frankfurt Stock Exchange), the Irish Stock Exchange; Eurex Repo GmbH; and Eurex Bonds GmbH as well as for OTC Interest Rate Swaps and Securities Lending transactions. Eurex Clearing on February 1, 2016, was granted registration by the Commission as a DCO to clear swaps subject to the requirements of Commission Rule 39.5(a)(2).[2]

[1] Eurex Clearing is located at Mergenthalerallee 61, 65760 Eschborn, Germany.
[2] Eurex Clearing may commence clearing swaps under its DCO registration following a demonstration of its capability to provide straight-through-processing of cleared swaps transactions.

Eurex Clearing offers to clear swaps as a DCO and generally accepts Euro and Euro-denominated securities as collateral on such cleared swaps. [3] As discussed in greater detail below, Eurex Clearing faces the same issues highlighted in the Notice with respect to the present limitations of Commission Rule 1.25 and, although not included in the proposed exemptive order, is similarly situated to those DCOs that are included.

Eurex Clearing supports the proposed exemptive order, but suggests two modifications. First, Eurex Clearing believes that its inclusion within the scope of the proposed exemption would benefit Eurex Clearing's members and their customers, and would be in the public interest. Accordingly, for the reasons discussed in greater detail below Eurex Clearing, through this comment letter, requests that it be included within the scope of the exemptive relief proposed in the Notice in connection with its clearing of swaps as a registered DCO.[4] In addition, Eurex Clearing believes that the condition of the exemptive relief that limits to 60 days the dollar-weighted average of the time-to-maturity of the portfolio of direct investments in the covered foreign sovereign debt should be lengthened to two-years and that the relief should clarify that the asset concentration limits of Rule 1.25 do not apply, the same as for U.S. government securities.

II. Background

As the Notice explains, Commission Regulation 1.25(a)(2) sets forth the investments in which DCOs may invest customer funds.[5] Before its amendment in 2011, Rule 1.25 permitted the investment of customer funds in foreign sovereign debt. The Commission amended Rule 1.25 in 2011, among other things, removing foreign sovereign debt as a permitted investment for segregated customer funds.[6] In doing so, however, the Commission stated that,

> it would consider permitting foreign sovereign debt investments (1) to the extent that the petitioner has balances in segregated accounts owed to customers or clearing member futures commission merchants in that country's currency and (2) to the extent that the sovereign debt serves to preserve principal and maintain liquidity of customer funds as required for all other investments of customer funds under Regulation 1.25.[7]

The Notice responds to a petition under section 4(c) of the Act by several affiliated DCOs ("Petitioners"), which if granted, would permit, subject to several conditions, the sovereign debt

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[3] Eurex Clearing's registration as a DCO only applies to its clearing of swaps. The exemptive relief, and Eurex Clearing's request to be included thereunder only applies with respect to its activities as a registered DCO, that is for the clearing of swaps to members subject to Section 4d of the Act. Section 4d of the Act, Commission Rule 1.25 thereunder, and this exemption therefrom are inapplicable to the investment of funds or collateral of non-U.S. persons related to cleared swaps.

Eurex Clearing also operates as a foreign clearinghouse when clearing futures contracts for the Eurex exchanges. Rule 1.25 and this requested relief therefore is inapplicable to Eurex Clearing's operation as the clearing organization of a foreign board of trade and its clearing of foreign futures and options on futures.

[4] The proposed exemptive relief would apply to Eurex Clearing once Eurex Clearing begins clearing subject to the conditions of its Registration Order rather than under the provisions of CFTC Letter 16-04.

[5] Commission Rule 22.3(d) applies to investments by DCOs of cleared swaps customer funds. Commission Rule 22.3(d) incorporates by reference Rule 1.25.

[6] See, "Investment of Customer Funds and Funds Held in an Account for Foreign Futures and Foreign Options Transactions," 76 *Fed Reg* 78776, 78782 (Dec. 19, 2011). ("2011 Amending Notice")

[7] Id.

of the Republic of France and of Germany, whether purchased directly or indirectly through repurchase transactions, to be acceptable investments of segregated customer funds.

