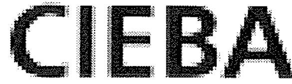

June 3, 2011

David Stawick
Secretary
Commodity Futures Trading Commission
Three Lafayette Center
1155 21st Street NW
Washington, DC 20581

Re: Reopening and Extension of Comment Periods for Rulemakings Implementing the Dodd-Frank Wall Street Reform and Consumer Protection Act;

RIN 3038-AC 96 – Swap Trading Relationship Documentation Requirements for Swap Dealers and Major Swap Participants.

Dear Mr. Stawick:

The Committee on the Investment of Employee Benefit Assets ("CIEBA") appreciates this opportunity to provide further comments to the Commodity Futures Trading Commission (the "CFTC" or "Commission") regarding the CFTC's proposed rulemaking entitled "Swap Trading Relationship Documentation Requirements for Swap Dealers and Major Swap Participants" (the "Proposed Rules") under the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") and the Commodity Exchange Act ("CEA").

CIEBA represents more than 100 of the country's largest pension funds. Its members manage more than $1 trillion of defined benefit and defined contribution plan assets on behalf of 15 million plan participants and beneficiaries. CIEBA members are the senior corporate financial officers who manage and administer corporate retirement plan assets governed by the Employee Retirement Income Security Act of 1974 ("ERISA"). CIEBA's recent annual survey of members showed an increased emphasis on managing and reducing plan risks and a corresponding increase in usage of swaps to address those risks.

Swaps play a critical role for our members' plans. Many plans regulated by ERISA use swaps to hedge or mitigate the risks endemic to plan liabilities and investments. These plans conduct swap transactions through fiduciaries that are subject to stringent regulation under ERISA such as a duty to act solely in the interests of the plan's participants. Consistent with ERISA, we are sure the Commission will want to avoid any possibility that the documentation

requirements of swaps, directly or indirectly, would adversely affect an ERISA fiduciary's ability to obtain the best possible swap terms for plan participants.

If swap trading becomes materially less available to plans, millions of Americans' retirement security would be detrimentally affected. Moreover, funding volatility could increase substantially, undermining participants' retirement security and forcing companies in the aggregate to needlessly reserve billions of additional dollars to satisfy possible funding obligations. Those greater reserves would vastly diminish working capital that would otherwise be available to companies to create new jobs and for other business activities that promote economic growth.

DEVELOPMENTS & INTERACTION OF THE COMMISSION'S PROPOSALS

In recent months, industry developments have occurred that concern ERISA plans. These developments heighten the prospect of negative consequences to ERISA plans if the Commission's proposals are implemented as proposed.

On March 31, the "G14" Dealers and a few others (collectively, the "Signatories") submitted a letter ("Commitment Letter") to the Federal Reserve Bank of New York ("NY Fed") that makes "industry" commitments regarding the processing of derivatives trades. Confusingly, these commitments were made to the NY Fed at the same time as the CFTC had proposed or was considering regulations governing much of the subject matter of the Commitment Letter.

On April 28, 2011, the CFTC released its proposed rules covering Margin Requirements for Uncleared Swaps for Swap Dealers ("SDs") and Major Swap Participants ("MSPs"). The proposed rules would require SDs and MSPs to collect initial margin from their counterparties, with specific minimum margin levels based on whether the counterparty is an SD/MSP, financial entity, or non-financial entity. Likewise, the various banking regulators ("Prudential Regulators") have proposed Margin and Capital Requirements for Covered Swap Entities,[1] which will impose similar requirements.

In its release reopening the comment period on the Proposed Rules, the CFTC notes that the rules which it has proposed "present a substantially complete mosaic of the Commission's proposed regulatory framework for swaps under the Dodd-Frank Act." 76 Fed. Reg. at 25,275. We appreciate the opportunity to provide further comments on the Proposed Rule in the context of these new industry developments and the significant number of other proposals which have been released.

SUMMARY OF FURTHER COMMENTS

Plans need the ability to negotiate customized swaps. *See* Prior Comment Letter at 3-4. Thus, the CFTC should not, in the absence of a Congressional mandate, change customized terms to standardized terms. Nor should the CFTC require plans to accede to ISDA protocols as

[1] 76 Fed. Reg. 27,564 (May 11, 2011).

a part of Dodd-Frank compliance. Plans should not be required to post initial margin on uncleared swaps. *See* Prior Comment Letter at 3-4.

Lastly, a written representation from a plan should be sufficient to satisfy any obligation to demonstrate the adequacy of a plans' independent representative. *See* Prior Comment Letter at 6. Swap dealers and major swap participants should not be permitted to seek confidential non-public information to determine such adequacy. *See* Prior Comment Letter at 6.

SUMMARY OF PRIOR COMMENT LETTER

We remain concerned about, and resubmit all prior comments on, this Proposed Rule by reference to our prior comment letter filed by CIEBA on April 11 ("Prior Comment Letter"). The following summarizes those comments in our Prior Comment Letter which are not discussed further below.

