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Mr. Christopher Kirkpatrick July 13, 2020
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Re: *Part 190 Bankruptcy Regulations (RIN 3038-AE67)*

Dear Mr. Kirkpatrick:

The Investment Company Institute[1] appreciates the opportunity to provide comments to the Commodity Futures Trading Commission ("Commission") on the Commission's proposal ("Proposal") to update its Part 190 regulations.[2] Part 190 governs the liquidation of a "commodity broker," including a futures commission merchant (FCM) or a derivatives clearing organization (DCO). In conjunction with the Commission's segregation requirements, Part 190 provides critical protections to the broad spectrum of commodity brokers' end-user customers, including ICI's members.

ICI applauds the Commission's focus on enhancing customer protections and bringing much needed clarity and modernization to the commodity broker liquidation process. Additionally, ICI supports the Commission's intention to establish new regulations regarding the liquidation of a DCO, especially in light of the implementation of the clearing requirements under the Dodd-Frank Act and the enactment of the Orderly Liquidation Authority (OLA) special resolution regime. We are concerned, however, that certain aspects of the Proposal would harm public customers and cause uncertainty and market

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[1] The Investment Company Institute (ICI) is the leading association representing regulated funds globally, including mutual funds, exchange-traded funds (ETFs), closed-end funds, and unit investment trusts (UITs) in the United States, and similar funds offered to investors in jurisdictions worldwide. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. ICI's members manage total assets of US$24.8 trillion in the United States, serving more than 100 million US shareholders, and US$6.5 trillion in assets in other jurisdictions. ICI carries out its international work through ICI Global, with offices in London, Hong Kong, and Washington, DC.

[2] *Bankruptcy Regulations*, 85 Fed. Reg. 36000 (June 12, 2020), *available at* https://www.govinfo.gov/content/pkg/FR-2020-06-12/pdf/2020-08482.pdf ("Proposal"). The Commission explains that the Proposal benefits from a model set of Part 190 rules submitted in 2017 by the Part 190 Subcommittee of the Business Law Section of the American Bar Association ("ABA recommendations"). Except as discussed in this letter, ICI generally supports the implementation of the ABA recommendations.

disruption in a time of stress. We urge the Commission to address these concerns before adopting final rules.

I. Background and Executive Summary

ICI's members—including US registered investment companies, such as mutual funds, ETFs, and other funds that are regulated under the Investment Company Act of 1940 ("registered funds"), and non-US regulated funds[3] (together with registered funds, "regulated funds")—use derivatives in a variety of ways. Derivatives are a particularly useful portfolio management tool in that they offer regulated funds considerable flexibility in structuring their portfolios. For example, a regulated fund may use derivatives to hedge its positions or certain risks they present, equitize cash that it cannot immediately invest in direct equity holdings, manage its cash positions, and adjust portfolio duration, all in accordance with the investment objectives stated in the regulated fund's prospectus.

ICI accordingly has a strong interest in the safety and soundness of the derivatives markets, including the protection of customer collateral and funds. Robust customer protection is critical to allow ICI's members to transact in the derivatives markets consistently with their obligations under applicable law and their duties to clients. For example, as fiduciaries to their clients, advisers to regulated funds require strong protections for fund collateral when funds trade in the derivatives markets. Registered funds also must ensure that their collateral arrangements satisfy the custody restrictions of the Investment Company Act of 1940.[4]

When transacting in uncleared swaps, registered fund advisers may satisfy their fiduciary obligations, and the fund's regulatory requirements to protect fund assets, by using tri-party custody arrangements. These arrangements ensure that the initial margin posted by the fund is isolated from the estate of the swap counterparty and thus subject to neither the fraud risk of the swap counterparty nor any kind of fellow customer risk. When transacting in cleared derivatives, by contrast, funds have virtually no ability to use contractual measures to segregate their margin or funds or to otherwise mitigate fraud or

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[3] "Non-US regulated funds" refer to funds that are organized or formed outside the United States and are substantively regulated to make them eligible for sale to retail investors, such as funds domiciled in the European Union and qualified under the UCITS Directive (EU Directive 2009/65/EC, as amended), Canadian investment funds subject to National Instrument 81-102, and investment funds subject to the Hong Kong Code on Unit Trusts and Mutual Funds.

[4] Under the Investment Company Act, registered funds are required to custody their assets in accordance with Section 17 of the Investment Company Act. Nearly all registered funds use a US bank custodian for domestic securities although the Investment Company Act permits other limited custodial arrangements. In addition to Section 17, the SEC has adopted six separate custody rules for the different types of possible custody arrangements: Rule 17f-1 (broker-dealer custody); Rule 17f-2 (self-custody); Rule 17f-4 (securities depositories); Rule 17f-5 (foreign banks); Rule 17f-6 (futures commission merchants); and Rule 17f-7 (foreign securities depositories). Foreign securities are required to be held in the custody of a foreign bank or securities depository. Rule 17f-1 permits registered funds to use a broker-dealer custodian, but the rule imposes conditions that are difficult in practice to satisfy. Non-US regulated funds, such as UCITS, are similarly subject to requirements regarding the safekeeping of their assets. *See* EU Directive 2009/65/EC, as amended.

fellow customer risk. Rather, funds and their advisers are largely dependent on the Commission's segregation requirements to safeguard fund assets. The Commission's clearing requirement increases ICI members' reliance on the Commission's regulations, as it effectively precludes members from opting for the protections available in the uncleared swaps context.

For this reason, ICI has a keen appreciation, and has consistently advocated, for ensuring strong protection of customer collateral and funds. We appreciate the Commission's consistent commitment to improve customer protection and support its efforts to revise Part 190 to enhance such protection. In particular, we support those aspects of the Proposal that would:

- increase the resources available to satisfy public customer claims;
- mitigate fellow customer risk;
- help ensure equitable distribution of customer property;
- remove roadblocks to porting;
- facilitate portfolio margining; and
- ensure that customer property is reserved for customer claims.

In Section II, we explain that these enhancements will limit the extent to which the failure of an FCM or a DCO will cause losses to public customers or market disruption. We also note in Section II some further steps the Commission should take to protect customers, including: (i) adopting a segregation regime for futures and foreign futures that would limit fellow customer risk; (ii) coordinating with other regulators to eliminate barriers to porting; and (iii) providing guidance to the trustee regarding the porting of separately managed accounts.

We also support the Commission's efforts in the Proposal to clarify and modernize Part 190. In our view, Part 190 has previously functioned well in both stand-alone bankruptcy proceedings and proceedings under the Securities Investor Protection Act (SIPA). We nonetheless agree with the Commission that organizational and clarifying updates are needed to reflect the market and legal changes that have occurred in the nearly four decades since the Commission first adopted Part 190.