III. The Proposed Order

The Notice proposes to exempt the sovereign debt of France and Germany subject to the following conditions:

1. Investments of customer funds in these instruments must be made with euro customer cash. The Commission explained that this limitation is appropriate because it was the requirement prior to the amendment of Rule 1.25 in 2011 removing foreign sovereign debt as a permitted investment. This limitation protects customers from cross-currency risks from the investment in foreign sovereign debt.

2. The DCOs may only invest in the permitted foreign sovereign debt if the two-year credit default spread of the issuing sovereign is 45 basis points or less. The Commission explained that the Commission intends that the expanded investments permitted under the exemption should have a similar risk profile to those that currently are permitted. The credit default spread of this condition is within the range that U.S. sovereign debt has traded during the last five years. If a permitted foreign sovereign debt instrument exceeds this amount, the DCO could not enter into new transactions for the instrument.

3. The dollar-weighted average of the time-to-maturity of each DCO's portfolio of direct investments in each foreign sovereign's debt may not exceed 60 days. Direct investments are purchases that are not paired with a contemporaneous agreement to resell the security.

4. A DCO may use segregated customer funds to enter into repurchase agreements for permitted foreign sovereign debt only if the counterparty is: (i) a foreign bank that qualifies as a permitted depository under Commission Regulation 1.49(d)(3) and that is located in a money center country or within the eurozone (ii) a securities dealer located in a money center country and regulated by a national financial regulator or (iii) the European Central Bank, the Deutsche Bundesbank, or the Banque de France. The Commission believes that limited counterparties of reverse repos to these entities will appropriately reduce the risk of the transaction.

5. The DCO may hold customer securities purchased under a repurchase agreement with a depository that does not meet the requirements of Commission Regulation 1.25(d)(7) only if the depository meets the location and qualification requirements contained in Commission Rule 1.49(c) and (d) and if the account complies with the requirements of Commission Regulation 1.26.

6. The DCOs must continue to comply with all other requirements in Commission Regulation 1.25, including but not limited to the counterparty concentration limits in Commission Regulation 1.25(b)(3)(v), and other applicable Commission regulations.

IV. The exemption is in the public interest

Eurex Clearing supports the proposed exemptive relief and agrees with the Commission and with the Petitioners that granting the exemptive relief would be in the public interest.

A. The covered sovereign debt meets the Commission's criteria

As discussed above, the Commission noted in the Amending Notice that it might consider reinstating the ability to invest in foreign sovereign debt to the extent that a DCO held segregated fund balances in the currency of the sovereign debt and the debt is consistent with "the objectives of preserving principal and maintaining liquidity, as required by Regulation 1.25." The sovereign debt of France and Germany ("Covered Sovereign Debt") permit access to funds in as timely a manner as U.S. government securities and has similar levels of risk of default, liquidity, and volatility. Thus, inclusion of the Covered Sovereign Debt through the exemptive relief would meet the objectives of Rule 1.25.

1. Default risk, liquidity, and volatility

The Notice concludes that the Petitioners have demonstrated that "the credit, liquidity, and volatility characteristics [of the Covered Instruments] . . . are comparable to US Government Securities, which are permitted investments under the Act and Regulation 1.25."[8] The Commission bases its conclusion on data relating to comparative historic spreads on credit default swaps for the three nations. In addition, the Petitioners provided data on the amount of outstanding marketable French and German debt and the daily transaction value of the repo markets for such debt. Data on daily changes to the sovereign debt yields demonstrate that the price stability of French and German debt is comparable to that of the U.S.. These data support the conclusion that the sovereign debt of France and Germany would serve to preserve principle and maintain liquidity of customer funds as required of Rule 1.25 permitted investments.[9] Eurex Clearing agrees with the Commission's conclusions that the Covered Sovereign Debt is comparable to that of U.S. government securities and that inclusion of the Covered Sovereign Debt as a permitted investment is therefore in accordance with the objectives of Rule 1.25.

