



April 26, 2004

Ms. Jean A. Webb
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

Mayer, Brown, Rowe & Maw LLP
190 South La Salle Street
Chicago, Illinois 60603-3441

Main Tel (312) 782-0600
Main Fax (312) 701-7711
www.mayerbrownrowe.com

Kenneth M. Rosenzweig
Direct Tel (312) 701-8354
Direct Fax (312) 706-9105
krosenzweig@mayerbrownrowe.com

**Re: Global Clearing Link — Segregated Funds
and Secured Amount Requirements**

Dear Ms. Webb:

We are writing on behalf of our client, The Clearing Corporation, to request that the Commodity Futures Trading Commission (the “Commission”) take steps to permit The Clearing Corporation and futures commission merchants (“FCMs”) to establish and maintain combined original margin and variation settlement accounts for U.S. Dollar- and Euro-denominated products in the circumstances described herein.

The Global Clearing Link. When fully implemented, the Global Clearing Link between The Clearing Corporation and Eurex Clearing Frankfurt, AG (“Eurex Clearing” and, together with The Clearing Corporation, the “Clearing Houses”) will give market participants the choice of clearing U.S. Dollar-denominated contracts traded on U.S. Futures Exchange LLC (“USFE”) and certain Euro-denominated contracts traded on USFE and Eurex Frankfurt, AG (“Eurex”); together with USFE, the “Exchanges”) through either The Clearing Corporation or Eurex Clearing.

Subject to the receipt of all required regulatory approvals, the Global Clearing Link will offer important benefits for the members of both clearing houses and for other market participants. These include, among other things, the ability of firms that are Clearing Corporation participants or members of Eurex Clearing to clear contracts made on USFE and Eurex without having to become a member of the other Clearing House; full fungibility for benchmark Euro-denominated interest rate and stock index products, regardless of whether they are traded on USFE or Eurex and cleared at The Clearing Corporation or Eurex Clearing; and a single collateral pool, with associated portfolio margining benefits, for correlated U.S. Dollar-denominated and Euro-denominated contracts.

The Clearing Corporation and Eurex Clearing propose to introduce the Global Clearing Link in two phases. Phase I would involve the clearing, at either The Clearing Corporation or Eurex Clearing, of Euro-denominated products traded on Eurex and approved for trading by U.S.

Brussels Charlotte Chicago Cologne Frankfurt Houston London Los Angeles Manchester New York Palo Alto Paris Washington, D.C.
Independent Mexico City Correspondent: Jauregui, Navarrete, Nader y Rojas, S.C.

Mayer, Brown, Rowe & Maw LLP operates in combination with our associated English limited liability partnership in the offices listed above.

Ms. Jean A. Webb
April 26, 2004
Page 2

persons (the “Euro Link”).¹ Phase II would extend the principles of the Global Clearing Link to permit the clearing of U.S. Dollar-denominated contracts traded on USFE at either The Clearing Corporation, as is the case currently, or at Eurex Clearing (the “U.S. Dollar Link”), as well as the listing on USFE of Euro-denominated products that are traded on Eurex with the option of clearing those contracts at either The Clearing Corporation or Eurex Clearing (“Cross-Listing”).²

Such an arrangement would ordinarily require firms wishing to clear contracts traded on one of the Exchanges to be a member of the Primary Clearing House for that Exchange (*i.e.*, The Clearing Corporation for USFE and Eurex Clearing for Eurex). One of the advantages of the Global Clearing Link, however, is that it will make these duplicate clearing memberships unnecessary. The Global Clearing Link accomplishes this objective by interposing the two Clearing Houses as “Special Clearing Members” of each other. Each Clearing House, therefore, will maintain an omnibus Special Clearing Member account on the books of the other, “Home Country Clearing House” in which it will carry the trades and positions of its clearing members or participants. The obligations of the Primary Clearing House will extend to its Special Clearing Member, but not to the Special Clearing Member’s participants or clearing members. Conversely, it is the Special Clearing Member, and not its participants or clearing members, that is contractually obligated to the Primary Clearing House for the performance of its participants’ or members’ obligations.

The Clearing Corporation will act as the Home Country Clearing House for all Dollar-denominated contracts; Eurex Clearing, in turn, will act as the Home Country Clearing House for all Euro-denominated products (regardless of whether they are traded on Eurex or USFE). The Home Country Clearing House will administer the payment and collection of variation margin, assign delivery notices and option assignments, and administer the delivery process for all of its “home country” contracts, treating the Special Clearing Member (that is to say, the other Clearing House) as though it were a clearing participant or clearing member carrying the accounts of other clearing firms on an omnibus basis. A Special Clearing Member, therefore, will be ultimately responsible to the Home Country Clearing House for the timely payment of

¹ As used herein, the term “Euro Link” refers to the clearing of the following Eurex-traded contracts at The Clearing Corporation (as opposed to Eurex Clearing): Dow Jones Global Titans 50 Future; Dow Jones STOXX 50 Future; Dow Jones EURO STOXX 50 Future; Dow Jones STOXX 600-Banks-Future; Dow Jones Euro STOXX-Banks-Future; DAX Future; One-Month EONIA Future; Three-Month EURIBOR Future; Options on Three-Month EURIBOR Future; Euro SCHATZ Future; Options on Euro SCHATZ Future; Euro BOBL Future; Options on Euro BOBL Future; Euro Bund Future; Options on Euro Bund Future; and Euro BUXL Future.