ICI is concerned, however, that certain components of the Proposal would harm public customers and cause uncertainty. In Section III, we detail our concerns regarding the Commission's proposal to defer to DCO loss allocation, recovery, and wind-down rules, even when such rules conflict with the substantive provisions of Part 190, such as the ratable treatment of customers. We agree with the Commission that clear, well-crafted, and well-vetted rules should be given effect in the liquidation of a DCO. However, DCO rules currently lack the clarity, transparency, rigorous review, comprehensiveness, and consistency required to facilitate an equitable and coherent liquidation that is consistent with Part 190. As a result, effectively incorporating such rules into Part 190 would undermine the goals of the Proposal by threatening to cause significant losses to customers and create uncertainty at a time of unprecedented market distress.

We therefore recommend that the Commission *not* defer to existing DCO rules in a Part 190 proceeding. Instead, the Commission should, first, require DCOs to implement governance processes that ensure that loss allocation, recovery, and wind-down rules are promulgated as part of a consultative process involving DCO members and customers, rather than on a unilateral and non-transparent basis. Second, the Commission should rigorously review such rules pursuant to its existing Part 40 regulations. Third, the Commission should supplement its existing Part 39 regulations with principles that DCO loss allocation, recovery, and wind-down rules must satisfy. Only once these protections for customers are implemented do we believe it would be appropriate to allow DCO rules to be given effect in a Part 190 proceeding. Even then, however, DCO rules should not be permitted to override any of Part 190's fundamental customer protections, such as the calculation of net equity or the priority right of public customer claims to customer property.

In Section IV, we explain that, while we generally agree with providing a Part 190 trustee discretion, we recommend that the Commission carefully tailor such discretion so that it is used to the benefit of public customers. More specifically, the Commission should make clear that the trustee shall: (i) use best efforts to satisfy those requirements of Part 190 that are designed to protect public customers, such as the requirement to follow the Commodity Exchange Act (CEA) and the Commission's regulations thereunder; and (ii) exercise any discretion granted to it with respect to the other requirements of Part 190 for the benefit of public customers.

Below we explain our recommendations in more detail.

II. Enhancing Customer Protection Under Part 190

The Proposal would comprehensively revise Part 190, while retaining and reinforcing the core tenets of existing Part 190 and Subchapter IV of Chapter 7 of the Bankruptcy Code ("Subchapter IV"). These tenets include: (i) the priority right of public customers to customer property in respect of their net equity claims; (ii) the preference for porting public customer transactions and margin in an FCM liquidation; and (iii) the *pro rata* distribution of customer property based on account class, which ensures equitable treatment of customers. These concepts are vital to protecting customers and limiting market disruption. We appreciate the Commission's efforts to not only reaffirm these principles, but further strengthen them.

A. *Increasing the Resources Available to Satisfy Public Customer Claims*

The principal mechanism by which Subchapter IV and Part 190 protect customers is the distribution of "customer property" ratably to customers on the basis of their net equity claims in priority to all other claims.[5] So long as there is sufficient "customer property" to satisfy all customer claims, customers should recover fully. If, however, there is any shortfall in customer property—whether due to fraud, the

[5] 11 U.S.C. § 766(h); 17 C.F.R. §§ 190.01(o), 190.07(c).

default of a fellow customer, investment losses, mismanagement (*e.g.*, poor recordkeeping by FCMs or DCOs or inaccurate calculations of residual interest requirements), or other operational losses—customers may incur losses. Congress has dictated,[6] and the Commission has implemented regulations providing, that such losses should be borne first by "non-public customers," *i.e.*, affiliates of the FCM, whose rights to customer property are subordinated to the claims of "public customers."[7]

We support the Proposal's preservation and strengthening of Part 190's protections against shortfalls in the resources available to satisfy public customer claims. These protections differ somewhat in the context of an FCM and a DCO insolvency, and we discuss each in turn.

1. FCM Insolvency

The Proposal would define "customer property" consistently with existing Part 190 to include assets and commodity contracts received from, or held for, the account of a customer.[8] In addition, the Proposal would expand the existing definition in the context of an FCM insolvency to include any cash, securities, and other assets that the FCM is required to set aside for the benefit of its customers, whether or not the FCM has segregated such assets.[9] The Proposal would also reaffirm the existing rule under Part 190 that "customer property" in an FCM insolvency includes any cash, securities, or other property of the estate that is necessary to satisfy the claims of an FCM's public customers.[10]

As an additional protection against shortfalls in the context of an FCM insolvency, the Proposal would make clear that the trustee must apply the Commission's "residual interest provisions . . . in a manner appropriate to the context of . . . [its] responsibilities as a bankruptcy trustee."[11] Those provisions require an FCM to maintain a buffer in segregated funds that is designed to "reasonably ensure that the [FCM] . . . remains in compliance with the [Commission's] segregated funds requirements at all times."[12]

We agree with the Commission that these provisions are critical to protecting customers against shortfalls in the assets that an FCM segregates for the benefit of customers. Without these protections, any customer default or any FCM or trustee miscalculation immediately preceding or following the

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[6] 11 U.S.C. § 766(h) ("[A] customer net equity claim based on a proprietary account . . . may not be paid either in whole or in part, directly or indirectly, out of customer property unless all other customer net equity claims have been paid in full.").

[7] 17 C.F.R. §§ 190.01(cc) (definition of non-public customer), (ii) (definition of public customer); 190.08(b).

[8] Proposed §§ 190.01, 190.09(a).

[9] Proposed § 190.09(a)(1)(ii)(G).

[10] Proposed § 190.09(a)(1)(ii)(L).

[11] Proposed § 190.05(f).

[12] 17 C.F.R. § 1.11(e)(3)(i)(D).

bankruptcy petition could result in insufficient segregated property and thus customer losses. The proposed provisions would help ensure that, if there is unsegregated property in such a situation, that property is allocated to customers, rather than general unsecured creditors. This allocation is appropriate, as customers, including ICI's members, enter into futures and cleared swaps on the basis of the Commission's and the CEA's protections. It would be inconsistent with their expectations to eliminate or relax those protections at a time when they are needed most.

Furthermore, these changes are consistent with Congress's intent in enacting Subchapter IV of the Bankruptcy Code. The definition of "customer property" in Subchapter IV specifically includes "other property of the debtor that any applicable law, rule, or regulation requires to be set aside or held for the benefit of a customer."[13] The Commission's proposed definition of "customer property" and application of its residual interest provisions to a debtor FCM and its trustee further this goal. Moreover, these changes are well within the scope of the Commission's authority, as Section 20 of the CEA expressly provides the Commission the ability to include or exclude assets from the scope of customer property and the method by which the business of a commodity broker is to be conducted post-petition.[14]

2. DCO Insolvency

In the context of a DCO insolvency, customer property is further divided into "member property" and customer property other than "member property."[15] Member property is distributed first to satisfy the net equity claims that a DCO member has in its proprietary capacity or on behalf of its non-public customers. Customer property other than member property is reserved to satisfy the net equity claims of a DCO member on behalf of its public customers.[16] As a result, the more customer property that is allocated to member property, the greater the possibility that public customers will incur losses.

