

July 30, 2003

RECORDS SECTION

8200 Jones Branch Drive • McLean, VA • 22102-3110

VIA FACSIMILE: (202) 418-5521

03-7
②

2003 JUL 31 PM 2:07

RECEIVED
C.F.T.C.

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

COMMENT

Re: Proposed Amendments to Regulation 1.25 – Investment of Customer Funds (68 F.R. 38654, June 30, 2003)

Ladies and Gentlemen:

This letter of comment is submitted in response to the Commodity Futures Trading Commission's (CFTC) proposal to permit futures commission merchants (FCMs) and derivatives clearing organizations (DCOs) to engage in repurchase agreements (repos) with securities deposited as margin by customers (customer collateral) without written disclosure or customer consent, as is now required under CFTC Interpretive Letter 84-24 (84-24).

Federal Home Loan Mortgage Corporation (Freddie Mac) is a shareholder-owned corporation chartered by the Congress to create a continuous flow of funds to mortgage lenders in support of homeownership and rental housing. We fulfill our public purposes by making mortgage credit more available for America's families at the lowest possible cost. Freddie Mac has a vital interest in ensuring that we can maintain strong risk management practices that help us keep mortgage rates low.

In pursuing these purposes, Freddie Mac is a large, institutional customer of several clearing and introducing FCMs. Freddie Mac actively engages in futures transactions in the Eurodollar, Treasury and Agency Bond markets. Freddie Mac posts margin to its clearing firms in the form of cash and readily marketable securities.

The CFTC proposal requests comment on how an FCM may fulfill its obligations to its customer in the event a repo counterparty defaults. The proposal asks whether payment by the FCM of the cash equivalent of the securities plus transactions costs would be sufficient, and raises the question of whether this payment would be insufficient for a customer that needs a specific security for risk management purposes.

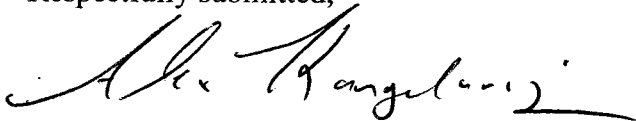
Freddie Mac believes that the written disclosure and customer consent requirements of 84-24 are appropriate and does not believe that the proposed amendments to Regulation 1.25 which would supersede those requirements are sufficient to protect the interests of Freddie Mac and other customers.

In posting margin to its clearing firms, Freddie Mac may transfer securities, which it holds in its long-term or short-term investment portfolio. These securities may include mortgage-related securities, which are not fungible. In certain cases, as recognized by the CFTC in the proposing release, Freddie Mac may need to have the same security returned in order to achieve its asset/liability management goals or for other risk management purposes. Freddie Mac could be exposed to greater risk in the event such securities were not returned to Freddie Mac due to a failure to perform by the FCM repo counterparty. In certain cases, the return of cash or another security may expose Freddie Mac to basis risk (i.e., the risk that an alternative form of collateral returned by an FCM will not change in value in the same way in the event of changes in interest rates or other market factors).

In Freddie Mac's view, the CFTC should consider retaining the written disclosure and consent requirements of 84-24. At a minimum, any change to Regulation 1.25 along the lines proposed should be made expressly subject to being over-ridden in a written agreement, such as a customer agreement, permitting customers and FCMs to provide contractually for disclosure and notice. Finally, Freddie Mac believes the portion of the proposed amendment allocating the risk of loss to the FCM, rather than the customer, in the event of a repo counterparty failure, should be made more explicit, and should specifically include losses from a customer's inability to maintain the risk profile of a portfolio or otherwise replicate necessary positions (e.g., "breakage"), transactional costs, and similar consequential losses resulting from the FCM's decision to re-hypothecate customer property.

Thank you for the opportunity to express our views on Proposed Amendments to Regulation 1.25. Feel free to contact the undersigned at (571) 382-3778, or Michael C. Fox, Assistant General Counsel, at (703) 903-2515, should you wish to discuss any aspect of this comment letter.

Respectfully submitted,



Alex Kangelaris
Vice President, Operations