² It bears emphasis that while we have, in the interest of simplicity, characterized Euro-denominated contracts traded on Eurex and Dollar-denominated contracts traded on USFE as capable of being “cleared” at either Clearing House, those contracts will in fact be cleared only at the “Primary Clearing House” for each Exchange — *i.e.*, The Clearing Corporation for all trades made on USFE, and Eurex Clearing for all trades made on Eurex. It is the Primary Clearing House — and only the Primary Clearing House — that will act as the central counterparty and be responsible to its clearing members and participants for the performance of all contracts made on the Exchange for which it is the Primary Clearing House.

Ms. Jean A. Webb
April 26, 2004
Page 3

variation margin and the performance of all other obligations, such as deliveries and the exercise of options, by its members or participants.

The Global Clearing Link is designed, however, to allow clearing members and participants to take day-to-day control over and responsibility for the trades and positions in their accounts. Thus, the Global Clearing Link anticipates that Clearing Corporation participants will establish their own Euro-denominated bank accounts and securities accounts for the purpose of effecting daily variation margin settlements and deliveries. As a legal matter, Eurex Clearing will act as The Clearing Corporation's agent when it debits and credits the accounts of Clearing Corporation participants. In other words, rather than establish its own Euro settlement and delivery systems and dealing exclusively with its participants, The Clearing Corporation has authorized Eurex Clearing to act as The Clearing Corporation's agent for this purpose and administer these processes on a day-to-day basis.³ The Clearing Corporation nonetheless remains fully responsible (as Special Clearing Member and "Destination Clearing House" for its clearing participants) in the event that one or more of its clearing participants fails to discharge its obligations timely and in full.

The Destination Clearing Houses will collect original margin from their respective clearing members and participants.⁴ The logic of this is apparent when one recalls that it is the Destination Clearing House (The Clearing Corporation for its participants, Eurex Clearing for its members) that is responsible for the performance of its members or participants. This is true where the Home Country Clearing House is also the Destination Clearing House (as would be the case where a trade in Treasury Bonds or Notes is cleared at The Clearing Corporation). It also is true where the Home Country Clearing House is not also the Destination Clearing House (as would be the case where a trade in Bunds or the Bobl or Schatz is made on Eurex but cleared at The Clearing Corporation).

The net effect of these arrangements is that Clearing Corporation participants are expected to establish Euro-denominated accounts at banks in Frankfurt for the purpose of effecting variation margin settlements in Euro Link products. At the same time, Clearing

³ The Link Clearing Agreement between The Clearing Corporation and Eurex Clearing permits The Clearing Corporation to act for its participants in effecting variation margin settlements. In other words, The Clearing Corporation would in such circumstances establish the necessary banking relationships for its clearing participants, thereby making it unnecessary for them to do so themselves. Although The Clearing Corporation has had preliminary discussions with some of its clearing participants about the desirability of such an arrangement, The Clearing Corporation does not yet know to what extent its participants will want to avail themselves of this facility (as opposed to establishing and/or maintaining their own banking arrangements).

⁴ The Clearing Corporation will be the Destination Clearing House for its clearing participants. Eurex Clearing similarly will be the Destination Clearing House for its clearing members. In the event that a firm is a member of both Clearing Houses, it will be required to designate either The Clearing Corporation or Eurex Clearing as its Destination Clearing House.

Ms. Jean A. Webb
April 26, 2004
Page 4

Corporation participants will deposit original margin with The Clearing Corporation for Euro Link contracts and for Treasury products traded on USFE.⁵

Segregation Requirements. Section 4d(a)(2) of the Commodity Exchange Act (the “Act”) and Commission Regulations 1.20 – 1.30, 1.32 and 1.36 (collectively, the “Segregation Requirements”) govern the segregation of customer funds for transactions effected on a contract market such as USFE. In general, the segregation requirements are designed to ensure that money, securities or property that have been deposited by a customer for use in connection with futures and option contracts traded on a contract market under the Act are not applied to any other purpose without the customer’s consent. Interpretative Letter No. 86-2, Comm. Fut. L. Rep. ¶22,933 (Feb. 18, 1986). Section 4d(a)(2) accordingly prohibits an FCM from commingling customer funds with its own funds, and further prohibits an FCM from using its customers’ money, securities or property to margin, guarantee or secure its own trades and positions. A clearing organization, in turn, is prohibited by Section 4d(a)(2) from using funds that have been deposited into a segregated account for the benefit of anyone other than the customers of the depositing FCM.

The general requirements of Section 4d are amplified by the provisions of Commission Regulation 1.20. Specifically, Regulation 1.20(a) prohibits an FCM from using any portion of “customer funds” for any purpose other than to purchase, margin, guarantee, secure, transfer, adjust or settle the contracts, trades or commodity options of the customers or option customers of such futures commission merchant.⁶ Regulation 1.20(b), in turn, requires a derivatives

⁵ The foregoing is descriptive of the arrangements that are being put into place to facilitate Phase I (the Euro Link) and, subject to further approvals by the Commission, the Cross-Listing of Euro products on USFE as part of Phase II. Assuming the receipt of all required approvals, reciprocal arrangements involving the establishment by members of Eurex Clearing of U.S. dollar bank and delivery accounts in the United States will be required to give effect to the Phase II U.S. Dollar Link.