The Proposal would include new provisions favoring allocation of customer property to "customer property other than member property" over allocation to "member property."[17] Specifically, the Proposal would first allocate guarantee deposits and assessments to customer property other than member property, and only then to member property if all of the public customer account classes are

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[13] 11 U.S.C. § 761(10)(A)(ix).

[14] 7 U.S.C. § 24(a).

[15] *See* 17 C.F.R. §§ 190.08 (describing allocation of customer property), 190.09 (describing allocation of "member property").

[16] *See* 17 C.F.R. §§ 190.08, 190.09.

[17] Proposed §§ 190.18(a), (c). It would also clarify the relationship between these two types of property, specifically referencing "customer property other than member property" in Part 190 for the first time. *See* Proposed §§ 190.00(c)(3)(ii), (iii)(A); 190.18.

fully funded.[18] In addition, any excess funds in any account class would first be allocated to customer property other than member property, and only then to member property if there are sufficient resources remaining to satisfy all claims on account of public customers.[19]

We strongly support these proposed amendments and agree with the Commission that they are necessary to further the policy embodied in Section 766(h) of the Bankruptcy Code—that the claims of public customers must have priority over the claims of non-public customers. That policy, which has been a hallmark of Part 190 and Subchapter IV for four decades, ensures that those least well-positioned to assess the DCO's risk, *i.e.*, those with the least proximity to the DCO, are given the greatest protection. DCO members, which participate in DCO risk committees and may have greater access to information concerning the DCO's financial health, have more tools available to protect themselves against losses. Public customers, by contrast, typically have no direct participation in the DCO's risk management and no insight into the transactions other customers have with the DCO. Therefore, public customers need the protections that the Commission proposes. Moreover, such protections are well within the scope of the Commission's authority, as Section 20 of the CEA expressly provides the Commission with the power to determine which property is to be included or excluded from the scope of member property.[20]

B. *Mitigating Fellow Customer Risk*

In the context of an FCM insolvency, one of the most likely causes of a shortfall in customer property is a fellow customer's default. Specifically, if one customer fails to meet its obligations regarding its transactions (*e.g.*, by failing to post initial or variation margin), the DCO may, except in relation to cleared swaps, apply the margin or funds posted by, or payable to, non-defaulting customers to satisfy the obligation. This DCO practice effectively exposes non-defaulting customers, including regulated funds and, indirectly, their shareholders, to the risk of a fellow FCM customer's default—a risk that is outside of a fund's ability to control or monitor.

As we have advocated in the past, the Commission should adopt a segregation regime for futures, foreign futures, and options thereon that provides a similar degree of protection from fellow customer risk as the "legally segregated operationally commingled" (LSOC) regime that the Commission adopted in Part 22 for cleared swaps.[21] LSOC effectively limits the extent to which each FCM customer bears fellow customer risk and more appropriately aligns risks and incentives. Further, it diminishes the

[18] Proposed §§ 190.18(b)(1)(iii), (c)(1).

[19] Proposed § 190.18(c)(3).

[20] 7 U.S.C. § 24(a).

[21] *See, e.g.,* Letter to Mr. Christopher Kirkpatrick, Secretary, Commodity Futures Trading Commission, from Dorothy M. Donohue, Acting General Counsel, Investment Company Institute, dated Sept. 28, 2017, *available at* https://www.ici.org/pdf/30889a.pdf.

likelihood of investors incurring unexpected losses because of a default of another customer with whom they have no connection.

Although we believe that an LSOC regime is necessary to fully protect customers that enter into futures, foreign futures, and related options, short of that we support the Commission's efforts in the Proposal to limit the extent to which a fellow customer's default following the commencement of liquidation proceedings may harm other customers. In particular, we support the provisions of the Proposal that would:

- preserve the existing requirement that the trustee fully credit the customer's funded balance for any margin payment made by a customer in response to the trustee's margin call;[22]
- expressly require the trustee to liquidate any customer account that is in deficit;[23] and
- maintain the existing requirement that the trustee promptly liquidate any customer account for which: (i) the customer fails to meet a margin call within a reasonable time;[24] or (ii) any payment of margin from that account would result in an account deficit.[25]

These existing Part 190 rules and proposed amendments represent critical protections for customers. As the Commission noted in the Proposal, a debtor FCM "will generally not have capital available to protect other customers by covering" account deficits, so "any loss suffered by customers whose accounts are in deficit will be at the risk of those other [non-defaulting] customers."[26] It is therefore vital that the trustee be required to swiftly crystallize, and therefore cap the losses resulting from, such deficits by promptly liquidating accounts in deficit or for which a customer has failed to meet a margin call. If any such accounts were allowed to remain open, additional losses on the delinquent customers' transactions would be borne by the FCM's non-defaulting customers. Furthermore, in order to ensure that non-defaulting customers continue meeting margin obligations post-petition, it is necessary that those customers be confident that they will fully recover such amounts. Any other approach would create a significant disincentive for customers to post margin, which could exacerbate fellow customer risk.

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[22] Proposed § 190.04(b)(3); *see also* 17 C.F.R. § 190.02(g)(3).

[23] Proposed § 190.04(b)(4).

[24] Because a customer's margin payment may be in transit or delivered to the FCM's custodian but not yet reflected on the FCM's books and records at the time of the trustee's appointment, the Commission should ensure the trustee consults with the FCM's custodian and personnel before making any margin calls or effecting any liquidations on the basis of a failure to meet a margin call. Similar consultations also may be appropriate before the trustee effects a transfer.

[25] Proposed § 190.04(b)(4); *see also* 17 C.F.R. §§ 190.03(b)(1)-(2).

[26] Proposal, at 36017.

C. *Reinforcing Equitable Treatment of Customers*

Although Subchapter IV and existing Part 190 provide for the *pro rata* distribution of customer property, actions by customers or the trustee may allow certain customers to effectively avoid *pro rata* treatment at the expense of other customers. Recognizing this possibility, the Proposal laudably includes a number of new provisions aimed at preventing certain customers from unfairly receiving a greater share of customer property than other customers. In particular, the Proposal would prohibit the trustee of an insolvent FCM from:

- making an upstream margin payment with respect to a customer account that would exceed the funded balance of that account;[27] or
- transferring any customer transaction or property that would result in insufficient customer property to make equivalent distributions to other customers.[28]

We support the addition of these provisions to Part 190. They would help to ensure that the trustee does not improperly favor, through payments or transfers, some customers over others in a way that would frustrate Part 190's mandate of *pro rata* treatment.

