October 26, 2020

Mr. Christopher Kirkpatrick, Secretary
Commodity Futures Trading Commission
Three Lafayette Center
1155 21st Street, NW
Washington, DC 20581

Re: Bankruptcy Regulations – Supplemental Notice of Proposed Rulemaking Part 190 (RIN 3038-AE67)

Dear Mr. Kirkpatrick:

The Asset Management Group of the Securities Industry and Financial Markets Association ("**SIFMA AMG**", or "**AMG**")[1] and the Managed Funds Association ("**MFA**"[2] and together, the "**Associations**") appreciate the opportunity to submit comments with respect to the supplemental notice of proposed rulemaking published by the Commodity Futures Trading Commission (the "**CFTC**" or the "**Commission**") which proposes amendments to its regulations governing bankruptcy proceedings of commodity brokers with respect to its efforts to foster a resolution proceeding under Title II of the Dodd-Frank Act (the "**Supplemental Proposal**").[3] The Associations remain strongly supportive of the Commission's efforts earlier this year (the "**Original Proposal**")[4] to update Part 190 to reflect current market practices and lessons learnt from past commodity broker bankruptcies, as well as efforts to address, *ex ante*¸ issues that may arise during the

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[1] SIFMA AMG's members represent U.S. asset management firms whose combined global assets under management exceed $45 trillion. The clients of SIFMA AMG member firms include, among others, tens of millions of individual investors, registered investment companies, endowments, public and private pension funds, UCITS and private funds such as hedge funds and private equity funds.

[2] MFA represents the global alternative investment industry and its investors by advocating for public policies that foster efficient, transparent, fair capital markets, and competitive tax and regulatory structures. MFA supports member business strategy and growth via proprietary access to subject matter experts, peer-to-peer networking, and best practices. MFA's more than 140 member firms collectively manage nearly $1.6 trillion across a diverse group of investment strategies. Member firms help pension plans, university endowments, charitable foundations, and other institutional investors to diversify their investments, manage risk, and generate attractive returns over time. MFA has a global presence and is active in Washington, London, Brussels, and Asia, supporting a global policy environment that fosters growth in the alternative investment industry.

[3] *See* Bankruptcy Regulations, 85 Fed. Reg. 60110 (September 24, 2020), available at https://www.cftc.gov/sites/default/files/2020/09/2020-21005a.pdf.

[4] 85 FR 36000 (June 20, 2020).

course of a derivatives clearing organization ("**DCO**") bankruptcy.[5] The Associations believe it is important that DCO rules receive positive qualified master netting agreement ("**QMNA**") treatment for bank capital purposes and therefore support the withdrawal of proposed 190.14(b)(2) and (3) as noted in the Supplemental Proposal. However, as discussed further below, the Associations strongly oppose the stay proposed in the Supplemental Proposal as unnecessary and as a potential increase to systemic risk.

I. Background

The Supplemental Proposal withdraws proposed regulation 190.14(b)(2) and (3) from the Original Proposal that provided for a 6-day delay prior to a liquidation of a bankrupt DCO and proposes to replace those provisions with a conceptual "springing provision" that would include a stay period following an order for relief for a systemically important DCO ("**SIDCO**").[6] This "springing provision" would consist of three elements:

(1) Subsequent to the order for relief with respect to a SIDCO, a stay period would apply to the termination of derivatives contracts outstanding at the time of the order for relief and the exercise of any other default right. There would be no continued collection of initial or variation margin during the stay period;

(2) The stay period would be the ***shorter of*** (a) the period of time beginning on the commencement of the proceeding and ending at the later of 5 p.m. (EST) on the business day following the date of the commencement of the proceeding and 48 hours after the commencement of the proceeding; or (b) the shortest such period specified in the action by any of the Prudential Regulators; and

(3) The proposed changes would not be effective until the Commission determines, following public notice and comment, that each of the Prudential Regulators has taken action sufficient to make the new stay provision consistent with QMNA status of SIDCO rules.[7]

