



Financial Industry Regulatory Authority

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September 13, 2011

Elizabeth M. Murphy  
Secretary  
U.S. Securities and Exchange Commission  
100 F Street, N.E.  
Washington, DC 20549-1090

Dear Ms. Murphy:

As previously stated in its rule filings, FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the Act.<sup>1</sup> The “burden” in the proposed rule change – the requirement that no members shall permit a customer to initiate a forex position with a leverage ratio greater than 4 to 1 – is appropriate to protect retail investors, who at higher levels of leverage, would face greater risks that funds used to initiate a forex position would be insufficient to maintain such position.<sup>2</sup> FINRA notes that the 4 to 1 leverage limitation is based on historical norms within the securities industry and adheres to longstanding prudential limits on acceptable leverage limitations for retail investors. FINRA also notes that 4 to 1 leverage limitations were deemed appropriate for “pattern day traders” whose buying power is limited to four times the customer’s maintenance margin excess as of the close of business of the previous day.<sup>3</sup>

<sup>1</sup> See Securities Exchange Act Release No. 60172 (June 25, 2009), 74 FR 32022 (July 6, 2009) (Notice of Filing of File No. SR-FINRA-2009-040); see also Securities Exchange Act Release No. 61090 (December 1, 2009), 74 FR 64776 (December 8, 2009) (Notice of Filing of Proposed Rule Change as Modified by Amendment No. 2 of File No. SR-FINRA-2009-040).

<sup>2</sup> This letter uses the term “retail investors” to describe persons who are not “eligible contract participants” as defined in Section 1a(18) of the Commodity Exchange Act, as re-designated and amended by Section 721 of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

<sup>3</sup> See Securities Exchange Act Release No. 44009 (February 27, 2001), 66 FR 13608 (March 6, 2001) (Order Approving Proposed Rule Change of File No. SR-NASD-00-03); see also U.S. Government Accountability Office, “Securities Operations: Day Trading Requires Continued Oversight,” Publication GAO 00-61 (February 24, 2000) (stating that the 4 to 1 leverage rules were “not only to protect the financial integrity of broker-dealers that provide credit, *but also to protect customers from taking on too much leverage.*”), page 23 (emphasis added).

Moreover, the proposed rule change does not preclude broker-dealers from offering forex to retail investors; rather, it helps ensure broker-dealers do so on terms that do not expose retail investors to the risks inherent in extreme leverage.

Firms engaging in a forex business generally fall into one of three categories: (i) broker-dealers, (ii) futures commission merchants (FCMs) or retail foreign exchange dealers (RFEDs), and (iii) dual broker-dealers/FCMs or RFEDs.<sup>4</sup> Effective October 1, 2011, all firms in categories (ii) and (iii) that are members of the National Futures Association (NFA) will be subject to the full suite of NFA rules relating to retail forex, including the NFA's net capital and leverage requirements. Proposed FINRA Rule 2380 would apply to FINRA member firms, i.e., firms in categories (i) and (iii). Accordingly, firms in category (iii) would comply with both FINRA and NFA rules, with the leverage limitations in the proposed rule change supplanting the NFA's 50 to 1 and 20 to 1 leverage standards. Notwithstanding these other requirements, FINRA believes that its rulemaking authority should be informed by its view of investor protection mandates, which in some instances necessitate heightened requirements compared to those of other federal regulators or other self-regulatory organizations (SROs). Indeed, SROs such as FINRA have historically adopted rules beyond the basic standards in the federal regulatory scheme.

Finally, FINRA staff does not interpret proposed Rule 2380 to prohibit a member from arranging a physically-settled, foreign exchange transaction for a customer in connection with the purchase or sale of a security, or the clearance or settlement of such purchase or sale, where the purpose of such foreign exchange transaction is to mitigate the customer's currency risk in connection with the securities purchased or sold.

If you have any questions on this matter, please do not hesitate to contact me at (202) 728-8104.

Very truly yours,



Gary L. Goldsholle

<sup>4</sup>

Retail forex also may be offered by banks. The Office of the Comptroller of the Currency (OCC) and the Federal Deposit Insurance Corporation (FDIC and, together with the OCC, the Bank Regulators) have issued final rules that permit U.S. financial institutions that are subject to the jurisdiction of a Bank Regulator to engage in forex transactions with retail investors. See 76 FR 41375 (July 14, 2011) (OCC Adopting Release); see also 76 FR 40779 (July 12, 2011) (FDIC Adopting Release).