99-32
(4)

NFA NATIONAL FUTURES ASSOCIATION
200 W. MADISON ST. • CHICAGO, IL • 60606-3447 • (312) 781-1300

October 25, 1999

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

Re: Commission Rule 30.12 – Exemption from Registration for Certain Foreign FCMs and IBs.

Dear Ms. Webb:

In the August 26, 1999 Federal Register, the Commodity Futures Trading Commission ("Commission") published a proposal to permit certain foreign firms acting as FCMs and IBs to accept and execute foreign futures and options transactions without having to register with the Commission. National Futures Association ("NFA") welcomes this opportunity to comment on this important proposal.

At the outset, NFA commends the Commission for both codifying the existing requirements relating to foreign order transmittal and, more importantly, for recognizing the need to revise these procedures to address the needs of institutional customers and the U.S. firms clearing their trades. The Commission's proposal goes a long way toward providing the needed relief for institutional customers and their U.S. clearing firms, while continuing to provide appropriate protection to these customers, the FCMs carrying their accounts and the financial markets. NFA believes, however, that the proposal can still be improved and encourages the Commission to revise the requirements related to the definition of authorized customers, the increased capital requirements, and automated order routing systems ("AORS").

Authorized Customers

Proposed Commission Rule 30.12 limits the persons who will be permitted to directly enter orders with a foreign futures or options broker to a newly defined category of customers known as "authorized customers." NFA agrees that direct foreign order transmittal should be limited to customers who are generally considered sophisticated. NFA disagrees, however, that there is any need to add yet another category of special customers to the Commission's regulations. There are currently six definitions of "sophisticated customers" included in the Commission's regulations: qualified eligible participants, qualified eligible clients, eligible swap participants, eligible participants for

exchange transactions under §4(c) of the Commodity Exchange Act, eligible customers for post-execution allocation, and customers for which FCMs and IBs are not required to provide the risk disclosure statement under Regulation 1.55. This new definition, along with the others, subjects firms to unnecessary compliance burdens without adding any real regulatory benefit.

Moreover, NFA does not believe that the category of persons which will be permitted to engage in foreign order transmittal should be any more restrictive than the category of persons who are eligible to engage in swap transactions under Part 35. NFA fails to understand why the Commission believes that a person needs to be more sophisticated to understand the diminished protections associated with entering into transactions with foreign entities than those associated with unregulated, and often highly complex, swap transactions.

In particular, NFA questions the significant increase in the amount of funds a CPO/CTA is required to have under management in order to utilize the foreign order transmittal procedures. The Commission appears to be arguing that the market proficiency of these entities may not include an understanding of the risks in dealing in foreign futures and option transactions and that this increased portfolio size somehow demonstrates that a particular entity has the sophistication required to participate in these types of transactions. NFA, however, has not seen any evidence that a pool with $5 million in assets has any lesser understanding of the risks associated with these transactions than a CP0/CTA with $50 million under management.

Moreover, this reasoning is inconsistent with other provisions of the definition which allow investment companies to participate in these transaction without regard to the amount of funds under management. A registered CPO/CTA should have a far greater understanding of the risks associated with foreign futures transaction than an entity whose primary expertise is in the securities markets.

NFA also believes that the provisions related to CPOs and CTAs are unclear. Although the Federal Register release indicates that CPOs and CTAs will be able to engage in these transactions on behalf of their clients, the rule as written appears to limit the relief to CPOs and CTAs trading on behalf of their own account. NFA encourages the Commission to revise this language to clarify the Commission's intent.

NFA continues to believe that the Commission should adopt a uniform definition for those types of customers who are considered qualified to engage in certain types of transactions or be excluded from particular regulatory requirements. NFA encourages the Commission to adopt NFA's enumerated person definition as described in NFA's June 5, 1998 petition for rulemaking. If the Commission is unwilling to do so, NFA encourages the Commission to adopt the definition of eligible swap participant as the standard for Rule 30.12.

Capital Requirements

The Commission's proposal also requires that FCMs whose authorized customers use direct foreign order transmittal to maintain adjusted net capital of either $50,000,000 or 12% of segregated funds and secured amounts. The Federal Register release indicates that the increased capital requirements are designed to ensure that FCMs possess sufficient capital to meet an unusually large margin call that might result from customers utilizing the foreign order transmittal procedures. NFA questions, however, whether 12% of segregated funds and secured amounts guarantees that a firm will maintain the amount of capital the Commission believes a firm needs in order to allow its customers to participate in these types of transactions. Specifically, with a smaller FCM, NFA can envision an instance where this requirement would be less than a firm's actual capital requirement and therefore not ensure the type of capital cushion the Commission desires. NFA recommends, therefore, that the Commission consider revising the capital rule to require either $50 million or three times the firm's capital requirement.

Automated Order Routing Systems

NFA also notes that the Commission would prohibit an authorized customer from placing orders with a foreign broker using an AORS. As we have noted in previous comment letters dealing with AORS, these systems are simply one means, among several, of getting an order to the exchange "floor." Given the fact that this proposed rule requires an FCM to have internal procedures to supervise the impact of foreign orders on its financial condition, to confirm and supervise foreign futures and options orders placed through its omnibus account and to maintain an audit trail of these orders, NFA does not believe that there are any added regulatory concerns associated with using an AORS to place orders with foreign brokers. NFA understands that the Commission may have issues with AORS in other contexts, but we urge the Commission to address these issues apart from the current proposal.

NFA

Ms. Jean A. Webb

October 25, 1999

Conclusion

NFA appreciates the opportunity to express its views on the Commission's foreign order transmittal proposal. NFA encourages the Commission to give serious consideration to these comments and the comments of entities that participate in these markets.

Sincerely,

Daniel J. Roth
General Counsel

/NAM(LTRS:Webb2.caw)