In addition, the Proposal would add new provisions related to letters of credit (LCs) in order to ensure that customers who post LCs as margin are unable to avoid *pro rata* treatment. In particular, the Proposal would modify the requirements for LCs so that an FCM may only accept an LC if it can be drawn in the event of proceedings in respect of the FCM or DCO, regardless of whether the customer has defaulted.[29] In addition, in the context of an FCM insolvency, the trustee would be permitted to request that any customer who has posted an LC as margin deliver substitute property to the trustee.[30] If the customer fails to do so within a reasonable time specified by the trustee, the trustee would be permitted to draw on the LC.[31] Then, the trustee would be required to treat: (i) any such substitute property or proceeds from drawing on the LC as customer property that may be distributed ratably; and (ii) any portion of the LC that is not drawn as having already been distributed to the customer.[32]

We strongly support these aspects of the Proposal, which would help to ensure that Part 190 does not improperly and inadvertently favor customers who post LCs as margin over others who post cash or securities as margin. As the Commission is well aware, the concerns related to LCs are not merely

[27] Proposed § 190.04(b)(1)(ii).

[28] Proposed § 190.07(d)(5).

[29] Proposed § 190.10(d).

[30] Proposed § 190.04(d)(3).

[31] Proposed § 190.04(d)(3).

[32] Proposed § 190.04(d)(3).

hypothetical. Customers who have posted LCs as margin have, in recent FCM liquidation proceedings, challenged the Commission's post-petition efforts to put those customers on an equal footing with customers who post cash or securities as margin.[33] The proposed provisions related to LCs would forestall any such future efforts and prevent customers from circumventing Congress's clear intent that similarly situated customers be treated similarly.

D. *Promoting Porting*

The Proposal would retain Part 190's expressed policy preference for porting, including its existing instruction to the trustee to use its "best efforts" to port public customer transactions and collateral.[34] In addition, the Proposal would add new provisions to Part 190 to mitigate or eliminate "speed bumps" that may hamper porting. Specifically, the Proposal would provide a transferee FCM with up to six months following the transfer to complete necessary customer diligence on the ported customers.[35] The Proposal also provides that the customer agreement in place between a transferred customer and a debtor FCM would govern the relationship between the customer and the transferee FCM unless and until the customer and the transferee FCM execute a customer agreement.[36]

1. Eliminating Barriers to Porting

We support the Proposal's efforts to eliminate barriers to porting. As the Commission noted, "[p]orting mitigates risks to both [FCM] customers . . . and to the market."[37] For many customers, including ICI's members, porting provides continuity and avoids the disruption, costs, and losses associated with having to terminate and re-establish their transactions.

We also encourage the Commission to coordinate with fellow regulators to reduce barriers to porting. For example, in addition to the Commission's diligence requirements, other regulators may impose on an FCM know-your-customer, anti-money laundering, and other diligence requirements. These requirements may apply to an FCM directly if, for example, the FCM is dually registered as a broker-dealer, or indirectly, if the FCM is part of a consolidated group that is subject to diligence requirements. In order to ensure that these requirements do not frustrate the trustee's efforts to port public customer transactions and margin, we urge the Commission to work with its fellow regulators to provide similar six-month grace periods.

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[33] *See* Proposal, at 36019.

[34] Proposed § 190.04(a); *see also* 17 C.F.R. § 190.02(e).

[35] Proposed § 190.07(b)(3).

[36] Proposed § 190.07(b)(4).

[37] Proposal, at 36076.

In addition, we urge the Commission to engage in advanced planning discussions with the Federal Deposit Insurance Corporation (FDIC) regarding how porting would be effectuated in the event an FCM became subject to proceedings under the OLA title of the Dodd-Frank Act.[38] OLA permits the Secretary of the Treasury ("Secretary"), following consultation with other federal regulators, to appoint the FDIC as receiver of an FCM if the Secretary determines that the failure of the FCM or its parent organization would have serious adverse consequences on financial stability in the United States.[39]

OLA has provisions that would allow the FDIC to transfer the transactions the FCM carries for customers to another institution. However, unlike Part 190, OLA contains very strict requirements related to such transfers. Specifically, it requires the FDIC to transfer within one business day following the commencement of proceedings all or none of the "qualified financial contracts," including futures and cleared swaps, "between" the institution subject to proceedings and a counterparty.[40] Depending on how "between" is interpreted in this context, OLA could be read to require the FDIC to either: (i) transfer all of the transactions cleared by an FCM at the same DCO to a single transferee; or (ii) allow the DCO to liquidate all such transactions. It is quite unlikely that the FDIC would be able to make such a large transfer to a third party so quickly, especially considering that an FCM that is large and interconnected enough to be eligible for OLA proceedings will almost certainly have a very large portfolio of customer transactions.

We do not believe it is correct to view transactions cleared for customers as being "between" the FCM and the DCO. Under the US agency model of clearing, transactions are between the customer and the DCO. As a result, in the event of OLA proceedings, the FDIC should have the ability to port some customers to one FCM, and other customers to other FCMs. Nonetheless, because the "all-or-none" determination must be made in a very short period of time, it is vital that the FDIC and the Commission coordinate in advance of any OLA proceeding to ensure that porting will be possible.

2. Ensuring Porting of Separately Managed Accounts Does Not Result in Undue Losses

We encourage the Commission to provide the trustee with guidance regarding the porting of separately managed accounts that belong to a single customer, including regulated funds that utilize multiple managers to separately invest portions of the fund's portfolio according to different investment mandates or strategies. In accordance with Commission No-Action Letter 19-17, a number of ICI's members maintain at a single FCM separate accounts for their funds or other clients.[41] Pursuant to the

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[38] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-230, 124 Stat. 1376 (2010).

[39] *See* 12 U.S.C. §§ 5383(a)-(b) (providing for the determination of a financial company as systemically significant where its insolvency under otherwise applicable insolvency law "would have serious adverse effects on financial stability in the United States"); *see also* § 5381(a)(11) (defining "financial company").

[40] 12 U.S.C. § 5390(c)(9).

[41] Commission No-Action Letter, CFTC Letter No. 19-17, Comm. Fut. L. Rep. (CCH) ¶ 34,523 (July 10, 2019).

staff's letter, an FCM calculates margin requirements for each such account on an independent basis. The managers of such accounts rarely, if ever, have access to information regarding the transactions or margin associated with other accounts or portions of funds they do not manage, even if those other accounts' transactions are cleared at the same FCM.