⁶ The term “customer funds” is defined by Commission Regulation 1.3(gg) as follows:

Customer funds. This term means all money, securities, and property received by a futures commission merchant or by a clearing organization from, for, or on behalf of, customers or option customers:

(1) In the case of commodity customers, to margin, guarantee, or secure contracts for future delivery on or subject to the rules of a contract market and all money accruing to such customers as the result of such contracts; and

(2) In the case of option customers, in connection with a commodity option transaction on or subject to the rules of a contract market –

(i) To be used as a premium for the purchase of a commodity option for an option customer;

(ii) As a premium payable to an option customer;

(iii) To guarantee or secure performance of a commodity option by an option customer; or

(iv) Representing accruals (including, for purchasers of a commodity option for which the full premium has been paid, the market value of such commodity option) to an option customer....

Ms. Jean A. Webb
April 26, 2004
Page 5

clearing organization separately to account for and to segregate all customer funds that are received by the clearing organization from a clearing member to margin, guarantee or secure the trades or positions of the clearing member's commodity or option customers, terms defined in Commission Regulations 1.3(k) and 1.3(jj) to exclude persons trading foreign futures and options. Regulation 1.20(b) additionally requires a derivatives clearing organization to maintain separate, segregated bank accounts to hold the customer funds of its clearing members.

Regulations 1.22 and 1.24 establish supplementary requirements that are directly applicable only to futures commission merchants. In particular, Regulation 1.22 provides that “[c]ustomer funds shall not be used to carry trades or positions of the same commodity and/or option customer other than in commodities or commodity options traded through the facilities of a contract market.” Finally, Regulation 1.24 effectively prohibits an FCM from depositing with a clearing organization money which it may use for any purpose other than to purchase, margin, guarantee, secure, transfer, adjust or settle the contracts, trades or commodity options of the customers or option customers of such futures commission merchant.

Secured Amount Requirements. Commission Regulation 30.7 sets forth analogous requirements for funds deposited in connection with trading by “foreign futures or foreign options customers” – *i.e.*, customers located in the U.S. who trade “foreign futures” or “foreign options” on or subject to the rules of a foreign board of trade (as defined in Commission Regulation 30.1(a)-(c)). In particular, Regulation 30.7 requires FCMs to maintain in a separate account money, securities and property in an amount at least equivalent to the “foreign futures or foreign options secured amount.” Regulation 30.7(d) nonetheless prohibits FCMs from commingling in the same account or accounts money, securities and property representing the foreign futures or foreign options secured amount with customer funds required to be separately accounted for and segregated on behalf of commodity and option customers. *See* Interpretive Letter No. 90-7, Comm. Fut. L. Rep. (CCH) ¶ 24,826 (May 1, 1990).

Although The Clearing Corporation is not directly subject to the requirements of Regulation 30.7, which apply only to FCMs whose customers trade foreign futures or foreign options, Euro Link transactions – *i.e.*, futures and option transactions executed on Eurex and cleared at The Clearing Corporation – ordinarily would be treated as foreign futures and foreign option transactions that are subject to secured amount requirements of Regulation 30.7. Thus, absent Commission action, The Clearing Corporation and its FCM participants will be required to reprogram their systems and establish new banking relationships in order to ensure that margin deposited to secure Euro Link transactions at The Clearing Corporation is not commingled with margin deposited to secure customers' USFE trades that also are cleared at The Clearing Corporation.

Requested Relief. Section 4d(a)(2) authorizes the Commission to permit an FCM to commingle and deposit money, securities and property that is otherwise required to be segregated pursuant to Section 4d(a)(2) “with any other funds money, securities or property received by such futures commission merchant and required by the Commission to be separately accounted for and treated and dealt with as belonging to the customers of such futures”

Ms. Jean A. Webb
April 26, 2004
Page 6

commission merchant” (emphasis added). Unlike the Commission’s Regulations, the Act makes no distinction between “customers” and “option customers” on the one hand and “foreign futures and foreign options customers” on the other. The Commission has, therefore, previously construed this authority to permit the commingling of segregated funds with funds deposited to margin, guarantee or secure foreign futures transactions.⁷

Rule 30.10 separately permits any party adversely affected by any of the requirements in Part 30 of the Commission’s Regulations to petition the Commission for an exemption from those requirements. Among other things, the Commission has exercised this authority to permit firms subject to regulation by the Financial Services Authority in the United Kingdom to offer certain U.S. customers the ability to “opt out” of otherwise-applicable segregation requirements.⁸

Consistent therewith, The Clearing Corporation hereby requests that The Clearing Corporation and futures commission merchants be permitted to deposit and maintain variation, original and initial margin deposits for Euro Link transactions in segregated funds, rather than in separate secured amount, accounts.⁹

The practical and legal effects of this aspect of the requested relief are twofold. *First*, customers will benefit from having their positions held in a combined account because The Clearing Corporation and the customer’s carrying FCM will be able to apply portfolio margining principles to the customer’s positions.¹⁰ This reduces systemic risk (since highly correlated positions are a better proxy for risk than cash or other forms of margin deposits). In addition, this approach also permits a more efficient use of resources – instead of maintaining separate segregated and secured amount accounts for U.S. Dollar and Euro positions that are being cleared at The Clearing Corporation, customers and their FCMs will be able to hold all of a customer’s USFE and Euro Link trades and positions in a single account, thereby making it unnecessary for customers and FCMs to move funds and securities back and forth between segregated and secured amount accounts to satisfy margin requirements.¹¹ *Second*, the requested

⁷ 64 Fed. Reg. 34110, 34111 (June 27, 2001) (MEFF Sociedad Rectora de Productos Financieros de Renta Variable, S.A. (“MEFF”).)

