



March 21, 2024

Mr. Christopher Kirkpatrick  
Secretary of the Commission  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21<sup>st</sup> Street NW  
Washington, DC 20581

**RE: Protection of Clearing Member Funds Held by Derivatives Clearing Organizations**

Dear Mr. Kirkpatrick:

LedgerX LLC (“**LX**”) appreciates the opportunity to comment on the Commodity Futures Trading Commission’s (“**CFTC**” or “**Commission**”) notice of proposed rulemaking titled Protection of Clearing Member Funds Held by Derivatives Clearing Organizations (“**Proposal**”).<sup>1</sup> As explained further below, LX fully supports the Proposal to extend safeguards currently afforded to funds of customers of FCM clearing members (“**Customer Funds**”) under the Commodity Exchange Act (“**CEA**”) and regulations thereunder to funds of clearing members (“**Proprietary Funds**”).<sup>2</sup> LX would also support further regulation to help ensure Proprietary Funds are afforded substantially similar safeguards to those currently received by Customer Funds under the CEA and regulations thereunder.

**I. Introduction**

LX is a wholly-owned subsidiary of Miami International Holdings, Inc. (“**MIH**”), the corporate holding company for a global exchange group that operates regulated markets for the listing, trading, and clearing<sup>3</sup> of commodity derivatives markets and the listing and trading of equity and equity derivative markets.<sup>4</sup> LX is regulated by the CFTC as a Derivatives Clearing Organization

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<sup>1</sup> Protection of Clearing Member Funds Held by Derivatives Clearing Organizations, 89 Fed. Reg. 286, (Jan. 3, 2024).

<sup>2</sup> The Proposal also would allow a DCO to hold Customer Funds and Proprietary Funds at the central bank of a money center country (as defined in 17 CFR 1.49) and would require a modified acknowledgment letter from that central bank. This comment does not address that part of the Proposal.

<sup>3</sup> MIH’s other DCO, the Minneapolis Grain Exchange (“**MGEX**”), has filed its own comment in response to the Proposal. The MGEX comment is consistent with this comment and also addresses issues that pertain to MGEX but not to LX.

<sup>4</sup> MIH is fourteenth largest global derivatives exchange group by executed volume in 2023 and the fastest growing exchange group for U.S. multi-listed options since 2016 (compiled from source data)

("DCO"), Designated Contract Market ("DCM"), and Swap Execution Facility ("SEF"). By the terms of its DCO registration,<sup>5</sup> LX is (i) permitted to clear fully collateralized futures, options on futures, and swaps, and is (ii) not yet permitted to clear for futures commission merchants ("FCM") on behalf of customers. As a result, and providing they meet the membership requirements in LX's rules, natural persons may become clearing members and clear fully collateralized products at LX directly ("**Non-Intermediated Clearing**"). Funds deposited by such natural persons are Proprietary Funds.

## II. Current Regulatory Treatment of Customer Funds and Proprietary Funds

The CEA and CFTC regulations thereunder place certain requirements on FCMs regarding Customer Funds, including: (i) segregating Customer Funds from their own funds; (ii) depositing Customer Funds in an account clearly marked as such; (iii) obtaining written acknowledgement letters from depository institutions; (iv) limiting the investment of Customer Funds to certain explicitly authorized instruments; and (v) creating requirements for authorized depositories.<sup>6</sup> These particular safeguards also apply to DCOs that receive and hold Customer Funds deposited by FCM clearing members.<sup>7</sup>

As noted in the Proposal, these safeguards exist primarily as a function of the customer-FCM relationship and do not apply to Proprietary Funds, whether the source of such funds is an FCM or corporate clearing member of a clearinghouse providing traditional, intermediated clearing, or from natural persons that are members of a clearinghouse providing Non-Intermediated Clearing. While the CEA and regulations thereunder contain some safeguards for Proprietary Funds, they are less specific than the requirements imposed on entities holding Customer Funds. For example, DCOs are required to establish standards and procedures that protect and ensure the safety of Proprietary Funds and are required to hold Proprietary Funds in a manner which minimizes the risk of loss or of delay in the access by the DCO to such funds.<sup>8</sup>

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available at theocc.com). See FIA ETD Tracker, Volume by Exchange, available at [https://www.fia.org/fia/etd-tracker?utm\\_campaign=0223&utm\\_content=FIA%20ETD%20Tracker&utm\\_term=&utm\\_medium=DAETD&utm\\_source=FIAEmail](https://www.fia.org/fia/etd-tracker?utm_campaign=0223&utm_content=FIA%20ETD%20Tracker&utm_term=&utm_medium=DAETD&utm_source=FIAEmail).

<sup>5</sup> See In the Matter of the Application of LedgerX LLC For Registration as a Derivatives Clearing Organization (Sept. 2, 2020), available at <https://www.cftc.gov/IndustryOversight/IndustryFilings/ClearingOrganizations/30998> ("**LX Registration Order**").