We recognize that, pursuant to the guidance of Commission staff, the separately managed accounts of an individual customer will be viewed on a combined basis for purposes of calculating the customer's net equity claim under Part 190. Nonetheless, viewing such customer's transactions and margin on a combined basis for purposes of making porting determinations could cause significant disruption and potential losses to customers. In particular, if the trustee were to effectuate a partial transfer that resulted in one of the separately managed accounts having a significant deficit following the transfer, the manager of that account would likely need to liquidate the bulk of the account's portfolio and other positions in order to eliminate or reduce the deficit. These liquidations would cause significant disruptions and losses to the customer. Indeed, they would cause the precise sort of disruptions and losses that Part 190 specifically seeks to prevent by facilitating porting.

Our concerns are demonstrated in the following simplified example:

- As of the petition date, assume a customer has three outstanding transactions:
  - Transactions A and B are managed by Manager 1; and
  - Transaction C is managed by Manager 2.
- In accordance with Commission No-Action Letter 19-17, the FCM maintains separate accounts for Manager 1 and Manager 2 and margins them separately.
- As of the petition date, Transactions A and C are each in the money to the customer by $100, and Transaction B is out of the money to the customer by $100.[42]
- On the petition date, the trustee is unable to determine each customer's funded balance, but concludes that it is in the best interest of public customers to effectuate a partial transfer, so long as such transfer does not effectively result in a distribution to any customer.

Under this example, the customer would have a net equity claim of $100 against the debtor FCM's estate. However, if the trustee transferred Transactions B and C to the transferee FCM and "left behind" Transaction A, Manager 1 could be faced with an immediate margin call from the transferee FCM. Although the transferee FCM could, in theory, calculate margin for the customer on the basis of its entire portfolio (and thus net Transactions B and C), it is unclear whether the FCM would actually do that or how the FCM could, as a practical matter, treat the separately managed accounts as a single customer. Separate agreements would likely govern the portfolios managed by Manager 1 and Manager 2 and, as noted, the individual managers are unlikely to have information regarding the positions managed by one another.

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[42] For the sake of simplicity, this example does not contemplate the customer having any margin posted to the FCM as of the petition date.

In order to meet its margin call, Manager 1 would likely need to liquidate Transaction B and other assets in order to obtain $100 of liquidity to deliver to the transferee FCM. These liquidations would likely result in significant disruption to Manager 1's portfolio and losses of the sort that the Commission's porting provisions are designed to prevent.

To avoid these kinds of disruptions and losses, we urge the Commission to provide guidance that the trustee should take due account of separately managed accounts when making porting determinations. Further, absent express customer consent, the trustee should not effectuate a transfer that will result in a separately managed account having a significant deficit following the porting.

E. *Facilitating Portfolio Margining*

The Proposal would clarify that transactions that are carried in a futures or cleared swaps account in accordance with Commission regulations constitute "commodity contracts" and thus are eligible for the protections Part 190 affords, regardless of whether such transactions are required to be carried in such an account.[43] Moreover, such transactions would be subject to "home field" rules, meaning that they would be treated the same as other transactions carried in the same account.[44]

We strongly support these amendments, as they would facilitate the ability of customers to portfolio margin transactions. Portfolio margining is critical for regulated funds to avoid undue costs associated with separate netting sets and conflicting regulatory requirements. A prerequisite for an effective portfolio margining regime is clarity regarding how transactions and margin that are portfolio margined in the same account will be treated in the event the FCM or broker-dealer becomes insolvent.

We appreciate the Commission's efforts to provide such clarity in the Proposal. In addition, we encourage the Commission to continue its portfolio margining harmonization efforts with the Securities and Exchange Commission (SEC) to further facilitate portfolio margining, including of security-based swaps and swaps.

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[43] The Proposal would clarify this point by defining "commodity contract" to include any "futures contract" and any "swap." Currently, Part 190 simply defines "commodity contract" by reference to Section 761(4) of the Bankruptcy Code. 17 C.F.R. § 190.01(h). "Futures contract" and "swap," in turn, would include not only those transactions that are generally treated as futures and cleared swaps for purposes of the Commission's regulations but also other transactions that may be portfolio margined with them. In particular, the Proposal would include in the "futures contract" definition: (i) any retail commodity transaction executed on or subject to the rules of a designated contract market (DCM) or foreign board of trade (FBOT) as if it were a futures contract; and (ii) a forward contract that is executed on or subject to the rules of a DCM or FBOT and cleared by a DCO (or foreign clearing organization) as if it were a futures contract. The "swap" definition would include any transaction that is carried in a cleared swaps account and is cleared by a DCO as if it were a cleared swap. *See* proposed § 190.01 (definitions of "commodity contract," "futures contract," and "swap").

[44] Proposed § 190.00(e).

In addition, we agree with the ABA recommendation that the Commission should amend its Part 22 regulations to make clear that, even if such transactions are not cleared swaps within the meaning of the Commission's regulations, LSOC applies to OTC transactions that are cleared by a DCO and carried, along with associated margin, in a cleared swaps account. Such amendments would ensure that FCMs and DCOs apply LSOC to these transactions in accordance with customers' expectations.

Were an FCM or DCO not to apply LSOC to such transactions, it would harm not only the customers who enter into such transactions but also customers who limit their activity to cleared swaps. This is because there would be a discrepancy between the transactions and collateral that form part of the cleared swaps account class under Part 190 and the transactions that the FCM or DCO treats as cleared swaps in accordance with Part 22. More specifically, under Part 190, customers that have claims arising from non-swaps and associated margin that are carried in a cleared swaps account would share ratably in respect of property allocated to the cleared swaps account class with customers that have claims arising on account of cleared swaps and associated margin. However, the available pool of assets that the FCM or DCO has segregated under Part 22 (and thus the property that would be allocated to cleared swaps account class in Part 190 proceedings) would be limited to cleared swaps and associated margin. Thus, customers who maintained non-swaps that were portfolio margined with cleared swaps would suffer losses, as would *all* cleared swaps customers.

We understand that staff resources to amend Part 22 may be limited. Therefore, we ask that the Commission or Commission staff provide guidance, such as an interpretive letter, that interprets Part 22 to require that OTC transactions cleared by DCOs and carried in a cleared swaps account be treated as cleared swaps subject to Part 22.

F. *Clarifying Who is Eligible for Customer Protection*

The purpose of Subchapter IV is to protect customers who entrust to a commodity broker their cleared transactions and associated margin on the basis of the Commission's regulations. It is not to protect counterparties that enter into uncleared transactions with an FCM and face the FCM on a bilateral basis. However, as the Proposal notes, in a previous FCM insolvency, counterparties to uncleared transactions with the insolvent FCM made innovative arguments as to why they should be entitled to customer property or otherwise have priority over, or parity with, public customers. These arguments took various forms, including that: (i) the transactions were "commodity contracts" due to their similarity to futures and cleared swaps; and (ii) the FCM held their associated collateral in a constructive or resulting trust (and thus that such property could not form part of the FCM's "customer property").[45] If successful, these claims would have eroded Part 190's customer protections because they would have left fewer assets available for the customers whom Subchapter IV and Part 190 are designed to protect.