The Associations are deeply concerned with the non-payments of initial or variation margin during the proposed stay. Should a Title II Resolution be triggered subsequent to the CFTC imposed stay, a second stay

[5] *See* SIFMA AMG and MFA comment letter to the Original Proposal at https://www.sifma.org/resources/submissions/joint-amg-mfa-response-to-the-cftc-proposal-to-amend-their-part-190-bankruptcy-regulations/
[6] There are currently only two SIDCOs (as defined in Regulation 39.2): Chicago Mercantile Exchange Inc. and ICE Clear Credit LLC.
[7] Supplemental Proposal at 60113.

under Title II would be imposed until 5 p.m. (EST) on the business day following the date of appointment of the FDIC as a receiver. While not specified in the Supplemental Proposal, we presume that since the SIDCO would not collect or pay initial and variation margin, similarly, clearing members would not collect or pay margins to customers during this stay period as well. As discussed further below, we believe these consecutive stays are unnecessary and would be harmful to market participants through enhanced systemic risk without any guaranty of a successful receivership. We respectfully request that the Commission not adopt the stay proposed in the Supplemental Proposal.

II. The proposed changes are unnecessary for SIDCOs

The Supplemental Proposal notes that the reason for introducing the proposed stay is to protect against the highly unlikely possibility that a SIDCO could file for bankruptcy before a process to place that SIDCO into a Title II Resolution could be initiated and, as a result of the bankruptcy, there would be an immediate (or near immediate) and irrevocable termination of the SIDCO's derivatives contracts with its members.[8] The Commission notes that it is concerned that such termination would undermine the Title II process should a SIDCO unexpectedly become subject to a bankruptcy proceeding.[9] The Associations do not believe that the Commission's concern is warranted given the heavy regulatory oversight of SIDCOs. The suggested basis for the added stay would be due to a lack of knowledge by the CFTC, FDIC, Federal Reserve and Secretary of the Treasury of an impending bankruptcy filing by a SIDCO. We find the possibility of a surprise bankruptcy filing implausible given the regulatory oversight framework. In weighing the costs of the potential dual stays against the risk of multiple days of increased (and likely uncollateralized) market exposure against the probability of a surprise SIDCO bankruptcy filing, the Associations do not see any cost-benefit tradeoff to the requirement for an automatic stay. As an alternative to the proposed stay, the Commission could require, as part of its Part 39 or Part 190 rules, that a SIDCO provide a 1 or 2 day notice to the Commission of any bankruptcy petition by a SIDCO. We believe this notice requirement would achieve the same goal in a materially less detrimental manner.

[8] *Id* at 60112.
[9] *Id.*

III. Proposed stay could increase systemic risk

As noted above, the proposed stay in the Supplemental Proposal could result in consecutive stay periods applicable to a contract cleared at a SIDCO. The first stay period is under the proposed change to Part 190 and would be the later of 48 hours after the commencement of the bankruptcy proceeding and 5 p.m. (EST) on the business day following the commencement of the proceeding.[10] The second stay period would be triggered by a Title II proceeding which would impose a stay until 5 p.m. (EST) on the business day following the date of appointment of the FDIC as a receiver under Title II. Depending on the day of the week the bankruptcy proceeding is commenced, the combined effect of the stays could be up to 3 business days or even 5 or 6 calendar days. During this time, no initial margin or variation margin would be collected or paid by the SIDCO. It is unclear in the Supplemental Proposal whether initial margin or variation margin would be collected by futures commission merchants from market participants. We assume that such variation margin from clearing members to customers would not be paid nor excess initial margin returned since the SIDCO would have ceased initial and variation margin payments. We further assume that any SIDCO bankruptcy filing would occur during a period of significant market stress. The combined effect of these stays, together with the non-collection/payment of margin, would result in extraordinary market exposures to market participants during highly volatile market conditions. The non-payment of margins could also result in a multiple day liquidity problem for market participants clearing at the SIDCO. Market participants would have limited options to hedge or mitigate the impact of the stays during these periods given the limited alternatives available for the types of products cleared by SIDCOs. As the Commission responsibly points out, since there would be no collection of initial or variation margin, "risk levels would increase during the stay period." The Commission further acknowledges this risk correctly in the Cost-Benefit Considerations of the Supplemental Proposal:

> *"…, there is at least one significant cost: For the duration of the stay period, clearing members and clients will be uncertain whether their contracts will continue (as part of a Resolution) or be terminated (and thus would need to be replaced). That uncertainty would mean that clearing members and clients would be disadvantaged in determining how best to protect their positions."*[11]

In sum, the Associations are concerned with any stay that fosters non-payment and strongly oppose the stay as proposed since it, together with a stay imposed under Title II, crystallizes non-payment of initial and variation

[10] The Supplemental Proposal suggests the timeframe could be shorter if required by the Prudential Regulators under their QMNA rules.
[11] *See* Supplemental Proposal at *60114*.

margin for up to three business days during significant market stress which could lead to significant financial loss by market participants without any expected foreseeable ability to mitigate the associated risks.

IV. The proposed stay is more expansive than other stays related to resolution

The Commission's proposed stay would be inconsistent with other resolution stays in the United States (i.e., the Federal Deposit Insurance Corporation Improvement Act ("**FDICIA**") or Title II of Dodd-Frank) by specifically prohibiting early termination as a result of a non-payment. It is also inconsistent with international standards for resolution.[12] In crafting the legislation for FDICIA and Title II, Congress only restricted counterparties from exercising early termination as a result of, or incidental to, the appointment of the receiver. Congress did not restrict early termination rights due to a payment failure or failure to meet a margin obligation. We do not believe that a new standard of stay power should be created for SIDCOs and are extremely concerned with a SIDCO's bankruptcy filing exposing market participants to multiple days of non-payment without the ability to early terminate their positions. We also note that the Commission's proposed stay would be created in order to ***contemplate the possibility*** of entry into resolution, not the entry into resolution itself, which would be inconsistent with the purpose of other resolution stays.

V. Supplemental Proposal does not contain regulatory text for public comment

As noted above, the Associations are supportive of the Commission's efforts to modernize the Part 190 rules. However, we believe that the addition of a stay period with non-payment of margin should be subject to further review and industry analysis. While we acknowledge the Commission's stated desire to complete the work of amending Part 190 in one coherent rulemaking,[13] we do not believe that the Commission should rush through the concept of adding a revolutionary stay period merely for the sake of coherence. Further, the Associations are concerned that the process laid out for finalization in the Supplemental Proposal fails to

[12] The stay suggested in the Supplemental Proposal is also inconsistent with the Financial Stability Board's (Key Attributes of Effective Resolution Regimes for Financial Institutions (the "**Key Attributes**"). https://www.fsb.org/wp-content/uploads/r_141015.pdf. The Key Attributes stipulate that a stay on early termination rights should apply only for termination rights that arise for reasons only of entry into resolution or in connection with the use of resolution powers should not interfere with payment or delivery obligations. The Key Attributes specify that if a firm in resolution fails to meet any margin, collateral or settlement obligations, its counterparty should have the immediate right to exercise an early termination right against the firm in resolution. The Key Attributes also contemplate a maximum stay period of 2 Business Days for entry into resolution.

[13] *See* Supplemental Proposal at *60114*.

provide the public with actual regulatory text and a meaningful opportunity to provide comment on the associated proposal.

VI. Conclusion

Accordingly, we request that the Commission withdraw the Supplemental Proposal and conduct further discussion with the prudential regulators and the public. The Commission should then submit a new rule proposal for notice and comment with specific rule text.

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We thank the Commission for providing SIFMA AMG and MFA the opportunity to comment on the Supplemental Proposal. Should you have any questions, please do not hesitate to contact Jason Silverstein at (212) 313-1176 or jsilverstein@sifma.org on behalf of SIFMA AMG, or Jennifer Han at (202) 730-2600 or jhan@managedfunds.org on behalf of MFA.

Respectfully submitted,

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