- The proposed rules correctly recognize that all terms should be agreed upon on or before a trade is executed. P. 4-5.
- Proposed rule 23.504(b)(4) appropriately recognizes the need for objective and agreed-upon procedures to resolve valuation of swaps. P. 5-6.
- Policies and procedures of SDs and MSPs should not have the force of law against non-SDs, non-MSPs. P. 3.

FURTHER COMMENTS

Plans must be able to continue to enter into customized swaps.

In its release of the Proposed Rules, the CFTC emphasized the importance of standardizing the ***documentation*** of swaps and noted that "the use of common legal documentation [would] also encourage[] standardization of traded products." Proposed Rules at 6,717. While we understand the benefits of having standard forms of documents to use as a starting point for negotiations and for standardizing documentation processes, we are concerned about the significant cost that plans will incur if ***products and their terms*** are ***required to be*** standardized and plans are deprived of the opportunity to negotiate customized terms applicable to their unique circumstances. *See* Prior Comment Letter at 3-4. Each plan has unique liabilities and the ability of a plan's fiduciary to negotiate swap terms is what allows the plan to effectively hedge those particular liabilities. If plans are limited to using swaps with only standardized terms, plans may not be able to hedge certain risks, a result which is certainly not in the interest of plans. This is not the intent of Dodd-Frank and we do not believe that this is the intent of the Commission either.

The very use of customized terms, which provides plans with effective hedges, also creates challenges for dealers to find offsetting swaps with the same terms. To facilitate the ability of dealers to enter into offsetting swaps that are matched, the swap dealer Signatories commit in the Commitment Letter to "continuing to drive a high level of product and processing

standardization in each asset class" of swaps. Commitment Letter, fn 3. This commitment in the Commitment Letter further escalates CIEBA's concerns about the continued ability of plans to enter into customized swaps that provide effective hedges of plans' liabilities.

Congress acknowledged the importance of customized swaps by ***not*** requiring that all swaps be standardized. Instead, Congress only called for those that ***are*** standardized to be traded on certain platforms.

In the absence of a Congressional mandate to standardize all OTC derivatives products, we believe the CFTC should not require that customized swap terms be changed to standardized swap terms.

The swap dealer Signatories' pledge in the Commitment Letter to standardize OTC derivatives products in every asset class extends beyond Dodd-Frank, which does not require that all swaps be standardized. *See* Commitment Letter at 6, note 3. CIEBA, along with the American Benefits Council, wrote a letter to the NY Fed expressing the concern that the Commitment Letter will be used to bind the buy-side. The NY Fed responded to CIEBA's letter and stated that the commitments made in the Commitment Letter are not binding on non-signatories; and we greatly appreciate the NY Fed's response and position on this issue. We continue to be concerned however, that swap dealers can claim that their obligations are "regulatory" obligations restricting their ability to trade with any counterparty which does not adhere to such commitment.

Although CIEBA sought to get clarification from the NY Fed on this particular issue, the NY Fed's letter to CIEBA did not address the important issue as to whether dealers will be viewed "in violation" of a "regulatory" obligation or subject to negative regulatory consequences if they transact swaps with non-signatory counterparties without adhering to the obligations set forth in the Commitment Letter. Without sufficient clarification, the requirements of the Commitment Letter may be used to bind and regulate the entire universe of swap counterparties that trade with these swap dealers, to the detriment of buy-side market participants.[2] Congress did not intend this nor would such private "regulation" be consistent with U.S. law (e.g., the Administrative Procedures Act).

Congress correctly granted exclusive jurisdiction for swap regulations to the CFTC, which has the power to consider the interest of all market participants (and granted jurisdiction

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[2] Signatories claim that because they submitted a letter to regulators containing commitments that such commitments are "regulatory" obligations of the swap dealers which they must comply with in order to trade with ERISA plan counterparties and that their ERISA plan counterparties must accept terms and/or processes resulting from such commitments even if the plan fiduciary believes it is not in the best interest of the plan. Swap dealer Commitment Letter requirements have included and/or are expected to include the "required":

(a) use of electronic confirmation (we note that virtually all persons who commented on electronic confirmations to the CFTC opposed a requirement to use electronic confirmations);

(b) use of terms developed by swap dealers or swap dealer-dominated trade groups (even though Dodd-Frank does not require standard terms or suggest that standardized terms be dictated by swap dealers); and

(c) use of only the ISDA designated SDR for the relevant swap asset class for swap reporting (even though both Dodd-Frank and CFTC proposals contemplate multiple SDRs). *See, for example,* Proposed Rule 45.7(b), which provides an end user counterparty that is the reporting counterparty with the choice of the SDR to which it would report the data for that swap.

for security-based swap regulations to the SEC). We urge the CFTC to protect market users against swap dealers' claims that such "commitments" are regulatory obligations of the swap dealers that market users must accept. The CFTC's reference to the Commitment Letter process in its release for the proposed rule raises the question of how the CFTC views the commitments of swap dealers in the Commitment Letter and whether the CFTC intends to permit dealers to claim that these commitments are "regulatory" obligations. Accordingly, we believe that market users would greatly benefit from a clarifying statement by the CFTC in its preamble to the final rules.

ISDA Protocols should not be forced upon plans.