⁸ 68 Fed. Reg. 58583, 58587 (October 10, 2003).

⁹ We are aware that the introduction of the U.S. Dollar Link and Cross-Listing envisioned in Phase II of the Global Clearing Link will require additional regulatory approvals. The relief being requested herein is entirely independent of, and would not necessarily affect, any determinations that may be made by the Commission or the staff in that context.

¹⁰ The relief that we are requesting is not intended in any way to affect the general prohibition on an FCM’s use of one customer’s funds to margin, guarantee or secure the trades of any other person.

¹¹ Funds transfers are not merely burdensome and expensive (particularly if they involve interbank transfers of funds). They also introduce the risk of errors (such as incorrect bank or brokerage account numbers on wire transfer instructions) and of temporary systems failures that can result in customer accounts being undermargined – or worse, undersegregated or undersecured – even though funds were intended to be transferred from the companion segregated or secured amount account to cover that shortfall.

Ms. Jean A. Webb
April 26, 2004
Page 7

relief will ensure that all of a customer's funds – including those deposited in connection with Euro Link transactions – will be governed by the Segregation Requirements rather than the less rigorous “secured amount” requirements of Regulation 30.7.¹² An FCM whose customers trade through the Euro Link, therefore, would be required to hold customer funds associated with trades made on USFE and Eurex in a manner consistent with the Segregation Requirements.

The Clearing Corporation believes that the protections afforded to U.S. customers by its risk management procedures (including, among other things, Clearing Corporation original margin requirements, capital requirements for clearing participants, and a Guaranty Fund which increases in size commensurate with increases in volume and margin on deposit), when coupled with the comprehensive safeguards embodied in the Global Clearing Link, are more than sufficient to protect the funds of customers trading futures and options on futures contracts on USFE or Eurex and held in a segregated funds account in the event of a default by Eurex Clearing or a Clearing Corporation participant. These safeguards are buttressed by the credit support that Eurex Clearing must provide to The Clearing Corporation pursuant to the terms of the Link Clearing Agreement. Finally, we would note that the Commission, having examined the regulatory structure governing transactions that are effected on Eurex and cleared through Eurex Clearing, has concluded that compliance with German legal and regulatory requirements and Eurex rules may appropriately be substituted for compliance with certain provisions of the Act and Commission Regulations.¹³

The Commission and its staff have previously granted relief comparable to that which is being requested by The Clearing Corporation. For example, the Division of Trading and Markets took the position in connection with the Mutual Offset System that had been established between the Chicago Mercantile Exchange (“CME”) and the Singapore International Monetary Exchange (“SIMEX”) that (i) all funds received by an FCM to margin, guarantee or secure a trade effected for a customer of a domestic FCM that was to be cleared at the CME, and all funds accruing as a result of such a trade, must be segregated and separately accounted for pursuant to Section 4d of the Act and the Commission's regulations thereunder; and (ii) other than to identify and mark in its records those Mutual Offset System transactions that are executed on SIMEX, an FCM need not, for segregation purposes, make any distinction between a Mutual

¹² Unlike the amounts that must be set aside in satisfaction of the Segregation Requirements, the secured amount is defined in Regulation 1.3(rr) effectively to exclude excess margin deposits and free credit balances. 52 Fed. Reg. 28980, 28984 (August 5, 1987) (“In essence, the ... secured amount is an amount equal to the money, securities and property held by, or held for or on behalf of [an FCM] ... to margin, guarantee, or secure open foreign contracts....”); *see* Commission Regulation 30.7(a) (FCM must maintain in separate account secured amount sufficient to satisfy FCM's current obligations to foreign futures or foreign option customers). The Commission nonetheless views the two requirements as being similar to each other. *E.g.*, 68 Fed. Reg. 58583, 58585 n.20 (October 10, 2003) (Financial Services Authority).

¹³ 67 Fed. Reg. 30785 (May 8, 2002) (Rule 30.10 relief).

Ms. Jean A. Webb
April 26, 2004
Page 8

Offset System trade executed on SIMEX and cleared at the CME and any other regulated futures contract for which funds required to be segregated can be commingled.¹⁴

Most recently, the Commission issued an Order, pursuant to Sections 4(b) and 4d of the Act and Regulation 30.10, in which it permitted clearing members of the CME to commingle in a single account funds received from customers trading on a contract market (or on a derivatives transaction execution facility) with funds received in connection with the clearing by the CME of futures contracts traded on MEFF.¹⁵ The Commission's Order was conditioned upon the satisfaction by the CME and FCMs of a variety of requirements, all of which are fully satisfied by The Clearing Corporation or are, in a few instances, inapposite. Appendix A to this letter restates each of those requirements, followed by a description of how it would be satisfied in the context of the Global Clearing Link.

