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Via E-Mail (secretary@cftc.gov)

COMMENT

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

Re: RIN 3038-AC66; Revised Adjusted Net Capital Requirements for Futures Commission Merchants and Introducing Brokers, 74 *Fed. Reg.* 21290 (May 7, 2009)

Dear Mr. Stawick:

National Futures Association welcomes this opportunity to comment on the Commission's proposed changes to its net capital requirements for FCMs and independent IBs. NFA applauds the Commission for reviewing its FCM and IB capital requirements to determine whether they are appropriate for protecting customer assets and ensuring that firms have the financial wherewithal to meet their obligations. While NFA agrees with several of the proposed changes, it believes that others are not appropriate at this time.

NFA supports the Commission's proposed amendment to its rules to increase the IB minimum net capital from \$30,000 to \$45,000. Current CFTC rules require independent IBs to maintain the higher of \$30,000 or the amount required by a registered futures association. Since NFA's minimum requirement is \$45,000, the change to the CFTC's rule would harmonize those rules with NFA's rules without increasing the amount IBs must maintain.

NFA also supports increasing the FCM minimum net capital requirement in the Commission's rules. Given that FCMs can hold customer funds and that the amount of these funds has increased dramatically in recent years, the proposed increase to \$1,000,000 not only recognizes this significant increase in customer funds but also ensures that FCMs have an appropriate minimum level of capital to meet their financial obligations.

The Commission also proposes two significant changes to the risk-based capital requirement, which is based on a percentage of margin requirements in accounts held at the FCM. NFA supports the first change—increasing the noncustomer percentage to match the percentage for customer positions—and believes that the Commission has provided a valid rationale for this change. In particular, the Commission states that in originally adopting the 4% requirement for noncustomer positions, it modeled this requirement upon SRO rules. SROs adopted this lower percentage for noncustomer positions *vis-a-vis* the 8% requirement for customer positions because SROs at the time believed that noncustomer accounts presented less risk to FCMs than customer accounts. As the Commission notes, however, more recent experience has shown that this assumption may no longer be correct, particularly under conditions of financial stress for the FCM. NFA recommends, however, that if the Commission moves the noncustomer requirement to 8%, then it should provide significantly longer than sixty days for FCMs to comply.

On the other hand, we have not seen any evidence to support the Commission's second significant change—increasing both the customer and noncustomer percentage amounts to 10%. While we recognize that the Commission cites "rigorous standards for FCM financial strength" as the rationale for this increase, we question the efficacy of this rationale. In particular, during the past year's significant market volatility and instability, there has been no evidence that the current risk based capital requirement has failed or has placed FCMs in precarious financial situations. To the contrary, even despite the insolvencies of several large financial institutions, the FCM subsidiaries of these firms had more than adequate segregated funds and capital to meet their liability to customers. In short, without a reasoned justification, NFA cannot support increasing the customer and noncustomer percentages to 10%.

With regard to OTC derivative positions, NFA supports including them in an FCM's risk based capital requirement. NFA believes, however, that the Commission should closely coordinate its overall capital treatment of cleared OTC positions—particularly those positions that are designed to hedge or offset the risk of other positions—with the other financial regulators so as not to provide a capital disincentive to clear these transactions. At this time, NFA also supports revisions to CFTC Regulation 1.17(j) to reflect that cleared OTC positions in proprietary accounts may be covered by positions that would qualify as cover for proprietary futures and options positions.

Finally, we applaud the Commission's initiative to review whether the current capital rules adequately account for an FCM/BDs overall risk. For many years now, the Commission has been at the forefront of adopting and utilizing capital rules that truly reflect the specific risk posed by a firm's operations. NFA believes that the Commission's current FCM capital requirements work exceptionally well with the segregation and secured amount requirements and special provisions of the Bankruptcy Code in protecting customers against insolvency losses. NFA notes, in particular, that since 1990 there have been few insolvencies by traditional FCMs trading on U.S. exchanges, and no customer segregated funds have been lost.

The Commission's actions in the capital area stand in stark contrast to the SEC, which still has overly simplistic capital requirements that do not truly account for a firm's specific risk. As you are aware, the Obama Administration's June 2009 Financial Regulatory Reform ("FRR") proposal calls for a study regarding the harmonization of the securities and commodities regulatory regimes. NFA strongly believes that the CFTC's risk-based capital approach should be the prevailing capital structure that emerges after that study.

On the other hand, we are very concerned about the current suggestion of increasing the ANC requirements for FCM/BDs by arbitrarily combining the CFTC and SEC capital requirements. While this approach may be appealing in its structure, it is a step backward and embraces a simplistic capital approach rather than being reflective and offering an approach that adequately measures specific firm risk.

At this time NFA, like the Commission, recognizes that the recent financial crisis has justifiably heightened concerns among all regulators that financial institutions have adequate capital appropriate for their specific business risk. The Obama Administration's FRR proposal also calls for firms identified as Tier 1 Financial Holding Companies ("Tier 1 FHCs") due to their size, leverage, and interconnectedness to be subject to robust consolidated regulation and supervision. The Administration's proposal also calls for the Federal Reserve Board to have the authority and accountability for consolidated supervision and regulation of these Tier 1 FHCs, and for the Treasury Department to lead a working group with participation by other federal financial regulatory agencies to conduct a fundamental reassessment of the existing capital requirements for banks, bank holding companies ("BHC"), and new Tier 1 FHCs. Treasury's review is to be completed by December 31, 2009, and focus on all elements of the capital framework, including composition of capital, scope of risk coverage, relative risk weights, and calibration.

NFA believes that most large FCM/BDs are either part of a BHC or will be classified as part of a Tier 1 FHC. Therefore, NFA encourages the Commission to closely coordinate its review of FCM/BD capital requirements with Treasury's reassessment of existing capital requirements for BHCs and Tier 1 FHCs. In the past, all financial regulators have had a tendency to use simple capital formulas that have worked well in most cases but may not have appropriately addressed firm specific risk. We should take this opportunity now to reassess our past approaches and determine whether a new capital framework can more appropriately measure an FCM/BD's specific risk.

NFA appreciates this opportunity to comment on the CFTC's proposals. We are confident the Commission will engage in a careful analysis and reach a result that protects customers and the futures markets without placing an undue burden on FCMs.

Respectfully submitted,

Thomas W. Sexton
Senior Vice President and General Counsel

(kpc/Comment Letters/Capital Requirements)