The Commitment Letter notes the use of ISDA protocols in efforts to standardize products. Commitment Letter at 26. We are concerned about the use of ISDA protocols to implement changes required by Dodd-Frank. We support the development of form documents such as the ISDA Master Agreement, the ISDA Credit Support Annex to the Schedule to the ISDA Master Agreement, and the various sets of ISDA Definitions, which are intended to provide potential swap counterparties with a common starting point for documentation purposes but which are not expected to be the "required" terms for any swap. In fact, swap dealers and their counterparties nearly universally modify and/or supplement such terms/forms. Although ISDA updates and revises its forms, not all "updates" are viewed positively by buy-side participants.[3] The fact that not all ISDA form "updates" are viewed as improvements underscores the importance that the use of such forms is, currently, completely voluntary and parties can choose to use other documents if they prefer.

In contrast, ISDA protocols, which are typically developed by dealer-dominated ISDA committees, are not form documents which can be revised by the parties. Rather, end users may only adopt these protocols on a "take it or leave it" basis. Accordingly, t**he CFTC should not, either explicitly or implicitly, require market participants to consent to ISDA protocols in order to comply with Dodd-Frank or the CFTC's regulations. Otherwise, the CFTC would be removing the ability of counterparties to SDs/MSPs to protect themselves from ISDA initiatives which may not be in their best interests. To the contrary, the CFTC should acknowledge in its release adopting its final rules that the CFTC rules are not intended to imply that swap dealers or their counterparties are required or encouraged to adopt ISDA protocols.**

Plans must not be required to post initial margin on uncleared swaps.

Requiring initial margin from plans and other end-users goes well beyond Dodd-Frank's requirements. *See* Prior Comment Letter at 5. Indeed, it is contrary to Congress' intent. Senator Chris Dodd stated that "[t]here is no authority to set margin on end users, only major swap participants and swap dealers." Congressional Record--Senate, S5904, July 15, 2010. We are

[3] For example, ISDA's 2002 form Master Agreement which was an update to its 1992 form Master Agreement has been largely unused by buy-side participants and viewed as less favorable than the 1992 Master Agreement.

concerned that Proposed Rule 23.504(b)(3)[4] could be read as requiring plans (which are neither SDs nor MSPs) to post initial margin on uncleared swaps (providing that requisite swap documentation "shall include credit support arrangements, which shall contain . . . initial and variation margin requirements . . . for uncleared swaps"). *See* Prior Comment Letter at 5.

Since filing our Prior Comment Letter, the CFTC and prudential regulators have proposed margin requirements for uncleared swaps that would require SDs and MSPs to collect initial margin from financial entities and to dictate the amount of initial margin that financial entities must post. *See* Proposed Rule 23.153. We will comment on these margin proposal directly, reiterating our prior comment that "[t]here is no authority to set margin on end users, only major swap participants and swap dealers." Congressional Record--Senate, S5904, July 15, 2010. However, even if the CFTC or Prudential Regulators does elect to require initial margin from plans, the CFTC should not do so tacitly through Proposed Rule 23.504(b)(3)(1).

> **To clarify that not all terms listed in proposed rule 23.504(b)(3) would apply to all parties, we request that the Commission revise the proposed rule by adding the words *"if any"* to the end of each of subsections (i) through (iv).**

SDs and MSPs should not be permitted access to plans' confidential non-public information.

Proposed Rule 23.505 would permit an SD or MSP access to considerable amounts of non-public information for the purpose of determining whether a swap is exempt from the mandatory clearing requirement. *See* Prior Comment Letter at 6. While ERISA plans currently do not qualify for the end-user exemption from mandatory clearing, we are concerned about the precedent that this proposal would create that could be applied to plans in other contexts. For example, the CFTC's proposed business conduct standard rules would require any SD or MSP that enters into a swap with an ERISA plan to make certain determinations about the plan's representative. *See* Proposed Rule 23.450(b). The CFTC's proposal would only allow an SD to rely on written representations with respect to this determination if the SD has a reasonable basis to believe that the representations are reliable and if the representations include "sufficiently detailed" information.

We believe that these requirements in Proposed Rules 23.505 and 23.450 could easily result in SDs and MSPs obtaining confidential non-public information, which would give the SDs and MSPs a trading advantage over their end-user counterparties. Accordingly, we believe that:

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[4] The swap trading relationship documentation shall include credit support agreements, which shall contain, in accordance with applicable requirements under Commission regulations or regulations adopted by prudential regulators and without limitation, the following:

(i) Initial and variation margin requirements;
(ii) Types of assets that may be used as margin and asset valuation haircuts;
(iii) Investment and rehypothecation terms for assets used as margin for uncleared swaps; and
(iv) Custodial arrangements for margin assets, including whether margin assets are to be segregated with an independent third party, in accordance with §23.601(e).

Proposed Rule 23.505 should require an SD or MSP to simply obtain from a counterparty claiming the end-user exemption a written representation that the end-user qualifies for the exemption.

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We thank the CFTC for the opportunity to comment on the proposed rules on the swap trading relationship documentation requirements.

Committee on the Investment of Employee Benefit Assets