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September 30, 2011

Mr. David A. Stawick  
Secretary  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21st Street, N.W.  
Washington, D.C. 20581

Re: Customer Clearing Documentation and Timing of Acceptance for Clearing (RIN 3038-AD51)

Dear Mr. Stawick:

The Investment Company Institute<sup>1</sup> (“ICI”) welcomes the opportunity to comment on the Commodity Futures Trading Commission’s (“Commission” or “CFTC”) Notice of Proposed Rulemaking on the appropriate documentation between a customer and a futures commission merchant (“FCM”) that clears on behalf of the customer and the timing of acceptance or rejection of trades for clearing by derivatives clearing organizations (“DCOs”) and clearing members.<sup>2</sup> As customers in the swaps markets, both of these issues are important to our members – registered investment companies – because they pertain to customer access to clearing and risk management through timely clearing.<sup>3</sup>

As part of the migration to centralized clearing and exchange trading, the Commission’s rules should ensure that all swap market participants that meet appropriate criteria have open access to all available counterparties, clearing houses, and trading venues. The Commission’s intent in proposing

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<sup>1</sup> ICI is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding and otherwise advance the interests of funds, their shareholders, directors, and advisers. Members of ICI manage total assets of \$12.9 trillion and serve over 90 million shareholders.

<sup>2</sup> Customer Clearing Documentation and Timing of Acceptance for Clearing, 76 Fed. Reg. 45730 (August 1, 2011).

<sup>3</sup> For purposes of this letter, the term “funds” will be used to refer to registered investment companies, including mutual funds, closed-end funds and ETFs.

the rules regarding customer clearing documentation is primarily to accomplish this goal, which underlies the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”). ICI strongly supports the prohibitions in the proposed rules because they should provide a uniform starting point for clearing documentation between customers and FCMs, swap dealers (“SDs”) and major swap participants (“MSPs”), and preserve flexibility when trading swaps.

In addition, ICI supports the proposed rules to shorten the time frame for acceptance or rejection of trades by DCOs and clearing members. They should increase certainty regarding, and result in faster matching for, swaps trades, which should reduce risk associated with prolonged exposures to the market.

### Customer Clearing Documentation

#### *Background*

The proposed rules would prohibit specific terms in execution-related contracts involving FCMs, DCOs, SDs, and MSPs for swaps that are intended to be cleared. The Commission explains these rules were proposed in response to the recently issued FIA-ISDA Cleared Derivatives Execution Agreement (hereinafter, “template”).<sup>4</sup> The template was designed to assist swap market participants in negotiating execution agreements with counterparties to swaps that are intended to be cleared. It was a highly negotiated project in which some of our members participated. Funds have concerns with the template but believe, as customers in the swaps markets, that the final document was an improvement from where it started. Importantly, funds believe that the document should be recognized for what it is – a voluntary template that establishes a starting point for negotiation between the counterparties to an execution agreement.<sup>5</sup> The template includes two parts, a core document to be used for bilateral agreements and an addendum to be used for trilateral agreements. The proposed rules appropriately would address the addendum only.<sup>6</sup>

#### *Framework for Customer Protection*

We support the Commission’s efforts to satisfy the Dodd-Frank Act’s principles of ensuring that customers have open access to clearing and exchange trading. The proposed rules would prohibit contractual provisions between FCMs, SDs, MSPs, and DCOs from including certain restrictions that

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<sup>4</sup> FIA is the Futures Industry Association and ISDA is the International Swaps and Derivatives Association. The template is available at [www.futuresindustry.org](http://www.futuresindustry.org). See press release, “FIA and ISDA Publish Documentation for Cleared Swaps” (June 16, 2011).

<sup>5</sup> The press release announcing the template noted that it may not be necessary or appropriate under all circumstances. See *supra* note 4.

<sup>6</sup> In commenting on the template, our remarks in this letter are therefore directed at the addendum, through which a clearing member could become a party to the template and set a limit on its customer’s swap exposure.

could infringe on these principles by, for example, disclosing the identity of a customer's counterparty, restricting a customer's choice of counterparty, or delaying acceptance of trades. These prohibitions should protect swap customers from discriminatory behavior by clearing members or counterparties and help ensure that customers have open access to the markets and an opportunity to obtain execution on competitive terms.