Bankruptcy Treatment. The term "commodity broker" is defined by Section 101(6) of the Bankruptcy Code to include a futures commission merchant (as defined in the Act) with respect to which there is a "customer." See Commission Regulation 190.01(f). The term "customer" is defined for this purpose in Section 761(9) of the Bankruptcy Code essentially to mean an entity for whom the FCM deals and that holds a claim against the FCM on account of a "commodity contract." See Commission Regulation 190.01(k). With respect to an FCM, a commodity contract means a "contract for the purchase or sale of a commodity for future delivery on, or subject to the rules of, a contract market or board of trade. . . ." 11 U.S.C. § 761(4) (emphasis added); see Commission Regulation 190.01(g). Euro Link contracts, therefore, will be "commodity contracts" within the meaning of the Bankruptcy Code.

In the event of the bankruptcy of an FCM, all cash, securities and other property, and any proceeds thereof, received by the FCM to margin, guarantee or secure Euro Link trades would be

¹⁴ Interpretative Letter No. 84-19, Comm. Fut. L. Rep. (CCH) ¶22,389 (August 9, 1984). Effectively identical relief was granted in connection with the linkage arrangement between the Commodity Exchange, Inc. and the Sydney Futures Exchange ("SFE"), even though that arrangement was "different in several significant respects" from the CME-SIMEX link. Interpretative Letter No. 86-26, Comm. Fut. L. Rep. (CCH) ¶23,359, at 32,990 (November 17, 1986), *cited with approval*, 52 Fed. Reg. 28980, 28985 n.14 (August 5, 1987) (adopting Part 30 Regulations). The Division of Trading and Markets further required in each case that customers' margin deposits be credited to a segregated account at the point that their trades successfully completed the inter-exchange transfer and substitution process. No such delay is necessary in the context of the Global Clearing Link, since all Euro Link trades made by a customer, and any margin deposited in connection therewith, will be treated as being subject to segregation requirements at all times. Each of the Interpretative Letters also addressed the responsibilities of an FCM in the event that a trade remained open or otherwise did not successfully complete the inter-clearinghouse transfer and substitution process. Although that could occur in the context of the Global Clearing Link only if one of the Clearing Houses were in default, we agree that the FCM should not in such circumstances assess the customer for losses resulting from the failure of the trade to be cleared at The Clearing Corporation. Finally, the Division of Trading and Markets required that segregated customer funds be maintained in accounts in the United States, subject only to a limited exception for foreign customers. That latter requirement has been superseded by the provisions of Commission Regulation 1.49.

¹⁵ 64 Fed. Reg. 34110 (June 27, 2001).

Ms. Jean A. Webb
April 26, 2004
Page 9

deemed to be “customer property” within the meaning of Sections 761(10) and 766 of the Bankruptcy Code and Commission Regulations 190.01(n) and 190.08(a). Euro Link customers, therefore, would be in the same position as they would if they were trading the same contracts on USFE. In short, Euro Link customers would be entitled to the same priority in payment and rights to *pro rata* distribution as are granted to other customers of a debtor commodity broker under Section 766(h) of the Bankruptcy Code.

The question then becomes whether there is any reason why customers who have traded through the Euro Link should not have their trades and associated margin deposits – which have been segregated by their FCM, together with their margin deposits for trades made on USFE and other contract markets – treated as part of the “futures account” class. This is potentially significant because Commission Regulation 190.08(c) provides that “property held by or for the account of a customer, which is segregated on behalf of a particular account class ... must be allocated to the ... account class for which it is segregated....”

The term “account class” is defined in Commission Regulation 190.01(a) to include both “futures accounts” and “foreign futures accounts.” Euro Link transactions, therefore, would appear to be capable of being characterized as falling within either “futures” or the “foreign futures” account class. The Commission has made clear, however, that the reason customers and customer property are allocated to different account classes is to ensure that “differing segregation requirements with respect to different classes of accounts benefit customer claimants based on the class of account for which they were imposed.” 66 Fed. Reg. 57535, 57536 (November 24, 1981). If the requested relief is granted, Euro Link transactions and margin deposits will be subject to the Segregation Requirements as fully as any other futures contract cleared by The Clearing Corporation or other derivatives clearing organizations.¹⁶ There is, therefore, no reason or basis in law to treat Euro Link contracts, and the customers trading such contracts, as belonging to anything other than the “futures account” class.

In summary, treating Euro Link transactions and any margin deposits and accruals associated therewith as “futures accounts” will ensure that customer property that has been held by an FCM subject to the Segregation Requirements is allocated to the customers for whom that property has been held, and not for the benefit of another account class, and that those customers will be able to claim their proper share of a bankrupt FCM’s estate.

* * *

¹⁶ By contrast, trades executed on Eurex and cleared through Eurex Clearing would not be segregated and, therefore, would be treated as part of the “foreign futures account class.”