<sup>6</sup> See generally 17 CFR 1.20, 22.5, and 30.7.

<sup>7</sup> See generally 17 CFR 1.20(g) (general requirements), 39.15(b) (segregation of Customer Funds), and 22.3(b)(1) (treatment of cleared swaps Customer Funds).

<sup>8</sup> See 7 U.S.C. 7a-1(c)(2)(F); 17 CFR 39.15. LX believes these provisions require it to hold Proprietary Funds at a bank, trust company, or DCO, consistent with the current CFTC requirement regarding Customer Funds in 17 CFR 1.20(g)(2). In other words, LX does not believe that current CFTC requirements would have permitted it to hold funds at a trading firm like Alameda Research. Chair Behnam's written testimony at the Senate Agriculture Committee on December 1, 2023 supports this view: "[m]any public reports indicate that segregation and customer security failures at the bankrupt FTX entities resulted in huge amounts of FTX customer funds being misappropriated by Alameda for its proprietary trading. But the customer property at LedgerX – the CFTC regulated entity – has remained exactly where it should be, segregated and secure. This is regulation working." Testimony of Rostin Behnam, Chairman, Commodity Futures Trading Commission, Why Congress Needs to Act:

### III. LedgerX's Current Treatment of Proprietary Funds

Acknowledging that LX would provide Non-Intermediated Clearing, the CFTC required in the LX Registration Order that LX segregate Proprietary Funds from LX funds.<sup>9</sup> LX's rules require it to (i) limit investments of Proprietary Funds to those investments authorized by 17 CFR 1.25 (as would be required by Proposed Rule 17 CFR 39.15(e))<sup>10</sup> and (ii) use Proprietary Funds only as belonging to clearing members (as would be required by Proposed Rule 17 CFR 39.15(f)(4)). LX also commingles Proprietary Funds only with other Proprietary Funds to enable it to "limit operational risks by simplifying [] banking processes and procedures."<sup>11</sup> LX's practice also includes: (i) obtaining written acknowledgement letters from commercial banks that hold Proprietary Funds, which letter is substantially similar to the acknowledgement letter currently required for DCOs that hold Customer Funds at commercial banks; and (ii) calculating on a daily basis the amount of Proprietary Funds it holds for all clearing members and reconciling that amount with the amount it should hold for all clearing members. As a result of the requirements imposed on it in the LX Registration Order, its own Rules, and its stated practices, LX currently complies with the requirements that would be imposed upon it by virtue of the Proposal. This should not be surprising: as Chair Behnam noted in testimony in front of the Senate Agriculture Committee, notwithstanding the treatment of funds of customers by LX's former holding company, "the customer property at LedgerX . . . remained exactly where it should be, segregated and secure."<sup>12</sup>

### IV. Proposal

The Proposal would apply several of the regulatory safeguards for the treatment of Customer Funds to Proprietary Funds. Under the Proposal, DCOs would be required to:

- invest Proprietary Funds only as permitted for investment of Customer Funds and bear all losses associated with the investment of Proprietary Funds;
- account for Proprietary Funds separately from its own funds and hold Proprietary Funds in accounts named to clearly identify the funds as belonging to clearing members;
- maintain in accounts holding Proprietary Funds financial resources sufficient in the aggregate to cover the total value owed to clearing members;

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Lessons Learned from the FTX Collapse, U.S. Senate Committee on Agriculture, Nutrition, and Forestry, December 1, 2022 ("**Chair Behnam Testimony**"), available at: <https://www.agriculture.senate.gov/imo/media/doc/The%20Honorable%20Rostin%20Behnam%20Testimony.pdf>.

<sup>9</sup> LX Registration Order, available at <https://www.cftc.gov/PressRoom/PressReleases/8230-20> ("LedgerX shall at all times maintain funds of its clearing members separate and distinct from its own funds.").

<sup>10</sup> See LX Rulebook, available at [https://assets.websitefiles.com/5f3a828e59758a2b0394173d/659d8b98d07ee56845e4ad54\\_LedgerX%20-%20Rulebook%20DCO%20\(2024-01-08\).pdf](https://assets.websitefiles.com/5f3a828e59758a2b0394173d/659d8b98d07ee56845e4ad54_LedgerX%20-%20Rulebook%20DCO%20(2024-01-08).pdf), Rule 7.2(g) ("[LX] may invest any cash deposited as collated in accordance with CFTC Regulations 1.25 and 39.15(e) . . .").

<sup>11</sup> Proposal at 290.

<sup>12</sup> Supra note 8, Chair Behnam Testimony.