Further, underlying the proposed rules is the Dodd-Frank Act goal of reducing risk in the swaps markets, and the U.S. financial system generally, by aiding in the transition from swap transactions executed in the bilateral over-the-counter ("OTC") market to the framework of centralized clearing and exchange trading. A smooth transition will be essential to minimizing disruption in the swaps markets. The Dodd-Frank Act creates an entirely new framework for trading and clearing swaps. The rules implementing the framework are still being developed and the framework itself is still evolving. Definitive and clear rules ensuring fair and level treatment for customers at the outset are therefore particularly integral to a successful migration as well as the future of the swaps markets.<sup>7</sup>

Moreover, the significance of strong unambiguous rules is particularly important with respect to limits on customer access that could be imposed by potential clearing members or counterparties. As envisioned by the Dodd-Frank Act, such proposed rules will lay the foundation for swap trading by preventing FCMs, SDs, and MSPs from entering into arrangements with customers that inappropriately limit open access to clearing and trading by entering, or in the case of DCOs, preventing an FCM from being required to enter, into such an agreement. Without the proposed rules, customers using the template could be subject to agreements that could, for example, increase customer and systemic risk by delaying, limiting, or blocking access to clearing; increase costs and reduce market efficiency by limiting the number of counterparties available for trading and imposing additional administrative and documentary burdens; or restrict access to clearing by limiting the potential clearing members with which a customer could interact.

With the proposed rules in place, the parties to a swap transaction would begin their negotiations with the template. The proposed rules would ensure that contractual limitations would not infringe on open access to clearing and trading by providing all customers with basic protections. It would be left to the parties, however, to negotiate the specific terms of the contractual agreement. In the case of smaller customers, whose influence in negotiations would be limited, this baseline protection would be particularly important. Yet all market participants – regardless of size – would benefit from the minimum level of protections provided by the proposed rules because they would ensure continued broad participation in the swaps markets during the period of transition to the new clearing and trading framework.

In addition, it would be critical that the Commission regularly monitor for and enforce any efforts to directly or indirectly circumvent the rules and their intended purpose of providing open

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<sup>7</sup> While ICI fully supports the proposed rules, we note that there may be circumstances for which guiding principles provide the appropriate regulatory approach.

access to clearing and trading as set forth in the Dodd-Frank Act. Compliance with the proposed rules could be built into the registration obligations of FCMs, SDs, MSPs, and DCOs.

#### Time Frames for Acceptance into Clearing

ICI supports the proposed rules to tighten the time frames for clearing members and DCOs to accept or reject swap trades submitted for clearing. Requiring definitive action as quickly as technologically possible if fully automated systems are used (*i.e.*, real-time), as set forth in the proposed rules, should result in prompt, efficient and accurate processing of trades – providing certainty to counterparties regarding the status of their trades.<sup>8</sup> We agree with the Commission that such an outcome would minimize risk stemming from the lapse of time between trade execution and acceptance into clearing by, for example, reducing the time during which exposures can accumulate when a trade is rejected and preventing market participants from acting on bad information by trading under a faulty presumption that an initial trade has cleared. The proposed real-time acceptance requirement could also improve the quality of counterparties with bids and offers posted in a limit order book. A DCO charged with quickly screening trades against applicable product and credit criteria before accepting or rejecting them is likely to pre-screen for credit-worthiness of customers.

Further, the Commission could eliminate the need for execution agreements generally by moving toward real-time acceptance requirements for clearing. By reducing the risk of failed trades, and therefore eliminating the need for tri-party agreements, such requirements would address the concerns articulated in the Commission's proposed rules relating to customer clearing documentation. Execution agreements are required as a means to provide protection during a period of exposure to counterparty credit risk by calculating and apportioning damages in the event that a trade is rejected or fails. The proposed real-time acceptance requirements would remove the justification for such agreements by eliminating the period of exposure for those swaps in which fully automated systems are used for clearing.

For the same reasons discussed above, we are supportive of the proposed time frames for over-the-counter swaps and other swaps executed non-competitively on or subject to the rules of a DCM or SEF.

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<sup>8</sup> The Commission should consider whether a delay may be necessary to accommodate allocation of trade blocks.

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If you have any questions on our comment letter, please feel free to contact me directly at (202) 326-5815, Heather Traeger at (202) 326-5920 or Sarah Bessin at (202) 326-5835.

Sincerely,

/s/ Karrie McMillan

Karrie McMillan  
General Counsel

cc: Honorable Gary Gensler, Chairman  
Honorable Michael Dunn, Commissioner  
Honorable Jill E. Sommers, Commissioner  
Honorable Bart Chilton, Commissioner  
Honorable Scott D. O' Malia, Commissioner