

KANSAS CITY BOARD OF TRADE

February 22, 2011

SENT VIA AGENCY WEBSITE

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

Re: Core Principles and Other Requirements for Designated Contract Markets
RIN 3038-AD09

Dear Mr. Stawick:

In response to your request for public comment on Core Principles and Other Requirements for Designated Contract Markets, the Kansas City Board of Trade ("KCBT" or "Exchange") offers the following:

Since December 21, 2000 with the passage of the Commodity Futures Modernization Act, all designated contract markets ("DCM") have been required to demonstrate their ability to comply with 18 core principles. This principles-based approach has served the industry well as it allowed DCMs to exercise discretion in determining the manner in which they complied with the core principles. With the passage of the Dodd-Frank bill on July 21, 2010 the Commodity Futures Trading Commission ("CFTC" or "Commission") has proposed numerous rule changes that shift the regulatory approach from a principles-based system to a prescriptive rule-based system in which the CFTC will mandate how DCMs comply with core principles. KCBT has always strived to maintain a high level of compliance with the applicable laws, rules, regulations and core principles of the CFTC. Market integrity and customer protection are the cornerstones of our business. KCBT agrees it is imperative that all DCMs have adequate programs and systems in place to demonstrate compliance with each of the core principles. However, KCBT does have concern over certain requirements being proposed as detailed below.

Proposed Regulation 38.3(g): Each existing DCM would be required to provide the Commission with a signed certification of its compliance with each of the 23 core principles and the Commission's regulations under part 38 as amended

within 60 days of the effective date of the publication of the final rules being proposed. This proposed effective date is unreasonable and would be burdensome for DCMs to meet. When combined with the numerous other DCM proposed rules deadlines, the proposed core principles effective date becomes even more problematic to meet. It will take time to convert DCM programs and processes from current acceptable practices to adherence to prescriptive objectives and deadlines, assuming adherence can be accomplished in all cases. Due to the grave consequences of non-compliance with the proposed deadline (grounds for revocation of the DCM's designation status), KCBT requests that the Commission reconsider the certification requirement and work with DCMs on reasonable compliance timeframes given the level of complexity in achieving each of the specific requirements.

Proposed Regulation 38.151(a): Requires that prior to granting a member or market participant access to its markets, the DCM must require the member or market participant to consent to its jurisdiction. KCBT Rule 102.00 Responsibility of Members states that any person approved as qualified for membership shall become and be subject to all the provisions of the Certificate of Incorporation, the by-laws, rules and regulations of the KCBT and before being entitled to the privileges of membership shall sign an agreement to abide by and comply with the provisions of the Certificate of Incorporation, the by-laws, rules and regulations of the KCBT or the Board of Directors, and with all orders and resolutions of the Board of Directors and the Business Conduct Committee. KCBT agrees in theory that if a market participant is granted the privilege of trading on a DCM, the participant should not only abide by the DCM's rules, but should also be subject to the DCM's jurisdiction and investigatory and disciplinary process. However, KCBT rules apply exclusively to members, so we question our jurisdiction over non-members. Even if a non-member market participant consents to KCBT's jurisdiction and process, but later fails to abide by such consent, KCBT's only recourse would be to revoke such participant's market access. Given this practical reality, we question the benefit of implementing this proposed regulation and posit that the current process provides adequate incentive for voluntary cooperation by market participants.

Proposed Regulation 38.151(b): Requires DCMs to provide its members, market participants and independent software vendors with impartial access to its markets and services which includes comparable fee structures. KCBT objects to the Commission's mandate of access and fee equality which may not take

into consideration all aspects of an exchange's varying fee or access structures, including beneficial rate structures for high-volume traders or Market Maker programs. Further, there may be varying levels of incentives within such programs. Consequently, we urge the Commission to withdraw from its attempt to impose fee restrictions on DCMs.

Proposed Regulation 38.151(c): Requires DCMs to establish rules that provide the board of trade with the ability and authority to obtain any necessary information to perform any function, including the capacity to carry out such international information-sharing agreements, as the Commission may require. KCBT takes exception to a Commission mandate that a DCM establish rules for and enter into information-sharing agreements as required by the Commission. KCBT currently is a party to several information sharing arrangements that serve the common good of all participants. These agreements were entered into voluntarily by KCBT following review of the specifics of each such agreement as well as an evaluation as to whether adherence to or compliance with such agreements could be reasonably expected or attained. A DCM should not be mandated to enter into information-sharing agreements, particularly when such agreements contain specific requirements unsuitable to a DCM or conditions that the DCM is unable to comply with.

