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Invested in America

June 3, 2011

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

Re: Risk Management Requirements for Derivatives Clearing Organizations (RIN 3038-AC98)

The Asset Management Group (the "**AMG**")[1] of the Securities Industry and Financial Markets Association ("**SIFMA**") appreciates the opportunity to provide the Commodity Futures Trading Commission (the "**Commission**") with comments regarding its proposed Risk Management Requirements for Derivatives Clearing Organizations (the "**Proposal**").[2] The AMG believes that the clearing requirements in the Dodd-Frank Wall Street Reform and Consumer Protection Act ("**Dodd-Frank**") may reduce systemic risk but must be implemented in a way that encourages sound risk management and does not unnecessarily decrease liquidity in, or otherwise harm, the swap markets. To that end, the AMG has a few suggestions relating to the derivatives clearing organization ("**DCO**") risk management proposal.

First, the AMG is concerned that the Commission has set the bar too low by requiring DCOs to set their minimum net capital requirement no higher than $50 million. We recommend the threshold be raised to $300 million of net capital. In making this calculation, we propose that only capital that is segregated or otherwise dedicated and not available for other purposes be included. In the case of entities that do not calculate net capital, $300 million in net assets should be required. While we support the goal of open access to DCO membership and recognize that artificially high capital requirements can serve as a barrier to membership of a diverse group of market participants, sound risk management principles dictate that thresholds higher than $50 million be required. Generally, a clearing member's default would put financial pressure on a DCO and its other members. When a clearing member defaults, other clearing members backstop the DCO through contributions to, and replenishments of, the DCO's guaranty fund and by participating in the default management process, including through bidding for and potentially assuming the risks of the positions of the defaulting clearing members. In the event of a member default, the DCO's guaranty fund will be diminished and

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[1] The AMG's members represent U.S. asset management firms whose combined assets under management exceed $20 trillion. The clients of AMG member firms include, among others, registered investment companies, ERISA plans, and state and local government pension funds, many of whom invest in commodity futures, options, and swaps as part of their respective investment strategies.

[2] Risk Management Requirements for Derivatives Clearing Organizations, 76 Fed Reg. 3698 (proposed January 20, 2011). The comment deadline for the Proposal was reopened until June 3, 2011. *See* Reopening and Extension of Comment Periods for Rulemakings Implementing the Dodd-Frank Wall Street Reform and Consumer Protection Act, 76 Fed. Reg. 25,274 (May 4, 2011).

contributions from other members may be necessary. This increases the burden on other, better capitalized, members and stresses the financial resources of the DCOs and, potentially, the financial system as a whole. In addition, highly creditworthy entities might not become clearing members if they believe that doing so will implicitly require them to subsidize less creditworthy members. In the current over-the-counter environment, AMG members perform careful credit analyses before choosing the counterparties with whom to trade. The move to a cleared environment should not force AMG members to face less creditworthy counterparties than they do today. We believe that our suggested threshold strikes the right balance between open access and prudent risk management.

Second, the AMG requests that DCOs explicitly not be permitted to *require* in their rules that the agreement governing execution of cleared swaps be a trilateral agreement among the customer, the executing counterparty and the clearing member. The question of a bilateral vs. trilateral execution agreement has been the subject of much discussion between the buy-side and sell-side. A group consisting of both buy-side and sell-side participants has been working on standard form documentation to serve as a template for negotiation. We understand that the current draft of the execution agreement is bilateral but would permit the counterparties to agree to add a clearing member as a party to the agreement and include trilateral provisions that permit a clearing member to impose trading limits through a customer's executing counterparty.

Our concerns about the trilateral approach primarily relate to the costs and complexity of the operational infrastructure that it will require, as well as potential impacts it may have on liquidity and best execution. Including the clearing member as a party to the execution agreement is tantamount to it guaranteeing execution of the transaction. We understand that clearing members would, in turn, require immediate visibility into the existing positions of potential executing counterparties and impose credit limits. This will require, at great cost, the build-out of information technology systems that permit the instantaneous sharing of customer positions and credit limits among swap execution facilities ("**SEFs**"), DCOs and swap dealers, all of which is not necessary under current practice in the futures market. The AMG believes that these added costs should be borne solely by those market participants that select the trilateral approach – and not by all market participants. In addition, the trilateral model would very likely result in delays in execution processing as a result of these additional limits.

Finally, the AMG believes that a 5-day liquidation period is too long for initial margin requirements for any cleared swaps. Under the Proposal, the initial margin model for cleared swaps must generate levels of initial margin to cover 99% of price movements over a liquidation period of 1 day if the swap is executed on a designated contract market ("**DCM**") or 5 days if the swap is not. We believe that initial margin should be set at a level that reflects a close-out, offset or other risk mitigation that occurs roughly contemporaneous with the default. In the context of cleared transactions, we believe that a 1-day liquidation period for swaps executed on either a DCM or SEF and a 2-day liquidation period for all other swaps is sufficient for this purpose, particularly in light of the relatively high 99% confidence interval. The AMG does not believe that there should be any distinction in the initial margin requirements for cleared swaps executed on a DCM or a SEF as swaps executed on either platform will be more liquid and require less time to close-out than other swaps. Moreover, we do not believe that such different treatment based on whether a swap is executed on a DCM or a SEF is consistent with congressional intent. Section 731 of Dodd-Frank requires the prudential regulators and the Commission, in order to "offset the greater risk to the swap dealer or major swap participant and the financial system arising from the use of swaps that are not cleared," to set margin requirements that are "appropriate for the risk associated with the non-cleared swaps held as a swap dealer or major swap participant."[3] By so requiring, Congress indicated that it understood there to be a risk-based difference between cleared and uncleared swaps that could be addressed by differential margin requirements. No similar indication about relative risk was made with respect to DCMs as opposed to SEFs. To the extent that specific cleared swaps have unique characteristics that make them particularly illiquid or difficult to close-out, offset or hedge, such characteristics would be captured by normal clearinghouse margin models operating within the specified liquidation periods.

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The AMG appreciates the opportunity to provide comments on the Proposal. Should you have any questions, please do not hesitate to call the undersigned at 212-313-1389.

Respectfully submitted,

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Securities Industry and Financial Markets Association

[3] Commodity Exchange Act § 4s(e)(3)(A) (as amended by Dodd-Frank Section 731).