



Commodity Futures Trading Commission

Office of Public Affairs

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Proposed Rule on Regulations 1.25 and 30.7 Regarding Investment of Customer Funds and Credit Ratings

Commodity Exchange Act, Section 4d(a)(2) provides that the investment of customer segregated funds is limited to obligations of the United States and obligations fully guaranteed as to principal and interest by the United States, and general obligations of any State or of any political subdivision thereof.

Commission Regulations 1.25 and 30.7: Pursuant to authority under Section 4(c) of the CEA, the Commission substantially expanded the list of permitted investments by amending Commission Regulation 1.25 in December 2000 to permit investments in general obligations issued by any enterprise sponsored by the United States, bank certificates of deposit, commercial paper, corporate notes, general obligations of a sovereign nation, and interests in money market mutual funds (MMMFs). In February 2004, the Commission adopted amendments regarding repurchase agreements using customer-deposited securities and time-to-maturity requirements for securities deposited in connection with certain collateral management programs of derivatives clearing organizations. In May 2005, the Commission adopted amendments related to standards for investing in instruments with embedded derivatives, requirements for adjustable rate securities, concentration limits on reverse repurchase agreements, transactions by futures commission merchants (FCMs) that are also registered as securities brokers or dealers (in-house transactions), rating standards and registration requirements for MMMFs, an auditability standard for investment records, and certain technical changes. Regulation 30.7 governs an FCM's treatment of customer money, securities, and property associated with positions in foreign futures and foreign options. Regulation 30.7 was issued pursuant to the Commission's plenary authority under Section 4(b) of the Act. Because Congress did not expressly apply the limitations of Section 4d of the Act to 30.7 funds, the Commission historically has not subjected those funds to the investment limitations applicable to customer segregated funds.

Section 939A of the Dodd-Frank Act obligates Federal agencies to complete a review of their respective regulations for the use of assessments of the credit-worthiness of securities or money market instruments within one year. The Act requires Federal agencies to make appropriate amendments to those regulations in order to decrease reliance on credit ratings.

The proposed rule would amend Regulations 1.25 and 30.7 in several respects. Certain amendments reflect the implementation of new statutory provisions enacted by Section 939A of the Dodd-Frank Act. The proposed rules address: (1) certain changes to the list of permitted investments, (2) a clarification of the liquidity requirement, (3) the removal of rating requirements, (4) an expansion of concentration limits including instrument-based, issuer-based, and counterparty concentration restrictions, (5) revisions to the acknowledgment letter requirement for investment in an MMMF, (6) revisions to the list of exceptions to the next-day redemption requirement for MMMFs, (7) the application of customer segregated funds investment limitations to 30.7 funds, (8) the removal of ratings requirements for depositories of 30.7 funds, and (9) the elimination of the option to designate a depository for 30.7 funds.

Comparison Chart – Regulation 1.25, Current vs Proposed Changes

| INSTRUMENT | | RATING | | INSTRUMENT-BASED CONCENTRATION (percentage of total assets in segregation) | | ISSUER-BASED CONCENTRATION (percentage of total assets in segregation) | |
|------------------|--|---|------------------|---|-------------|---|-------------|
| CURRENT | PROPOSED | CURRENT | PROPOSED | CURRENT | PROPOSED | CURRENT | PROPOSED |
| Treasuries | (No change) | None | (No change) | No limit | (No change) | No limits | (No change) |
| Municipals | (No change) | Highest short-term rating of an NRSRO or one of the two highest long-term ratings of an NRSRO | No credit rating | No limit | 10% | 5% | (No change) |
| GSE Securities | GSE securities that are fully guaranteed as to principal and interest by the U.S. | Highest short-term rating of an NRSRO or one of the two highest long-term ratings of an NRSRO | No credit rating | No limit | 50% | 25% | (No change) |
| CDs | Non-negotiable CDs | Highest short-term rating of an NRSRO or one of the two highest long-term ratings of an NRSRO | No credit rating | No limits | 25% | 5% | (No change) |
| Commercial Paper | Commercial paper that is fully guaranteed as to principal and interest by the U.S. | Highest short-term rating of an NRSRO or one of the two highest long-term ratings of an NRSRO | No credit rating | No limit | 25% | 5% | (No change) |

| INSTRUMENT | | RATING | | INSTRUMENT-BASED CONCENTRATION (percentage of total assets in segregation) | | ISSUER-BASED CONCENTRATION (percentage of total assets in segregation) | |
|---------------------------|--|--|------------------|---|----------|---|-------------------------|
| CURRENT | PROPOSED | CURRENT | PROPOSED | CURRENT | PROPOSED | CURRENT | PROPOSED |
| Corporate Notes & Bonds | Corporate notes & bonds that are fully guaranteed as to principal and interest by the U.S. | Highest short-term rating of an NRSRO or one of the two highest long-term ratings of an NRSRO, unless asset-backed. Asset-backed corporate notes or bonds must have the highest ratings of an NRSRO. | No credit rating | No limit | 25% | 5% | (No change) |
| Foreign Sovereign Debt | Eliminated | | | | | | |
| Money Market Mutual Funds | (No change) | None | (No change) | No limit | 10% | No limit | 2% (family of funds) |
| In-house transactions | Eliminated | | | | | | |

Additional notes:

- Repurchase agreements with affiliates would be eliminated.
- Repurchase agreements would be subject to a 5% counterparty concentration limit (currently there is no such limit).
- The requirement that all investments be “readily marketable” would be replaced with a “highly liquid” standard.
- The rulemaking would clarify that acknowledgement letters for money market mutual funds (MMMFs) are to be from a party that has substantial control over the fund’s assets and has sufficient knowledge and authority to facilitate redemption.
- The rulemaking would update and clarify the next-day redemption requirement for MMMFs. (Appendix has safe harbor language for MMMF prospectuses)
- 30.7 funds, which currently have no instrument-related limitations, would follow Regulation 1.25 rules for investment of customer funds.
- The rulemaking would require that a foreign depository have \$1 billion of regulatory capital. Currently, a foreign depository may hold 30.7 funds if it has \$1 billion of regulatory capital, but can also qualify through other means (such as having commercial paper or corporate notes/bonds that meet certain credit rating requirements or receiving specific permission from the Commission upon the request of a customer).