



January 18, 2011

Mr. David A. Stawick  
Secretariat  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21<sup>st</sup> Street, N.W.  
Washington, D.C. 20581

Re: RIN 3038-AD99; Protection of Cleared Swaps Customers Before and After  
Commodity Broker Bankruptcies

Dear Mr. Stawick:

National Futures Association appreciates the opportunity to comment on the Commission's Advance Notice of Proposed Rulemaking regarding various alternative means for handling customer segregated funds posted as margin for cleared OTC transactions.

In considering the advantages and disadvantages of the four models discussed by the Commission, it is important that we not lose sight of the public policy issue that is at the heart of the question. Congress sought primarily to protect the public, not the counterparties to OTC transactions, by reducing the systemic risk involved in OTC derivative transactions. Congress decided to require certain OTC transactions to be subject to clearing and permitted clearing pursuant to the baseline model that had been successfully employed in the futures industry for over 100 years.

Certain counterparties to OTC derivative transactions have stated that the baseline model is not the optimal solution to their risk management needs because those counterparties would be exposed to the risk of loss due to the default of other customers of their clearing FCM. Their concerns are well stated and understandable. Neither the baseline model nor any of the other models discussed by the Commission completely eliminates the risk of loss to counterparties due to insolvency. In our view, that does not in any way undermine the congressional determination that the baseline model is an acceptable means of protecting the public from systemic risk and the CFTC ought not overturn that congressional determination.



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If the baseline model offered by certain clearing organizations does not provide the best alternative for certain counterparties, someone else will build a better mouse trap. That better mouse trap may involve supplementing protections offered by the baseline model through private insurance or other clearing organizations adopting one of the other models discussed by the Commission. The Commission's regulations should ensure that DCOs have the flexibility to offer those alternative structures and that counterparties receive adequate disclosures regarding the residual risks of the structure offered by the DCO. In all of the discussion of this issue, however, we have heard nothing to undercut the proposition that the baseline model is an acceptable means of protecting the public by reducing the systemic risk posed by OTC derivatives.

This model has proven to be an effective and operationally efficient means of dealing with FCM insolvencies. Since 1975, when the CFTC began operations, total insolvency losses for funds required to be segregated have amounted to less than twelve million dollars. Almost three-fourths of these losses occurred between 1978 and 1980, when the CFTC made a concerted effort to close down firms that engaged in various fraudulent activities, including using customer funds for their own purposes. Most impressively, there have been no insolvency losses in segregated funds during the last twenty years.

With respect to the alternative models discussed by the Commission, each presents different policy issues, and we know the Commission will seriously consider the comments it receives on these issues. For example, the Commission should consider how each model would affect:

- An end user's incentive to conduct due diligence before choosing (or remaining with) an FCM;
- The effect on competition among FCMs (including whether a model will eliminate smaller FCMs and decrease the number of FCM players);
- An end user's willingness to post excess margin collateral;
- The ease and likelihood of portfolio margining;
- The effect on an end user's choice to clear or not clear certain swap transactions;
- An FCM's willingness to maintain excess net capital;



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- DCO guarantee fund requirements; and
- Operational efficiencies (or the lack thereof) for promptly transferring funds and positions in the event of an FCM insolvency.

We look forward to continuing discussions with the Commission on this important issue as the rulemaking process moves forward.

Very truly yours,

A handwritten signature in blue ink, consisting of several loops and a long horizontal stroke extending to the right.

Thomas W. Sexton, III  
Senior Vice President and General Counsel

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