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[45] *See* Proposal, at 36005-06.

The Commission successfully rebuffed these claims during that FCM insolvency proceeding. The Proposal would now codify the Commission's positions from that proceeding and confirm that: (i) off-exchange foreign currency transactions are not "commodity contracts;" and (ii) property cannot be excluded from the scope of customer property (and thus be unavailable to satisfy the claims of public customers) on the basis that it is held in a "constructive, resulting, or other trust that is implied in equity."[46]

We appreciate the Commission's prior efforts to prevent these counterparties from circumventing Part 190's protections for public customers and thereby contravening Congress's intent. Accordingly, we strongly support the Commission's proposed codification of these positions. These codifications will ensure that customer property is available to those customers whom Congress intended to protect, *i.e.*, customers who enter into futures and cleared swaps that are carried or cleared by the commodity broker.

G. *Providing Greater Clarity and Certainty*

In addition to the enhancements discussed above, the Proposal would make a number of organizational and clarifying changes. These include:

- subdividing Part 190 into three subparts: one general subpart, one subpart particular to FCM insolvencies, and one subpart particular to DCO insolvencies;
- adding a new Section 190.00 as an explanatory section that sets out core concepts and rules of construction and outlines the interaction of Part 190 with both OLA and SIPA;
- consolidating all ordinary course obligations applicable to FCMs in revised Section 190.10, in order to facilitate the orderly application of Part 190;
- clarifying the trustee's obligation to issue account statements to customers, including to reflect any liquidation or transfer;[47] and
- adding provisions that clarify the standards applicable to an FCM's liquidation of a debtor FCM's transactions and the way a trustee must assign liquidating transactions in the context of a partial liquidation.[48]

We appreciate the Commission's efforts to provide greater clarity regarding the application of Part 190 and support the proposed organizational and clarifying changes. We believe these changes will provide greater clarity to trustees, market participants, and courts regarding Part 190's requirements and intended functioning. In particular, we support proposed clarifications concerning account statements.

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[46] Proposed §§ 190.00(d)(2)(ii), (3).

[47] Proposed § 190.05(d).

[48] Proposed §§ 190.04(b)(5), (e)(3).

Such account statements are important for ICI's members, as they provide a basis for regulated funds to confirm the existence and value of their transactions and associated margin.

In addition, we believe that Section 190.00 will provide helpful guidance regarding Part 190's scope and tenets to those who may not be intimately familiar with them. Nonetheless, we do not believe that such a clarifying section is a substitute for a knowledgeable and experienced trustee. As the Commission knows well, proceedings under Subchapter IV or SIPA are fast-paced and involve unique, and sometimes arcane, concepts. Although the Commission may not have control over the selection of the trustee, we urge the Commission to engage with the Securities Investor Protection Corporation or the relevant bankruptcy court to ensure that any selected trustee has the experience and knowledge to act in accordance with the duties contained in Part 190 and Subchapter IV.

We further urge the Commission to consult with the FDIC regarding Part 190 well in advance of any commodity broker's resolution under OLA. Such consultation would help ensure that, if the FDIC is appointed as receiver of a commodity broker under OLA, it is familiar not only with Part 190's distributional scheme that is applicable in OLA but also with Part 190's core concepts. As discussed above, the Commission and the FDIC may need to coordinate in advance regarding certain issues, such as porting under the "all-or-none" requirement, so that the FDIC's actions in the event of an OLA proceeding are consistent with Part 190 and the protection of customer assets.

III. Part 190 Should Defer to DCO Rules Only if They Are Well-Drafted, Consistent, and Clear

The most significant, and troubling, aspect of the Proposal is that it would amend Part 190 to explicitly defer to DCO loss allocation, recovery, and wind-down rules in a DCO liquidation. Although we agree with the policy objective of having clear and well-vetted rules guide the liquidation of a DCO, we do not believe that existing DCO loss allocation, recovery, and wind-down rules are clear or well-vetted. The reality is very much the opposite. Currently, DCO loss allocation, recovery, and wind-down rules are ambiguous, inconsistent, and lack effective oversight from the Commission, members, customers, or the public. Before it directs trustees to defer to DCO rules, the Commission must fix this problem. Moreover, even clear and well-vetted DCO rules should not override the provisions of Part 190 and the customer protections that Congress intended to provide.

A. *Policy Objectives of the Proposal's Amendments Addressing DCO Insolvencies*

Under the Proposal, Part 190 would:

- provide that the trustee cannot avoid or prohibit any DCO action that was reasonably taken within the scope of the DCO's recovery and wind-down plans;[49]

[49] Proposed § 190.15(a).

- instruct the trustee to take actions in accordance with the DCO's recovery and wind-down plans;[50]
- require the trustee's calculation of DCO members' net equity claims to include the full application of the DCO's loss allocation rules and procedures;[51] and
- require the trustee to follow DCO recovery and wind-down plans applicable to making up shortfalls in settlement funds received by the DCO.[52]

These changes would not only give effect to DCO loss allocation, recovery, and wind-down rules, but also permit such rules to override the fundamental customer protections that Part 190 and Subchapter IV are meant to safeguard. If these changes are implemented, Part 190 will no longer guarantee to a customer a *pro rata* share of customer property based on its transactions and margin in accordance with Subchapter IV. Rather, a customer would only be entitled to such a *pro rata* share to the extent the DCO rules did not modify the distribution of the DCO's assets, whether pre- or post-petition, through measures such as variation margin gains haircutting or partial tear-up of transactions. Furthermore, a number of the other customer protections discussed above would only apply to the extent the DCO loss allocation, recovery, and wind-down rules did not contain differing requirements.

As support for these changes, the Proposal emphasizes the need for greater clarity and certainty regarding the resolution of a DCO. It notes that a DCO insolvency would be unprecedented, so neither the trustee nor market participants would be able to leverage past experience. In addition, the Proposal notes an insolvent DCO could be resolved in an OLA proceeding. In such a proceeding, Subchapter IV's provisions concerning the distribution of customer property would apply. Thus, the Commission must provide clear guidance addressing how such a DCO would be resolved under Part 190.[53]

The Proposal asserts that DCO rules should serve as the roadmap to guide the liquidation of a DCO, as they "will, in most cases, have been developed pursuant to the Commission's regulations in part 39, and subject to staff oversight."[54] Moreover, the Proposal states that DCO rules represent "the contract between and among the members and the DCO."[55] As a result, the Proposal suggests giving effect to

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[50] Proposed § 190.15(c).

[51] Proposed § 190.17(b)(1).