Ms. Jean A. Webb
April 26, 2004
Page 10

We very much appreciate the Commission's willingness to consider this request. Nancy Brooks, the General Counsel of The Clearing Corporation, and I would be pleased to discuss this further with the Commission or to answer any questions that may arise.

Very truly yours,

/s/

Kenneth M. Rosenzweig

Attachment

cc: James C. Carley
Patrick J. McCarty
John C. Lawton
Lawrence B. Patent
Thomas J. Smith

**A Comparison of the Operational Safeguards Established for the Euro Link
Between The Clearing Corporation and Eurex Clearing with the
Terms and Conditions of the Relief Previously Granted by the Commission
in Connection with the CME-MEFF Linkage¹**

1. CME will maintain a clearing system that will perform the following functions:

a. mark-to-market the prices of DFCs on a daily basis;

b. pay settlement variation and option premium to, and collect settlement variation and option premium from, MEFF and CME clearing members on a daily basis;

Euro Link contracts will be marked to market daily. Clearing Corporation participants clearing Euro Link contracts will receive or make Euro-denominated variation margin payments each morning. Those payments will either be made directly by clearing participants to Eurex Clearing (which will collect and disburse those funds in its capacity as agent for The Clearing Corporation) or to The Clearing Corporation which, as Special Clearing Member, is the party obligated to make variation margin payments to, and entitled to receive variation margin payments from, Eurex Clearing.²

In either case, Eurex Clearing will issue net payment instructions to the bank designated for each Clearing Corporation participant, indicating the amount that is to be paid to or collected from that participant's account. The bank will debit or credit the clearing participant's (or The Clearing Corporation's) account, as applicable. The clearing participant will, in turn, debit or credit the accounts of its customers or its house account. In cases where The Clearing Corporation has provided a Euro variation margin settlement facility for its clearing participants, it will convert the Euro amounts into U.S. dollars and debit or credit the clearing participants' house and customer accounts accordingly.

¹ The italicized text restates the Terms and Conditions set forth in the Commission's Order approving the commingling of customer segregated funds with funds deposited to margin, guarantee or secure transactions in foreign futures contracts. *See* 67 Fed. Reg. 34110, 34111-12 (June 27, 2001). The text that follows each of those italicized headings describes the ways in which the safeguards that will be put in place for the Euro Link are, to the extent relevant, either equivalent or superior to those established for the CME-MEFF linkage.

² Variation margin payment instructions would be issued to The Clearing Corporation's Euro settlement bank if The Clearing Corporation were to offer a variation settlement service for its clearing participants. The purpose of such an arrangement would be to make it unnecessary for Clearing Corporation participants to establish their own Euro-denominated bank accounts. In such a case, Eurex Clearing would debit or credit The Clearing Corporation's account directly, rather than paying and collecting variation margin to and from the accounts of Clearing Corporation participants in the first instance.

c. verify and post matched trades;

All trades that are submitted to The Clearing Corporation will have already been matched by the Eurex trading platform.

d. hold the initial margin deposits of MEFF and CME clearing members;

The Clearing Corporation will collect and hold original margin from its clearing participants for Euro Link contracts. Unlike the MEFF-CME arrangement, however, where the CME acted as the sole clearinghouse for all linked contracts, Eurex Clearing will continue to act as the Destination Clearing House for its clearing members and as such will collect original margin from its members.³

e. determine and record MEFF's gross open positions;

The books and records of each Clearing House will reflect the gross open positions of its clearing participants or clearing members. (There is no reason for The Clearing Corporation to determine or record Eurex Clearing's gross open positions in Euro Link Contracts until the introduction of Phase II, at which time Eurex Clearing's Special Clearing Member account at The Clearing Corporation will include positions in contracts that are traded on USFE.)

f. maintain sub-accounts for each MEFF clearing member on CME's books;

The Clearing Corporation will receive information identifying its clearing participants' sub-accounts directly from Eurex Clearing, which will maintain sub-accounts for each Clearing Corporation participant who trades through the Global Clearing Link.

It is only the trades that are cleared into the account of the Special Clearing Member at the Home Country Clearing House (Eurex Clearing during Phase I) that need to be identified by sub-account. Thus, unlike the CME-MEFF arrangement, where all contracts are cleared at the CME, a reciprocal arrangement for the maintenance of sub-accounts for members of Eurex Clearing on the books of The Clearing Corporation is not required for Phase I of the Global Clearing Link.

g. determine and record margin requirements, exercise and assignment, and final cash settlement records;

Each Clearing House will establish its own original margin requirements, although they are ordinarily expected to be similar, if not identical, in order to discourage "margin arbitrage." As indicated above, exercise, assignment and final cash settlements will be effected by the Home Country Clearing House

³ We have used the term "original margin" to refer to the performance bond deposits that are required to be made by clearing participants (and use the term "initial margin" to refer to customer margin requirements).

(Eurex Clearing in this instance) in order to ensure conformity across all contracts for the same product.

h. determine and report daily price fluctuations, total open interest and trading volume for each contract traded pursuant to the Master Agreement for each trading session; and

Price data, volume and total open interest for the Euro Link contracts, which are traded solely on Eurex during Phase I, will be captured and disseminated by Eurex Clearing after the close of each trading day. (Pursuant to the terms of the Link Clearing Services Agreement between the Clearing Houses, Eurex Clearing will be required to provide this information to The Clearing Corporation for Euro-denominated products traded on USFE. This daily exchange of electronic data files will commence with the introduction of Phase II.)

i. ensure the timely and orderly flow of funds in settlement of MEFF's trading profits and losses.