2. Duration and concentration limits

The Commission proposes to limit the length-to-maturity of direct investments in the Covered Sovereign Debt to an average of the time-to-maturity of the portfolio of direct investments in each type of Covered Sovereign Debt to 60 days or fewer. The Commission explains that it is

> proposing to limit the length to maturity of direct investments in Designated Foreign Sovereign Debt to limit permitted investments to those with a lower risk profile. Specifically, the proposed order requires each of the ICE DCOs to ensure that the dollar-weighted average of the time-to-maturity of their portfolio of direct investments in each type of Designated Foreign Sovereign Debt does not exceed 60 days. This restriction is consistent with Securities and Exchange Commission requirements for money market mutual funds and ensures that the ICE DCOs will not hold Designated Foreign Sovereign Debt investments on a long-term basis, and that the investments will mature relatively quickly, providing the ICE DCOs with access to euro cash. The Commission believes that the liquidity timing needs of money market mutual funds are an appropriate analogue

[8] Notice at 59588
[9] Id. at 59588.

to those of a DCO in this instance and that the 60-day time-to-maturity limit will further limit the risks of investments in Designated Foreign Sovereign Debt. (footnote omitted).[10]

This conclusion is contrary to Rule 1.25's generally applicable duration requirement. The time-to-maturity requirement under Commission Rule 1.25(b)(4)(i) for a portfolio of permitted investments is 24 months, except for investments in money market funds. The Commission analogizes Covered Sovereign Debt to money market funds, which have a much shorter time to maturity requirement. Eurex Clearing believes that a longer time to maturity would be more appropriate for the following reasons.

The Commission has concluded that the default risk, liquidity, and volatility of the Covered Sovereign Debt is comparable to that of U.S. government securities. Accordingly, Eurex Clearing believes that for purposes of time-to-maturity of the portfolio, Covered Sovereign Debt should be treated the same as U.S. government securities, and that the general 24-month limitation therefore should apply. Imposition of the much shorter 60-day period will make far less practicable a DCO's direct investment in the Covered Sovereign Debt. In this regard, it should be noted that, like Rule 1.25(b)(4)(i), Regulation (EU) 648/2012 ("EMIR") imposes a time-to-maturity requirement applicable to the portfolio of investments made with customer segregated funds. Like Commission Rule 1.25(b)(4)(i), that period is 24 months.[11] Eurex Clearing believes that the Commission should apply the same 24-month period to the Covered Sovereign Debt as would apply under EMIR and as the Commission applies to U.S. government securities under Rule 1.25.

In addition to duration limits, Commission Rule 1.25(b)(3) imposes limits on the concentration of certain instruments which may be held in a portfolio. Under Commission Rule 1.25(b)(3)(i) investments in U.S. government securities are not subject to a concentration limit. Under Commission Rule 125(b((3)(iii), repurchase and reverse repurchase securities are combined with the concentration limits of direct investments in securities. The Notice provides that "DCOs must continue to comply with all other requirements in Commission Regulation 1.25, including but not limited to the counterparty concentration limits in Commission Regulation 1.25(b)(3)(v), and other applicable Commission regulations.[12] Insofar as the Commission has determined that "the credit, liquidity, and volatility characteristics [of the Covered Sovereign Debt instruments] . . . are comparable to US Government Securities," Eurex Clearing asks the Commission to clarify that Covered Sovereign Debt, like U.S. government securities, is not subject to an asset-based concentration limit.

3. Counterparty and depository conditions

The Commission proposes in the exemptive order to provide relief (subject to conditions) relating to acceptable counterparties and depositories. This relief is necessary in order to make investments by a DCO in the Covered Sovereign Debt practicable. In the absence of this further relief, investment by CPOs in repurchase and reverse repurchase in these instruments would be severely restricted. To this end, the Commission is proposing to permit the counterparty of such transactions to be a foreign bank that qualifies under Commission Rule 1.49(d)(3) and that is

[10] Id. at 59589.

[11] Annex II Nr. 1 (c) Commission Delegated Regulation (EU) No 153/2013 of 19 December 2012 supplementing Regulation (EU) No 648/2012.

[12] Notice at 59590

located either in a money center country or which has adopted the euro as its currency; certain regulated securities dealers, and the European Central Bank, the Deutsche Bundesbank, or the Banque de France. In addition, the Commission is proposing that these transactions be able to be held by depositories that qualify under Rule 1.49. Eurex Clearing supports this relief and the associated conditions. The conditions apply comparable regulatory requirements to the market for Covered Sovereign Debt and will facilitate DCOs entering into these transactions.