[52] Proposed § 190.19(b)(1).

[53] Proposal, at 36035.

[54] Proposal, at 36002. Specifically, Part 39 requires certain DCOs to "maintain viable plans" for recovery and orderly wind-down, submit such plans to the Commission, and provide the Commission and the FDIC "with information needed for purposes of resolution planning." 17 C.F.R. §§ 39.19(c)(4)(xxiv); 39.39(b).

[55] Proposal, at 36038.

DCO rules will provide the trustee for the DCO, or the FDIC, as applicable, with a clear and vetted framework to use to manage the liquidation of the DCO and the distribution of its estate.[56]

ICI agrees with the Commission that Part 190 should provide a well-crafted, clear, and properly vetted roadmap to guide the liquidation of a DCO.[57] Such a roadmap would benefit regulated funds and their shareholders by allowing them to understand what to expect during a DCO insolvency. Clear and well-vetted provisions would also allow the trustee or the FDIC to quickly develop and implement a coherent and coordinated approach to the resolution of a DCO.

However, we do not believe that existing DCO loss allocation, recovery, and wind-down rules can effectively serve as this roadmap. Such rules do not provide the level of specificity and detail that is required to give certainty to market participants or clarity to the FDIC or a trustee. Rather, they simply enumerate a wide variety of tools that a DCO may deploy to recover losses, including assessments, variation margin gains haircutting, and tear-ups. These measures have the capacity to alter the entitlements of customers relative to what Part 190 provides and, in so doing, withdraw significant amounts of capital and liquidity from the financial system at a time of severe market stress. Despite such potentially detrimental consequences, DCO rules do not provide any rigorous or specific standards that must be followed to ensure that the massive costs of deploying these tools do not outweigh their benefits. Consequently, deferring to DCO loss allocation, recovery, and wind-down rules would frustrate the customer protections set forth in Part 190 and exacerbate financial stress.

The principal reason why DCO loss allocation, recovery, and wind-down rules provide DCOs with immense discretion to impose losses on members and customers is that such rules are not the result of a meaningful or consultative vetting process. DCO members or customers usually have very limited opportunities to participate in the DCO rulemaking process. Moreover, although the Proposal points to the Commission's ability to review DCO rules,[58] the Commission's current review practices are not nearly robust enough to make up for the absence of a consultative and inclusive drafting process involving DCO members and customers. Indeed, given the potential inconsistency of existing DCO loss allocation, recovery, and wind-down rules with existing provisions of Part 190, there is some question whether those rules satisfy the standards set forth in Section 5c(c) of the CEA and Part 40 of the Commission's regulations.

We applaud the Commission for fulfilling Congress's mandate by drafting a careful and clear set of provisions in the Proposal to promote the protection of customers. We urge the Commission not to

[56] Proposal, at 36002, 36038.

[57] To further increase clarity and certainty regarding a DCO's resolution, we also encourage the Commission to consider and provide guidance on if and when a non-US DCO, and the non-US operations of a US-based DCO, would be subject to Part 190's provisions.

[58] *See* Proposal, at 36002; *see also* 17 C.F.R. §§ 40.5, 40.6, 40.10.

upend those protections by deferring to DCO rules that do not provide a similar level of clarity or specificity, potentially exposing customers to catastrophic losses.

B. *Recommendations for the Commission*

Before the Commission gives effect to any DCO loss allocation, recovery, and wind-down rules in a Part 190 proceeding, it must take steps to ensure that such rules are clear, well-drafted, and properly vetted. We recommend three actions that, if taken together, would dramatically improve the clarity and effectiveness of such rules and better effectuate the Proposal's goal of creating certainty and protecting customers.

First, the Commission should develop and codify minimum principles that must be reflected in any DCO loss allocation, recovery, or wind-down rule. These minimum principles are necessary to create greater clarity and consistency across DCOs. Such principles need not dictate substantive requirements (*e.g.*, the amount of assessments that a DCO must make). Rather, they should focus on ensuring that any imposition of losses is subject to a consultative process. That process should be aimed at ensuring that both members and customers, and potentially the Commission and the FDIC, are involved in determining whether, when, and to what extent any such tool is deployed.

Second, the Commission should review both existing DCO rules and proposed rule changes to ensure they are consistent with the Commission's minimum principles. We encourage the Commission to exercise its ability to reject any rule that is inconsistent with its minimum principles, or any other component of the CEA or the Commission's regulations thereunder.[59] When reviewing a proposed rule change under its existing Part 40 review procedures, the Commission should suggest changes to any component of the proposed rule change necessary to bring it in line with these standards. Moreover, if the Commission finds that it needs more than the statutorily prescribed ten-business-day review period to review a proposed rule change submitted through the self-certification process,[60] we encourage the Commission to use its ability to extend the review period to up to ninety days.[61] In this regard, the Commission should view any changes to DCO loss allocation, recovery, or wind-down rules (other than clerical or otherwise immaterial changes) as presenting novel or complex issues in consideration of the fact that no DCO has ever been liquidated and any such liquidation is likely to be both novel and complex. It is critical that the Commission use this mechanism to seek input on these rule changes from the public, including DCO members and customers.

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[59] *See* 7 U.S.C. § 7a–2(c)(5)(A).

[60] *See* 7 U.S.C. § 7a–2(c); 17 C.F.R. § 40.6(b).

[61] The Commission has the ability to extend its review window, and thus place a stay on the effectiveness of the proposed rule change, if it determines that the such change "presents novel or complex issues that require additional time to analyze, . . . is accompanied by an inadequate explanation, or . . . is potentially inconsistent with the [CEA] or the Commission's regulations thereunder." 17 C.F.R. § 40.6(c); *see also* 7 U.S.C. §§ 7a–2(c)(2)-(3).

Third, the Commission should require DCOs to change their governance process for rule changes to give stakeholders greater opportunities for input. Because of the exclusive ability of DCOs to clear certain products and the requirement that such products be cleared, customers are faced with a choice of either accepting the DCO rules as drafted or foregoing the hedges they need. Given this imbalance in bargaining power, DCOs have not been incentivized to provide members and customers with greater input in the DCO rulemaking process.[62] As a result, Commission action is necessary to change DCO governance procedures for rule changes. Such changes should at a minimum require DCOs to offer members and customers, outside of any risk committee, the opportunity to review and provide feedback on any proposed DCO rule change concerning loss allocation, recovery, or wind-down. Moreover, DCO members and customers should have the power to vote on any such proposed change. Such voting powers are necessary to ensure that customers have the ability to evaluate and prevent proposed changes that would unreasonably endanger their margin and hedges.