The Link Clearing Agreement and the Link Clearing Services Agreement incorporate standards and requirements for the timely payment and collection of funds.

2. MEFF will become and remain a special clearing member of CME subject to all of the rules and policies of CME that govern the rights and responsibilities of other clearing members at the CME including, but not limited to, meeting required security deposit requirements and being subject to CME assessment powers.

As discussed above, Eurex Clearing will become a Special Clearing Member of The Clearing Corporation and The Clearing Corporation, in turn, will become a Special Clearing Member of Eurex Clearing. The Clearing Corporation and Eurex Clearing have concluded that it is unnecessary for the Clearing Houses to make deposits to each other's Guaranty Funds or to be liable for assessments to those Funds.⁴

3. For each trade executed pursuant to the Master Agreement, MEFF will submit to CME a clearing record submission containing information as CME may require, including, at a minimum, the following information:

a. an indication that the trade is being made pursuant to the Master Agreement;

⁴ In this regard, it is instructive to note that MEFF's share capital totaled €18,030,000 at December 31, 2002; its book value was €22,412,000 as of the same date. (The Commission's Order was issued in May 2001. MEFF share capital and book value information is not readily available for 2000 or 2001.) By contrast, The Clearing Corporation's unaudited shareholder equity (book value) was \$103.2 million. Eurex Clearing's obligations are supported by Deutsche Börse AG, which has issued an unlimited guarantee for 80 percent of any deficit arising out of the default of a member of Eurex Clearing. Deutsche Börse AG is a publicly traded company with shareholder equity of €3.34 billion and total assets of €3.29 billion at December 31, 2003.

- b. identification of the executing clearing member(s);*
- c. identification of the terms of the contract being traded, including the delivery month, put/call indicator, strike price, underlying futures contract, if applicable, house or customer origin, whether the trade was a buy or sell transaction, and the date the trade was executed;*
- d. the number of contracts and the price at which the contracts traded; and*
- e. an indication as to whether each side of a matched trade will clear in the MEFF special clearing account or in a CME clearing member's account.*

With one exception, The Clearing Corporation will receive the same types of information for all trades and positions that are cleared in its Special Clearing Member account at Eurex Clearing. In cases where the opposite side of the trade is being cleared by a member of Eurex Clearing, the information provided to The Clearing Corporation will for that purpose merely identify Eurex Clearing as the opposite party, without further identification of the opposite executing broker.

4. Upon receipt of each clearing record submission, CME will validate the transaction to ensure the trades are for DCFs [Designated Futures Contracts] and for the existence of two offsetting legs with a trade price that is within a reasonable price range for the contract, and, where necessary, inform MEFF as soon as practicable of any reason validation failed and return the trade to MEFF for correction or nullification.

Comparable arrangements are unnecessary in the context of the Global Clearing Link, where all trades that are submitted to The Clearing Corporation will have already been matched by the Eurex trading platform. Eurex's Market Supervision Department reviews all trading activity and has the authority to reverse trades that are outside a defined trading range that is reflective of current market conditions.

5. Upon acceptance of a trade for clearing and guarantee, the CME will post the legs of the trade to the appropriate clearing member subaccount of the MEFF special clearing account or to the appropriate CME clearing member's account.

Eurex Clearing will post the legs of the trade to the appropriate clearing participant sub-account in the Special Clearing Member account of The Clearing Corporation or to the appropriate account of a member of Eurex Clearing.

6. CME will retain the right to adjust the marking price for clearing purposes to be different from the settlement price in cases where the settlement prices vary significantly from the theoretical market value of the instruments as determined by the CME.

As we understand it, the CME reserved to itself the right to establish its own settlement price (the "marking price for clearing purposes"). The Clearing Corporation, like the CME, has always had authority to disregard the settlement price that has been determined by an exchange (whether the Chicago Board of Trade or USFE) if in its judgment that price is not fairly reflective of market conditions. Of necessity, that discretion has to be circumscribed in cases where

the settlement price in question is determined, not by an exchange (as is the case with the CME and MEFF) but by another Clearing House (as is the case with the Global Clearing Link). In such circumstances, it would be impractical – not to mention extremely imprudent – for each Clearing House to set its own settlement prices independently. (If nothing else, such a scenario would immediately result in imbalances in the daily pay-collect cycle, with some clearing members expecting to receive more than their counterparts were instructed to pay.)

Eurex Clearing and The Clearing Corporation are sensitive, however, to the possibility that there could be circumstances (such as the occurrence of events after the close of a market) that could justify a Clearing House taking steps to collect additional margin for its own protection. Thus, although settlement prices will be established by the Home Country Clearing House (Eurex Clearing, in the case of Euro Link contracts), The Clearing Link Agreement expressly permits the other Clearing House to establish a different settlement price for its own risk management purposes.

7. For the purpose of making and receiving margin and daily settlement payments in connection with the clearing of DFCs, CME and MEFF will establish separate accounts at a mutually agreed-upon bank located outside the U.S. authorized to effectuate transfers between accounts.

