Federated Hermes

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January 17, 2024

VIA ONLINE SUBMISSION

Mr. Christopher Kirkpatrick
Secretary
U.S. Commodity Futures Trading Commission
1155 21st Street, NW
Washington DC 20581

Re: Investment of Customer Funds by Futures Commission Merchants and Derivatives Clearing Organizations Proposal

Dear Mr. Kirkpatrick:

Federated Hermes, Inc. and its subsidiaries ("**Federated Hermes**")[1] submit this comment letter to the U.S. Commodity Futures Trading Commission (the "**Commission**" or "**CFTC**") regarding the Commission's proposal to amend the Commission's regulations governing the safeguarding and investment by futures commission merchants ("**FCMs**") and derivatives clearing organizations ("**DCOs**") of funds held for the benefit of customers engaging in futures, foreign futures, and cleared swaps transactions (the "**Proposal**").[2] Among other things, the Proposal would amend the list of "*Permitted Investments*" in Regulation 1.25, including, but not limited to, by limiting the scope of money market funds ("**MMFs**") whose interests qualify as Permitted Investments to government MMFs that do not elect to apply a discretionary liquidity fee ("**Permitted Government MMFs**"). The Proposal also sets forth lower concentration limits on Permitted Government MMFs.

Federated Hermes supports including Permitted Government MMFs as Permitted Investments. However, the proposed 5% issuer-based concentration limitation for Permitted Government MMFs is an unnecessarily restrictive and arbitrary number. As such, Federated Hermes fully supports and agrees with the comments and recommendations contained in the comment letter submitted by the Investment Company Institute (the "**ICI**") related to concentration limits on Permitted Government MMFs, as set forth in its comment letter in response to the Proposal (the "**ICI Letter**").

[1] Federated Hermes, Inc. (NYSE: FHI) is a global leader in active, responsible investment management, with $715.2 billion in assets under management as of September 30, 2023. We deliver investment solutions that help investors target a broad range of outcomes and provide equity, fixed-income, alternative/private markets, multi-asset and liquidity management strategies to more than 11,000 institutions and intermediaries worldwide. Our clients include corporations, government entities, insurance companies, foundations and endowments, banks and broker-dealers.

[2] CFTC, *Investment of Customer Funds by Futures Commission Merchants and Derivatives Clearing Organizations*, 88 Fed. Reg. 81236 (Nov. 21, 2023), available at https://www.govinfo.gov/content/pkg/FR-2023-11-21/pdf/2023-24774.pdf.

In particular, we strongly agree with the ICI that the Commission's proposed 5% issuer-based concentration limitation for Permitted Government MMFs is not supported by the Commission's purported concerns. We also agree that the concentration limits for Permitted Government MMFs should be 25%, the same concentration limits for U.S. agency obligations.

The Commission's proposed the 5% limitation is meant to mitigate its concerns regarding potential risks associated with concentrating investments of Customer Funds in any single government MMF or family of government MMFs, which may be susceptible to cyber-attacks and operational incidents that may result in the inability to timely process redemption requests of FCMs and DCOs.[3]

Notwithstanding the fact that government MMFs are low-risk and highly liquid investment vehicles, the proposed 5% issuer limitation is an arbitrary number and has no reasonable relationship to the risk it supposedly addresses.

The Commission correctly notes that cyber-attacks and other operational incidents may impact transactions in any Permitted Investment, including U.S. government securities.[4] However, it's belief that the potential risk of Customer Funds becoming unavailable "*is elevated when access to such funds depends on the operations of a third party, such as a MMF*"[5] is not supported by any data and can be effectively mitigated without resorting to the Commission's arbitrary concentration limits. For example, we assert that the risk is substantially mitigated by MMFs existing policies and procedures which are required under Rule 38a-1[6] under the Investment Company Act of 1940 and cybersecurity programs, which may already be in place for MMFs.

As acknowledged by the Securities and Exchange Commission (the "**SEC**") in its recent Cybersecurity Risk Management for Investment Advisers, Registered Investment Companies, and Business Development Companies rule proposal (the "**SEC Cybersecurity Risk Management Proposal**"), cybersecurity programs have been implemented by some funds without any specific cybersecurity rule requirement as "*funds take into account the specific risks they face, often including any specific cybersecurity risks, when developing their compliance policies and procedures"* under Rule 38a-1.[7]

The SEC Cybersecurity Risk Management Proposal is expected to be finalized in the near future.[8] The industry anticipates that any final rules will require funds to have policies and procedures that have measures to detect, respond to and recover from a cybersecurity incident and that are reasonably designed

[3] *Id*. at 81 and 130.
[4] *Id*. at 82.
[5] *Id*.
[6] In 2003, the SEC adopted Rule 38a-1, which required registered investment companies, including Permitted Government MMFs, to adopt and implement written compliance policies and procedures reasonably designed to prevent violation of the federal securities laws. See Compliance Programs of Investment Companies and Investment Advisers ("**Rule 38a-1**"), Advisers Act Rel. No. 2204 (Dec. 17, 2003) [68 FR 74714 (Dec. 24, 2003)].
[7] SEC, Cybersecurity Risk Management for Investment Advisers, Registered Investment Companies, and Business Development Companies, 88 Fed. Reg. 81236 (March 21, 2023), available at https://www.federalregister.gov/documents/2023/03/21/2023-05766/cybersecurity-risk-management-for-investment-advisers-registered-investment-companies-and-business ("**SEC Cybersecurity Risk Management Proposal**"). Pages 10 - 12.
[8] Pursuant to the SEC's "*Agency Rule List – 2023*", the SEC Cybersecurity Risk Management Proposal is listed as being in the "*Final Rule Stage*", with an anticipated "*Final Action*" (issuance of final rule) date of April 2024. https://www.reginfo.gov/public/do/eAgendaViewRule?pubId=202310&RIN=3235-AN08

to ensure that a fund can continue to operate during a cybersecurity event, as noted in the SEC Cybersecurity Risk Management Proposal.[9]

While the Commission feels that the issuer-based concentration limit may not be burdensome (based on the large number of government MMFs that are available on the market and which are likely to meet Permitted Investments eligibility criteria[10]), the proposed concentration limitation is not supported by any meaningful data. In our view, risks associated with concentration of Customer Funds in any such government MMFs are adequately addressed by existing Rule 38a-1 policies and procedures and cybersecurity programs. Consequently, the Commission should permit issuer-based concentration limits for Government MMFs to be at least 25%.

Federated Hermes opposes any rule or adoption of any final rule until data, which demonstrates the need for any such rule, has been presented to the industry for further public comment. Accordingly, we strongly object to the proposed concentration limits for Permitted Government MMFs in the Proposal. We also caution the Commission on the practice of proposing or adopting unwarranted proposed rules as it could result in additional unjustified regulatory rules and amendments being adopted in the future which would have costly and unintended consequences for the financial industry, including market participants and underlying investors.

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Federated Hermes appreciates the opportunity to comment on the Proposal. Please let us know if you have any questions or comments on this submission.

Sincerely,

Madison Dischinger

Madison Dischinger
Corporate Counsel

cc: The Honorable Rostin Behnam
The Honorable Kristin N. Johnson
The Honorable Christy Goldsmith Romero
The Honorable Summer K. Mersinger
The Honorable Caroline D. Pham

Amanda L. Olear, Director, Market Participants Division

Commodities Futures Trading Commission

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[9] SEC Cybersecurity Risk Management Proposal at 29.
[10] *Id*. at 82