Only with these changes do we believe that DCO rules could provide a level of clarity, equity, and comprehensiveness necessary to warrant allowing them to apply in a Part 190 proceeding. We do not believe that even well-drafted DCO rules should override the critical customer protections that Part 190 and Subchapter IV provide. Congress developed a framework for the liquidation of a commodity broker and tasked the Commission, not DCOs, with developing and implementing the framework. To the extent both Congress and the Commission are silent on a given issue arising in a DCO liquidation, it may be appropriate for well-drafted DCO rules to address and govern the resolution of that issue. However, DCO rules should never override the calculation of a customer's net equity claim, the priority right of public customer claims, or the other issues Part 190 specifically addresses. Customers depend on the investor protections contained in Part 190, and should not be subject to change absent notice and comment in accordance with the Administrative Procedure Act.

IV. The Trustee Should Have Discretion, but Not at the Expense of Customer Protection

The Proposal materially departs from existing Part 190 by providing the trustee with significantly more discretion than it has today. Throughout the Proposal, the Commission proposes to relax what are currently mandatory or "best efforts" requirements in order to give the trustee greater flexibility. Of particular note, the Proposal would:

- convert from mandatory to "reasonable efforts" the requirements that the trustee: (i) comply with the CEA and the Commission's regulations; and (ii) compute the funded balance for each customer account containing open commodity contracts or other property on a daily basis;[63]

[62] Although some DCOs have risk committees on which employees from such parties sit, those representatives owe their duties to the DCO, rather than to their employers. As a result, those representatives are severely limited in their ability to present the alternative perspectives that well-crafted rules require.

[63] Proposed §§ 190.05(a), (b).

- convert existing Part 190's requirement that a trustee make margin calls to an option that the trustee may elect to exercise;[64]
- require the trustee to use "all reasonable efforts" to provide account statements for customer accounts containing open commodity contracts or other property;[65]
- allow the trustee to request an exemption from any procedural requirement of Part 190; [66]
- require the trustee to comply with the Commission's residual interest provisions only "in a manner appropriate to the context of [its] responsibilities as a bankruptcy trustee;"[67]
- permit the trustee to request permission of the Commission to continue operating a debtor DCO for up to six calendar days;[68]
- provide a more generalized approach for valuing certain commodity contracts;[69] and
- eliminate a number of timing requirements.[70]

These proposed changes are intended to permit the trustee to make decisions that are more tailored to circumstances of the particular commodity broker's insolvency, and thereby improve the trustee's ability to operate efficiently and effectively. The Commission explains that providing the trustee with greater discretion is motivated by both practical necessity and positive past experience.[71]

We agree with the Commission that trustees need some flexibility given the myriad decisions they must make in a short period of time and the unique circumstances that each commodity broker insolvency may present. We further agree with the Commission that trustees to date have exercised their discretion in a manner that has generally promoted customer protection.

However, we believe that providing the trustee with greater discretion is only appropriate to the extent doing so furthers Part 190's overarching goal of protecting public customers. As the Proposal correctly notes, affording the trustee "increased discretion comes [with] a risk of trustee mistake or misfeasance; in other words, a trustee making decisions that turn out not to be in the best interests of the customers."[72] It also presents the risk that the trustee will prioritize certain considerations over customer protection. Moreover, in certain instances, such as computation of funded balances or

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[64] Proposed § 190.04(b)(2).

[65] Proposed § 190.05(d).

[66] Proposed § 190.02(a).

[67] Proposed § 190.05(f).

[68] Proposed § 190.14(b).

[69] Proposed § 190.08(d)(1)(ii).

[70] *See, e.g.*, proposed §§ 190.03(a)-(c).

[71] *See* Proposal, at 36043.

[72] Proposal, at 36043; *see also* Proposal, at 36049, 36055, 36058.

provision of account statements, the failure of the trustee to provide such information could hinder the ability of a regulated fund to confirm the existence and value of its transactions and associated margin.

As a result, certain limitations on a trustee's discretion are necessary to help ensure that the trustee prioritizes the protection of customers, as provided for in Part 190 and Subchapter IV. First, where the Part 190 provision at issue is specifically aimed at protecting customers, the trustee's discretion should be quite limited. Of course, at times, compliance with these provisions may be impractical or impossible or may cause harm to customers. However, a standard such as "reasonable efforts" could signal that the trustee has wider latitude to depart from the requirement at issue. Therefore, we urge the Commission to require the trustee to use its "best efforts" to:

- comply with the CEA and Commission regulations;
- compute the funded balance for each customer account containing open commodity contracts or other property on a daily basis;
- make margin calls;
- provide account statements for customer accounts containing open commodity contracts or other property; and
- comply with the Commission's residual interest provisions.

We believe that this standard would ensure that any departures from these important customer protection provisions are limited to circumstances where compliance is not reasonably practical or would cause harm to customers.

Second, for any other Part 190 provision that affords the trustee discretion, we urge the Commission to make clear in Section 190.00 that the trustee must exercise that discretion in a manner that it determines will result in the greatest recovery for, and the least disruption to, public customers. Such a standard will ensure that the trustee does not exercise the discretion Part 190 affords to it to further other considerations, such as operational expedience, requirements imposed by other regulatory bodies, or protection of the commodity broker's general estate. Rather, it would ensure that, to the extent the trustee exercises discretion provided by Part 190, that discretion is applied in a manner that promotes the best interest of public customers.

Third, we support the proposed amendment that would allow the trustee to request an exemption from any procedural requirement of Part 190[73] and urge the Commission to limit this amendment as drafted to procedural requirements. The trustee should not be permitted to depart from Part 190's substantive requirements. Customers enter into futures and cleared swaps on the premise of Part 190's substantive protections. It would distort their expectations if the trustee were able to depart from them.

[73] Proposed § 190.02(a).

We also agree that any decision to continue operating a DCO in liquidation must be made with Commission input and consent.[74] The continued operation of a DCO has the potential to result in significant continued losses for customers and exacerbate stress. The trustee should thus not have the unilateral ability to make such decisions. In considering whether to grant a request to allow a failed DCO to continue operating, the Commission should consider potential harm to customers and should request input from both DCO members and customers.

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We appreciate the opportunity to comment on the Proposal. If you have any questions about our comment letter, please feel free to contact me at (202) 326-5835.

Sincerely,

/s/ Sarah A. Bessin

Sarah A. Bessin
Associate General Counsel

cc: The Honorable Heath P. Tarbert
The Honorable Brian D. Quintenz
The Honorable Rostin Behnam
The Honorable Dawn DeBerry Stump
The Honorable Dan M. Berkovitz

Clark Hutchison III, Director, Division of Clearing and Risk
Robert Wasserman, Chief Counsel and Senior Advisor, Division of Clearing and Risk
Commodity Futures Trading Commission

[74] The Commission should only approve such an application from a trustee to continue operating a DCO in liquidation if it determines that the trustee has the knowledge and experience to manage such operations.