Proposed Regulation 38.154: Requires DCMs that contract with a registered futures association or another registered entity to assist in complying with the core principles to remain responsible for the performance of any regulatory services received and for compliance with the DCM's obligations under the CEA and Commission regulations. This requirement with respect to another registered entity is burdensome and duplicative, particularly when such service provider is another DCM who is also required to comply with the same core principles. KCBT is a party to an electronic trading services agreement with a DCM obligated to comply with DCM core principles. As such, it is costly, burdensome and duplicative to expect KCBT to perform periodic reviews of the adequacy and effectiveness of the services and hold regular meetings with required agendas. Further, we object to proposed regulation 38.154(c) that requires all decisions concerning the cancellation of trades remain as the exclusive authority of the DCM. Under our services agreement, the error trade policy (including authority to cancel or price adjust trades) has been delegated to the service provider. This system has been in place for several years and has served the industry well because of the continuity of processes and procedures between the two DCMs.

Proposed Regulation 38.251(c): Requires DCMs to conduct real-time monitoring of trading and comprehensive and accurate trade reconstructions. Intra-day trade monitoring must include the capacity to detect position limit violations. KCBT envisions significant problems with intra-day position limit compliance. First, customer reportable positions are received once daily on a T + 1 basis. Second, market moves impact option deltas and consequently delta-equivalent positions. Monitoring intra-day position limits for high frequency traders and automated trading systems will be problematic given their trading styles. Furthermore, at the current time it doesn't seem practical for a DCM to monitor accounts during the trading session each day for possible intra-day position limit violations. Reportable positions are reported to the Commission on a T + 1 basis. For these reasons, it is impractical to require DCMs to monitor for intra-day compliance with position limits. With the myriad of proposed regulations and requirements currently before us, KCBT respectfully requests that the CFTC remove this requirement from consideration.

Proposed Regulation 38.252(a)(1): Requires DCMs to monitor each contract's terms and conditions as to whether there is convergence of the futures price to the cash price of the underlying commodity. The Commission requested comment on what other factors, in addition to the delivery mechanism, a DCM should be required to consider in determining whether convergence is occurring. There are many factors that should be reviewed when determining whether convergence is occurring. Some of the factors that may affect convergence include the quality of the crop, carryout of inventories, global demand, transportation costs, storage space, storage costs, location differentials, cash bid/offer information. The value of delivery wheat should reflect the value of wheat "in store" at delivery locations based on published elevator bids. The proposed regulation requires DCMs to take meaningful corrective action, including to address conditions that interfere with convergence or if appropriate, change contract terms and conditions, when lack of convergence impacts the ability to use the markets for making hedging decisions and for price discovery. KCBT cautions the CFTC against making this proposed rule overly prescriptive. The review of a contract's performance should be a careful and deliberate process by the exchange and its appropriate committees to insure that when changes are necessary due to structural deficiencies rather than short-term anomalies, such changes are fair and balanced in their impact on all market participants and implemented in a thoughtful and sensitive timeframe.

Proposed Regulation 38.252(a)(3): Requires DCMs to assess whether the deliverable commodity reasonably can be expected to be available to short

traders and salable by long traders at its market value in normal cash marketing channels. The U.S. Warehouse Act grants the Secretary of Agriculture exclusive authority over federally-licensed warehouses. As such, KCBT rules governing registered delivery warehouses may only impose reasonable requirements as to location, accessibility, and suitability for warehousing and delivery purposes. Accessibility relates to railway connections and bulk receiving and loading facilities adequate for the prompt dispatch of business. Suitability pertains to storage capacity, load-out capacity, bonding, insurance and financial requirements. KCBT actively monitors deliverable supplies of the contract commodity in registered warehouses, but has no control over cash market purchases and sales. Consequently, while the KCBT can make reasonable judgments as to the availability of supplies, it can make no guarantees as to the pricing expectations of cash market sales of the commodity stopped in the delivery process.

Proposed Regulation 38.254: Requires DCMs to have rules in place that require traders to keep records, including records of their activity in the underlying commodity and related derivative markets. If the Commission desires traders to maintain certain types of records, it should provide for such in its regulations (i.e., Section 1.35) rather than requiring rulemaking on the part of a DCM. Given that KCBT Rule 1000.00 incorporates by reference the requirements of the Commodity Exchange Act, KCBT considers the requirement of exchange rules that mirror CFTC regulations to be duplicative, unnecessary and burdensome.