8. CME will determine the initial and variation margin levels for each DFC required to be maintained by MEFF and calculate MEFF's margin requirements based upon MEFF's net positions with respect to each delivery month, taking into account any applicable spread margin reductions.

The Link Clearing Agreement requires each Clearing House to establish a bank account for the purpose of making and receiving daily variation margin (settlement) payments in the “home country currency.” Thus, The Clearing Corporation will maintain a Euro-denominated settlement account with a bank that has an account (either directly or through a correspondent relationship) with the Deutsche Bundesbank, the German central bank. Although not required for Phase I, Eurex Clearing will establish a Dollar-denominated settlement account at a commercial bank reasonably acceptable to The Clearing Corporation. As discussed above, each Clearing House will collect original margin from its own participants and members and will not, therefore, collect original margin from the other Clearing House.

9. In the event of a MEFF default, as defined by the Master Agreement, CME may, in addition to all other rights and remedies contained therein, or otherwise permitted by applicable law:

a. apply margin deposits to the obligations of MEFF to make payments to the CME when and as they become due;

b. liquidate the positions and collateral of MEFF, including but not limited to its security and seat assignment deposits and apply other assets of MEFF available to the

CME to discharge the obligations of MEFF to make payments to the CME when and as they become due;

c. by notice to MEFF, suspend the operation of the MEFF special clearing account as to all subsequent trades;

d. establish an alternative market for DFCs through electronic means or otherwise; and

e. allow MEFF clearing members to transfer their positions to a CME clearing member.

Notwithstanding the above, if a MEFF default exists because of a failure by MEFF to make a payment required by the Master Agreement, the CME may liquidate the positions in the MEFF special clearing account.

The rights of the Clearing Houses in the unlikely event of a default of the other Clearing House are set forth in the Clearing Link Agreement. These include (i) drawing on the third-party credit support provided by the defaulting Clearing House in the net amount of the defaulted payments (including any delivery failure losses); (ii) charging the defaulting Clearing House interest on the net defaulted amount; (iii) reducing and setting off the aggregate of amounts payable to one Clearing House by the other; (iv) terminating the agency authority (and any related power of attorney) of the defaulting Clearing House to collect and distribute variation margin, debit and credit clearing members' delivery settlement accounts, or instruct deliveries with respect to the variation margin and delivery settlement accounts of the non-defaulting Clearing House and its clearing members; and (v) liquidating all or a portion of the open contracts in the Special Member Accounts by offsetting those contracts against each other, causing them to be closed in the open market or settled at the settlement price (or, if no settlement price is available or the non-defaulting Clearing House reasonably believes that such settlement price is not fairly reflective of market conditions, at such other price or prices as the non-defaulting Clearing House may deem fair and reasonable in the circumstances); and (vi) terminating the Clearing Link Agreement.

10. CME will receive from MEFF the following information on an ongoing basis:

a. upon written request and within three business days, all information relating to the markets in DFCs that may assist the CME in its efforts to maintain the integrity of the marketplace;

b. periodic reports listing all large trader positions setting forth positions equal to or exceeding a threshold to be determined jointly by CME and MEFF; and

c. upon a special call and within 24 hours, a report that contains, at a minimum, information required to be included in large trader reports and account identification information.

Comparable procedures are not necessary for the Euro Link. Unlike the arrangement between the CME and MEFF, which resulted in the CME being the sole clearinghouse for the “Designated Futures Contracts” that were traded on MEFF, Eurex and Eurex Clearing will have primary responsibility for the maintenance of market integrity in the contracts for which Eurex Clearing is the Home Country Clearing House (*i.e.*, Euro-denominated contracts). The addition of The Clearing Corporation as an additional clearing venue should not and does not diminish those responsibilities. The Clearing Corporation nonetheless retains the ability to obtain trade data and other information, including information relating to the financial integrity of its clearing participants.

11. All money, securities, and property received by a participating FCM to margin, guarantee, or secure DFCs, or accruing as a result of DFCs, and held subject to the terms of this Order, shall be deemed to have been received by the participating FCM and shall be accounted for and treated and dealt with as belonging to the customers of the participating FCM consistently with Section 4d of the Act.

12. Subject to the terms and conditions of this Order, notwithstanding any provision to the contrary in the Commission’s rules (including, but not limited to, Rules 1.20(a), 1.22 and 1.24), the money, securities, and property described in the preceding paragraph of this Order may be commingled with money, securities, and property received by a participating FCM to margin, guarantee, or secure trades or positions in commodity futures or commodity option contracts on a [designated contract market or derivatives transaction execution facility], or accruing as a result of such trades or contracts, and otherwise required by the Commission to be segregated under the Act.

The Commission’s Order appropriately allows the inclusion in a segregated funds account of money, securities and property received by an FCM to margin, guarantee or secure the “Designated Futures Contracts” traded on MEFF and cleared at the CME. We request that the same relief be afforded to The Clearing Corporation with one minor qualification. Specifically, the CME requested relief only for itself and its clearing members. We do not believe it is appropriate to deny the benefits of the requested relief to FCMs that are not Clearing Corporation participants but whose customers may wish to trade through the Euro Link and ask, therefore, that the benefits of any such relief be extended to all FCMs.