V. Inclusion of Eurex Clearing is in the public interest

As discussed above, Eurex Clearing, as a DCO, clears swaps, including euro-denominated swaps. Permitting investment in Covered Sovereign Debt furthers responsible risk management, particularly with respect to euro-denominated swaps. It is in the public interest to enable Eurex Clearing to invest in Covered Sovereign Debit considering Eurex Clearing's existing investment practices and policies and its long-standing history of investing in such instruments with respect to operation of its clearinghouse. Absent inclusion in the exemptive relief, Eurex Clearing would be precluded from investing in Covered Sovereign Debt, an outcome which is contrary to efficient risk management, especially for a clearinghouse with long and deep roots in the Euro-zone.

Moreover, inclusion of Eurex Clearing in the scope of relief is in the interest of customers. Investing customer funds in the Covered Sovereign Debt would pose less risk than the available alternative—holding such funds in unsecured demand accounts at commercial banks. Moreover, customers will be subject to cross-currency risk if the euro funds that they deposit as collateral may not be invested in Covered Sovereign Debt. For this reason, it is in the interest of customers that Eurex Clearing be included within the scope of the relief.

VI. Inclusion of Eurex Clearing is in accordance with the section 4(c) criteria

Section 4(c)(1) provides that the Commission may exercise its exemptive authority "in order to promote responsible economic or financial innovation *and fair competition.*" The Commission is also required under Section 15 of the Act "to endeavor to take the last anticompetitive means of achieving the objectives of the Act . . . in issuing any order." The Commission's issuance of this exemptive order under section 4(c) therefore should take into consideration the order's effect on competition. Unless included in this relief, Eurex Clearing would be at a competitive disadvantage. Accordingly, Eurex Clearing should be included within the scope of the relief unless there is a specific and compelling regulatory reason otherwise.

Inclusion of Eurex Clearing within the exemptive relief meets the specific section 4(c)(2) criteria.[13] Section 4(c)(2) provides that the Commission may grant exemptions that would be consistent with the public interest, apply to appropriate persons and that will not have a material adverse effect on the ability of the Commission or any contract market to discharge its regulatory or self-regulatory duties under this Act. For the reasons discussed above, including Eurex Clearing within the final order granting exemptive relief is in the public interest. And, as the Commission concluded in the Notice, "the Commission does not believe that any of the section 4(c)(2) exceptions would prevent a grant of the requested exemption."

[13]See section 4 (c) of the Act.

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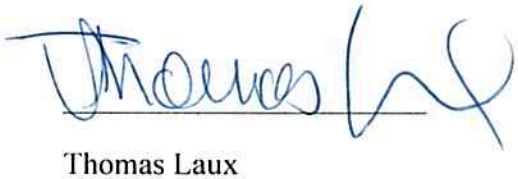
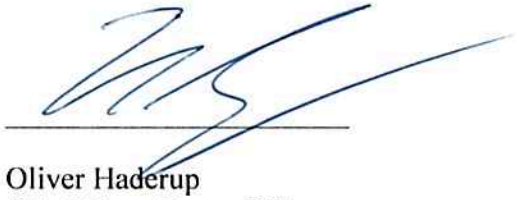
For the reasons discussed in this letter, Eurex Clearing supports the Commission granting the requested exemption to permit DCOs to invest customer funds in the sovereign debt of the Republic of France and of Germany. As discussed above, Eurex Clearing agrees with the conclusion, supported by the data provided, that the Covered Sovereign Debt "has credit, liquidity and volatility characteristics that are comparable to U.S. Government Securities, which are permitted investments under the Act and Regulation 1.25." Following from that conclusion, Eurex Clearing requests that the condition of the Order relating to time-to-maturity of the portfolio of investments be lengthened from 60 days to 24 months, the same as for U.S. government securities and the period which applies to Eurex Clearing under European Union regulation. Finally, for the reasons discussed above, Eurex Clearing requests that it be included with the scope of the final exemptive Order issued by the Commission. The inclusion of Eurex Clearing within the scope of the Order is in the public interest and is in accordance with the criteria of section 4(c) of the Act.

Eurex Clearing appreciates the opportunity to comment upon this important issue. Please contact the undersigned at +49 69 211-15075, or our outside counsel, Paul M. Architzel of Wilmer Cutler Pickering Hale and Dorr LLP at (202) 663-6240 if we can provide any additional information.

Respectfully submitted,



Thomas Laux
Member of the Executive Board



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