Proposed Regulation 38.255: Requires DCMs to have in place effective risk controls, including but not limited to pauses and/or halts to trading in the event of extraordinary price movements that may result in distorted prices or trigger market disruptions. The CFTC requests comments on which risk controls should be mandated. KCBT has many risk controls already in place such as daily price limits, dynamic price limits, stop logic functionality, no bust ranges, stop loss order protections and maximum order size limits that serve to reduce the potential risk of market disruptions and ensure orderly market conditions. Each DCM should be given the latitude to determine what risk controls are most appropriate for their market to reduce the potential risk of market disruptions and ensure orderly market conditions. KCBT cautions the CFTC about mandating risk controls in which "one size fits all". The risk controls needed for an equity index product may differ from those needed for a futures contract in a physical commodity. Our wheat contract in conjunction with wheat contracts traded at CME and MGE have been served well with having coordinated price limit rules.

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Proposed Regulation 38.350: Requires DCMs to adopt rules to provide for the exercise of emergency authority. KCBT already has emergency rule authority. Liquidation of positions and special margin requirements are more appropriately addressed in DCO rules and procedures.

Proposed Regulation 38.400: Requires DCMs to make available to market authorities, market participants and the public information concerning the terms and conditions of the contracts of the contract market and the rules and regulations (including new rules and rule amendments) for executing transactions on the contract market. Given that CFTC already posts publicly all submissions of DCMs and DCOs, and given further that current KCBT rules are made publicly available on our website, to mandate that DCMs and DCOs also post regulatory submissions of new or amended rules is duplicative. Further, substantive proposed KCBT rules or rule changes are currently communicated to members and the public via circulars or press releases.

Proposed Regulation 38.502: No designated contract market may continue to list a contract for trading unless an average of 85% or greater of the total volume of such contract is traded on the designated contract market's centralized market as calculated over a 12 month period. KCBT is concerned as you clear more swaps, you will have more EFRs and combined with EFPs could exceed the arbitrary 15% limit. If KCBT started to get close to the 15% limit we would have to consider possibly limiting the number of EFPs and EFRs that are executed. We do not feel this would be in the best interest of the contract and would harm the important function of risk transfer. We ask the Commission to revisit the arbitrary nature of this artificial market impediment.

Proposed Regulation 38.505: Requires the price differential between the two legs of an exchange of derivatives for related position ("EDRP") to reflect commercial realities and at least one leg of the transaction should be priced at the prevailing market price. KCBT rules for EDRP allow the transactions to be executed at such prices as are agreed upon by the parties. Even though the majority of EDRP transactions are executed at the prevailing market price, it is still best to allow participants the flexibility to use any price that is agreeable to both parties. It is not uncommon for basis trades to be executed in which the basis is locked in at the current date for shipment at a later date. The customer may not trade futures for the transaction until a later date when the board is more favorable and then not execute the EDRP until the shipment date. In this example neither the cash or futures trade would take place at the prevailing market price but the transaction would still be a valid EDRP.

Proposed Regulation 38.505(d): Requires EDRP trades to be reported to the designated contract market within five minutes of execution. KCBT does not see the benefit of requiring the reporting the EDRP to the contract market within 5 minutes of execution. The current practice of reporting EDRP at the KCBT involves each party's clearing member firm entering the transaction into the DCO (not DCM) for clearing purposes once they have confirmed the transaction with each other. The following business day, the KCBT publishes the total EDRP transactions for each delivery month that were executed for the previous day. KCBT requests clarification from the CFTC as to the benefit of reporting EDRP within five minutes of execution.

Proposed Regulation 38.603: Requires DCMs to adopt rules for the protection of customer funds, including the segregation of customer and proprietary funds, the custody of customer funds, the investment standards for customer funds, intermediary default procedures and related recordkeeping. Since KCBT Rule 1000.00 incorporates by reference the requirements of the Commodity Exchange Act, KCBT considers the requirement of implementing exchange rules that mirror CFTC regulations to be duplicative, unnecessary and burdensome. In addition, the Kansas City Board of Trade Clearing Corporation already has rules in place to address intermediary default procedures.