- obtain from any depository (other than Federal Reserve Banks) holding Proprietary Funds a written acknowledgement that the funds belong to the DCO's clearing members and cannot be used by the DCO for any other purpose;<sup>13</sup>
- limit commingling of Proprietary Funds to other Proprietary Funds;
- limit the use of Proprietary Funds only as belonging to the clearing member that deposited the funds;
- calculate the amount of funds owed for each type of segregated account in which it holds Customer Funds or Proprietary Funds and reconcile the total amount (aggregate across all clearing members) for each type of segregated account with the amount for each type of segregated account held across all depositories by noon of each business day on balances held as of the close of business on the previous business day; and
- report to the Commission any discrepancies in the amount of Proprietary Funds or Customer Funds that it holds for each clearing member and in any of the daily reconciliations that would be required by the Proposal ("**Reconciliation Reporting Requirement**").

The Commission's customer protection regime is a critical component of vibrant and sound commodity derivatives markets. LX agrees that strengthening safeguards for Proprietary Funds is an important step to safeguarding all funds held by DCOs and one that aligns with the current practices of many DCOs that have implemented comparable protections. LX applauds the Commission for taking this step and fully supports the overall goal of the Proposal. The Commission requested specific comment on several aspects of the Proposal, and LX responds to those that pertain to it herein.

First, the Commission requested specific comment whether "classification of guaranty fund contributions as proprietary funds inhibit DCOs' current guaranty fund programs." LX currently clears only fully-collateralized products and thus does not maintain a guaranty fund. However, LX notes that DCOs that clear products on margin maintain a guaranty fund to which all clearing members contribute to mutualize the loss associated with a clearing member default. In the event of a clearing member default at a DCO that does maintain a guaranty fund, the DCO will deploy financial resources to cover any losses associated with the default according to a pre-established order ("**Default Waterfall**"). It is common for a Default Waterfall to include use of non-defaulting clearing members' Proprietary Funds that have been earmarked for the guaranty fund. LX believes the Commission's explicit statement that a DCO may use Proprietary Funds for this purpose is sufficient and that the Proposal does not inhibit a DCO's use of Proprietary Funds for such purpose.

The Commission also requested specific comment whether the Commission should expand the Reconciliation Reporting Requirement so that the daily calculation and reconciliation required by the Proposal would be reported to the Commission daily irrespective of whether there was a discrepancy between the calculation and the amount of Proprietary Funds or Customer Funds that the DCO holds for each clearing member. LX does not believe the Commission should

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<sup>13</sup> Commercial banks would be required to provide the acknowledgement letter in the form of a template provided by the Commission; central banks of a money center country would be permitted to provide their own written acknowledgement stating that (i) the bank was informed that the funds deposited with it are Proprietary Funds and (ii) that the bank agrees to respond to requests from the Commission for information about the account, including the account balance.

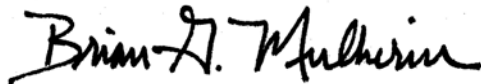
require reporting when no discrepancy exists, as it would provide the Commission with no additional information than under the Proposal (where the Commission should know that no discrepancy exists by virtue of the DCO not filing a report).

Finally, the Commission requested comment whether it should impose anti-money laundering or know-your-customer requirements on DCOs offering Non-Intermediated Clearing.<sup>14</sup> Under the terms of the LX Registration Order, LX is currently required to comply with anti-money laundering and know-your-customer provisions located in the Bank Secrecy Act, the International Emergency Economic Powers Act, the Trading with the Enemy Act, and the executive orders and regulations issued pursuant thereto (including those issued by the Department of the Treasury) as if LX were a “financial institution” within the meaning of the Bank Secrecy Act.<sup>15</sup> LX takes these responsibilities seriously and believes they are core elements of an effective Customer Fund and Proprietary Fund safeguarding regime. As such, LX would fully support a requirement that Non-Intermediated DCOs adhere to applicable federal laws and regulations as if they were “financial institutions” under the Bank Secrecy Act.

## **V. Conclusion**

LX appreciates the opportunity to comment on the Proposal and fully supports the Commission’s goal of establishing comprehensive protection of Proprietary Funds held by DCOs. LX believes this Proposal would codify sound practices regarding the safeguarding of Proprietary Funds to which it already adheres and is an important step to ensuring that DCOs providing Non-Intermediated Clearing are doing so in a manner that safeguards Proprietary Funds. LX looks forward to working with the Commission on this important issue going forward and respectfully requests the Commission consider its comments on the Proposal.

Sincerely,



Brian Mulherin  
General Counsel

cc: Honorable Chairman Rostin Behnam  
Honorable Commissioner Christy Goldsmith Romero  
Honorable Commissioner Kristen N. Johnson  
Honorable Commissioner Summer K. Mersinger  
Honorable Commissioner Caroline D. Pham

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<sup>14</sup> DCOs are not “financial institutions” under the Bank Secrecy Act and thus are not generally subject to anti-money laundering or know-your-customer requirements. FCMs are “financial institutions” and thus are required to maintain anti-money laundering and know-your-customer surveillance programs for their customers. DCOs that permit FCMs to clear for customers reap the benefit of these programs.

<sup>15</sup> See LX Registration Order, available at <https://www.cftc.gov/PressRoom/PressReleases/8230-20>, paragraph 8.