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The Honorable Mary Schapiro
Chairman
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Recent CFTC Action on Money Market Mutual Funds

Dear Chairman Schapiro:

I want to call to your attention a recent action by the Commodity Futures Trading Commission ("CFTC") confirming that agency's positive view of the liquidity and stability of money market mutual funds ("MMFs"), as well as their utility for investment of customer segregated funds. In adopting amendments to its Regulation 1.25,[1] the CFTC retains MMFs as a permitted investment under Regulation 1.25, permits unlimited investments in Treasury-only MMFs and up to a 50 percent asset-based concentration in other MMFs, subject to limits on investments in smaller MMFs.

Regulation 1.25 is the principal CFTC rule establishing safeguards for the investment of customer segregated funds by futures commission merchants ("FCMs") and derivatives clearing organizations ("DCOs").[2] As the CFTC has stated, "[C]ustomer segregated funds must be invested in a manner that minimizes their exposure to credit, liquidity, and market risks both to preserve their availability to customers and DCOs and to enable investments to be quickly converted to cash at a predictable value in order to avoid systemic risk."[3] Regulation 1.25 therefore establishes a general prudential standard that all permitted investments be "consistent with the objectives of preserving principal and maintaining liquidity."[4]

Beginning in 2007 with a review by the CFTC's Division of Clearing and Intermediary Oversight in 2007, a reassessment following the events of 2008, an Advance Notice of Proposed Rulemaking in May 2009, a Notice of Proposed Rulemaking in October 2010 ("Proposing

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[1] *Investment of Customer Funds and Funds Held in an Account for Foreign Futures*, RIN 3038-AC79, __ FR _____ (Dec. 5, 2011) ("Release").

[2] 17 C.F.R. § 1.25.

[3] Release at 5.

[4] *Id.* at 6, citing 17 C.F.R. § 1.25(b).

Release"), and a review and assessment of dozens of public comments received in connection with the various releases, the CFTC sought to evaluate and, where appropriate, modify the range of permitted investments in Regulation 1.25.[5] Based upon this review and the extensive public record, the CFTC, in its final rule, eliminated a number of previously permitted investments (most commercial paper and corporate notes or bonds, foreign sovereign debt, in-house transactions), but retained MMFs as permitted investments.[6] The CFTC also pared back its initial proposal to establish a 10 percent asset-based concentration limit for investments in MMFs and, instead, in the final rule permitted unlimited investments in Treasury-only MMFs, and a 50 percent asset-based concentration limit for all other MMFs, in both cases subject to limits on investment in small MMFs.[7] In addition, the CFTC revised its proposal to limit investments in any Money Fund family of funds to two percent of total assets held in segregation, and adopted in its final rule no family-of-funds or issuer-based concentration limit for MMFs that consist entirely of Treasuries, and a 25 percent family of funds issuer-based limit as well as a 10 percent individual fund issuer-based limit for all other MMFs.[8]

The Release states that commenters discussed a variety of topics, including the safety of MMFs, the recent enhancements of Securities and Exchange Commission ("SEC") Rule 2a-7, a comparison of the safety of MMFs to other permitted investments, the appropriate concentration limits for MMFs, and the potential problems that would arise as a result of a 10 percent concentration limit, among other matters.[9] Commenters stressed that MMFs are safe, liquid investments and that only two funds in the 40-year history of MMFs have failed to return $1 per share to investors.[10] Commenters also noted that recent enhancements to SEC Rule 2a-7 have made MMFs even safer and more prepared to withstand heavy redemption requests and have increased Money Fund transparency.[11] Commenters also compared the safety and liquidity of MMFs to other permitted investments, including Treasuries and municipal bonds.[12]

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[5] *See* Release pp. 6-10.

[6] *Id.* at 17-33, 48-51.

[7] *Id.* at 48-50.

[8] *Id.* at 53-54.

[9] *Id.* at 42.

[10] *Id.* at 43.

[11] *Id.*

[12] *Id.* at 43-44.

The Release also states that commenters noted that the proposed concentration limit on Money Fund investment could lead to greater risk of loss, for example, because more funds might be held in cash at banks (with only $250,000 FDIC insurance) or because funds would hold large amounts of Treasuries, which could experience potential loss in the secondary market.[13] Commenters also warned that the proposed concentration limit on MMFs could decrease diversification, instead of increase it, and could force FCMs and DCOs to self manage accounts, placing customer funds at greater risk.[14]

In permitting an FCM or DCO to invest all of its customer segregated funds in Treasury-only MMFs, subject to limits applicable to smaller funds, the Release states that the CFTC "agrees with commenters that since an FCM or DCO may invest all of its funds in Treasuries directly, an FCM or DCO therefore should be able to make the same investments indirectly" via a Money Fund.[15] For MMFs other than Treasury only funds, the Release states that the CFTC was persuaded to increase the proposed concentration limit from 10 percent to 50 percent by commenters who noted that MMFs are "safe and liquid relative to other permitted investments."[16] Importantly, the Release states that the CFTC was cognizant of the potential unintended consequences of decreasing investment options and "over-concentrating customer funds into a small universe of viable investments."[17] It further notes the importance of providing FCMs and DCOs with "the ability to delegate investment decisions for their entire portfolio of customer segregated funds" to MMFs, should the FCMs and DCOs not wish to make such decisions on their own.[18]

The CFTC's action is an endorsement of the SEC's comprehensive and effective oversight and regulation of MMFs, and its 2010 amendments to 2a-7 in particular. As the CFTC states in its Release, "[C]ustomer segregation is the foundation of customer protection in the commodity, futures and swaps markets" and customer segregated funds "most be invested in a manner which preserves principal and maintains liquidity … ."[19] The CFTC, after a multi-year review and careful consideration of an extensive public record, affirmed the use of MMFs for this purpose and, moreover, acknowledged that limiting the ability of FCMs and DCOs to use

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13 *Id.* at 45.

14 *Id.* at 45-46.

15 *Id.* 48.

16 *Id.* 49.

17 *Id.*

18 *Id.*

19 *Id.* at 32.

MMFs for investment of customer funds could have the unintended result of putting customer funds at greater risk.

The CFTC's action not only endorses the SEC's actions and role with respect to MMFs, but emphasizes the tremendous utility of using MMFs as a vehicle for safeguarding funds "at a predictable value."

I urge the SEC to take note of this action in considering the effectiveness of its current regulation of MMFs and in fully evaluating the potential for unintended consequences of regulation that would diminish their utility in any way.

Sincerely,

Jerry

John D. Hawke, Jr.

cc: The Honorable Luis A. Aguilar
The Honorable Daniel M. Gallagher, Jr.
The Honorable Troy A. Paredes
The Honorable Elisse B. Walter
Eileen P. Rominger
Robert E. Plaze