Proposed Regulation 38.604: Requires each DCM to continually survey the obligations of each FCM created by the positions of its customers and as appropriate, compare those obligations to the financial resources of the FCM. Currently, on a daily basis KCBT already reviews the open positions and percentage of open interest held of each clearing member for concentration of positions. Pay/collect information based upon open positions and reportable positions are also reviewed on a daily basis. During volatile markets KCBT contacts all clearing members carrying positions opposite the market move to ascertain if the clearing member is experiencing any difficulties and to determine if the clearing member is capable of meeting its continued financial obligations with respect to the positions being carried. It would still be prudent for the Designated Self-Regulatory Organization ("DSRO") to review the obligations of each firm they are DSRO for. After all, it is the DSRO that would have access to all customer positions to ensure that the FCM has sufficient capital for the overall positions being carried and not just the positions of one market. KCBT is concerned with the overly vague use of the terms "continually" and "excessive".

Proposed Regulation 38.1101(a)(1)(3): Requires DCMs to maintain sufficient financial resources to cover operating costs for at least one year, calculated on a

rolling basis. Implementation of this proposed regulation would result in duplication. Proposed Regulation 39.11 requires Derivative Clearing Organizations (“DCO”) to maintain sufficient financial resources to meet its financial obligations to its clearing members notwithstanding a default by the clearing member creating the largest financial exposure for the DCO in extreme but plausible market conditions. In our case, it is the DCO’s (not DCMs) capital at risk in the unlikely event of a default. Kansas City Board of Trade Clearing Corporation was established as a wholly-owned subsidiary corporation of KCBT for purposes of limiting liability. As a privately-owned, for-profit corporation, KCBT should be able to determine its own levels of capital resources and deployment.

Proposed Regulation 38.1101(b): Financial resources available to satisfy the applicable financial requirements would include the DCM’s own capital and any other financial resource deemed acceptable by the Commission. The Commission invites commenters to recommend particular financial resources for inclusion in the final regulation. See response to proposed regulation 38.1101(a)(1)(3) above.

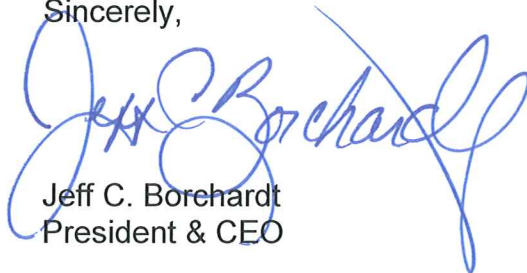
Proposed Regulation 38.1101(e): Requires DCMs to maintain unencumbered liquid financial assets, such as cash or highly liquid securities, equal to at least six months operating costs. If a DCM does not have six months worth of unencumbered liquid financial assets, it would be allowed to use a committed line of credit or similar facility to satisfy this requirement. The committed line of credit can not be used as a financial resource to satisfy the operating costs for one year requirement pursuant to proposed regulation 38.1101(a)(1). See response to proposed regulation 38.1101(a)(1)(3) above.

Proposed Regulation 38.1101(e): Requires DCMs at the end of each fiscal quarter to report the amount of financial resources necessary to meet the requirements set forth in the regulation and the value of each financial resource available to meet those requirements. A DCM would also have to provide the Commission with a financial statement, including the balance sheet, income statement and statement of cash flows of the DCM. KCBT provides the Commission with its annual audited financial statement and objects to the filing of additional financial reports and information. It is one thing for a regulator to question a registrant’s financial resources. It is quite another for the registrant to have to provide continued proof of such. Annual submissions should suffice. See response to proposed regulation 38.1101(a)(1)(3) above.

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Kansas City Board of Trade appreciates the opportunity to comment on the Core Principles and Other Requirements for Designated Contract Markets regulations currently being proposed. KCBT takes issue with other prescriptive regulations proposed by the Commission in RIN 3038-AD09. However, time and resources do not afford us the opportunity to fully address all of these issues. We are concerned and disappointed that the CFTC is apparently using the Dodd-Frank legislation to not only implement a regulatory regime for previously unregulated OTC trading, but as an opportunity to propose unnecessary and extremely prescriptive regulations on already regulated derivative markets. The regulated markets were not the cause of the 2008 financial crisis. In fact, these regulated markets operated exemplary under extreme market volatility and pressures. We are left wondering why, with all of the regulatory initiatives required to implement the provisions of Dodd-Frank, does the CFTC find it necessary to impose prescriptive regulations on an already well-functioning regulated marketplace. This abrupt shift away from principles-based to prescriptive regulation will not serve the industry in competing globally for market share and liquidity and could impact jobs and growth going forward. If you have any questions please feel free to contact me or our chief regulatory officer Joe Ott at 816-753-7500.

Sincerely,



Jeff C. Borehardt
President & CEO