

MEMO# 32553

June 24, 2020

ICI Draft Comment Letter to CFTC on Proposed Amendments to Part 190 Bankruptcy Regulations - Your Comments Requested by July 2

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June 24, 2020 TO: Derivatives Markets Advisory Committee RE: ICI Draft Comment Letter to CFTC on Proposed Amendments to Part 190 Bankruptcy Regulations - Your Comments Requested by July 2

On April 14th, the Commodity Futures Trading Commission (CFTC or “Commission”) unanimously approved proposed amendments to its Part 190 bankruptcy regulations. The Commission’s proposal (“Proposal”) is intended to comprehensively update Part 190 for the first time in 37 years to reflect current market practices and lessons learned from past commodity broker bankruptcies. Comments on the proposal are due on July 13th.

ICI, with the assistance of our outside counsel at Cleary Gottlieb, has prepared the attached draft comment letter for your review and feedback. Please provide your written comments on the letter to Sarah Bessin at sarah.bessin@ici.org no later than Thursday, July 2nd. The draft comment letter is summarized below.

ICI’s letter supports the Proposal, which would enhance customer protection and bring needed clarity and modernization to the commodity broker liquidation process. We express concern, however, that certain aspects of the Proposal would harm public customers and cause uncertainty. We urge the Commission to address these concerns before adopting final rules.

ICI’s letter supports the Commission’s efforts to revise Part 190 in order to enhance customer 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.

The letter explains that these enhancements will limit the extent to which the failure of a futures commission merchant (FCM) or a derivatives clearing organization (DCO) will cause losses to public customers or market disruption. The letter also notes 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.

The letter 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. 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.

The letter expresses concern, however, that certain components of the Proposal would harm public customers and cause uncertainty. 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 govern the liquidation of a DCO. However, DCO rules currently lack the clarity, 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 allow existing DCO rules to override Part 190's fundamental protections. 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, rather than on a unilateral 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 override Part 190's fundamental customer protections. Until then, the substantive provisions of Part 190, as adopted by the Commission through notice and comment, should govern the liquidation of a DCO.

The letter explains 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 rules thereunder; and (ii) exercise any discretion granted to it with respect to the other requirements of Part 190 for the benefit of public customers.

Sarah A. Bessin
Associate General Counsel

[Attachment](#)

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