February 22, 2011

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

Re: RIN 3038-AD25 / Business Conduct Standards for Swap Dealers and Major Swap Participants With Counterparties

Dear Mr. Stawick:

The American Benefits Council (the "Council") and the Committee on Investment of Employee Benefit Assets ("CIEBA") appreciate this opportunity to provide comments to the Commodity Futures Trading Commission (the "CFTC") regarding the proposed rules under the Wall Street Transparency and Accountability Act of 2010 (the "Act" or "WSTAA") relating to business conduct standards for swap dealers and major swap participants (the "Proposed Rules").

The Council is a public policy organization principally representing Fortune 500 companies and other organizations that assist employers of all sizes in providing benefits to employees. Collectively, the Council's members either sponsor directly or provide services to retirement and health plans that cover more than 100 million Americans.

CIEBA represents more than 100 of the country's largest corporate sponsored 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 individually manage and administer ERISA-governed corporate retirement plan assets. 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.

KEY POINTS

We very much appreciated the opportunity to discuss the business conduct standard issues with the CFTC prior to the publication of the Proposed Rules. And we thank the CFTC for the important provisions included in the Proposed Rules pursuant to that dialogue. However, we have to report that the reaction from the plan community to these Proposed Rules has been

one of great alarm and concern. These Proposed Rules are widely viewed as threatening to end plans' ability to use swaps.

Conflict with DOL Proposed Regulations. The concern regarding the Proposed Rules comes from two primary sources. First, there is a lack of coordination between these Proposed Rules and the Department of Labor's ("DOL") proposed new definition of a "fiduciary" published October 22, 2010 ("DOL Proposed Fiduciary Regulations"). The test for fiduciary status under the DOL Proposed Fiduciary Regulations is a functional test, and does not turn on whether the Proposed Rules make reference to fiduciary status. As discussed below, the Proposed Rules would require swap dealers and major swap participants ("MSPs") to take actions that would make them plan fiduciaries under the DOL Proposed Fiduciary Regulations. If a swap dealer or MSP is deemed to be a plan fiduciary under the Employee Retirement Income Security Act of 1974 ("ERISA") and it enters into a swap with that plan, the swap dealer or MSP would be committing a prohibited transaction under ERISA, with devastating consequences. There is no way for a swap dealer or MSP that is a fiduciary to an ERISA plan (a "Plan") to enter into a swap transaction with the Plan without violating ERISA.

Informal discussions between the CFTC and the DOL cannot solve this coordination issue. The coordination can only be addressed through an explicit statement in the DOL regulations that no act required by the CFTC's regulations will make a swap dealer or MSP a fiduciary. If there is not a formal announcement from the CFTC and the DOL to that effect, then no amount of informal discussion between the agencies is likely to prevent these Proposed Rules from having a devastating effect on plans.

A formal resolution of this issue prior to finalization of the Proposed Rules is critical for several reasons. First, there is a very compelling argument that even under the current DOL rules, the Proposed Rules would require swap dealers or MSPs to become ERISA fiduciaries. That would force all swaps to cease as soon as the Proposed Rules are effective. Second, even if a swap dealer or MSP could conclude that it would not become a fiduciary under the current DOL rules, it would have to cease entering into swaps with plans as soon as the DOL Proposed Fiduciary Regulations are effective. This would have a chilling effect on swap activity as soon as the Proposed Rules are finalized.

It is even possible that all previously executed swaps would have to be terminated. We strongly believe that the business conduct standards should not apply to any swaps executed prior to the effective date of those standards. But if this is not the case, the Proposed Rules could require swap dealers or MSPs entering into swaps prior to the effective date of the DOL Proposed Fiduciary Regulations to perform valuation functions that would become fiduciary acts as of the effective date of the DOL Proposed Fiduciary Regulations. If this were to occur, all outstanding Plan swaps would instantly need to be terminated to avoid a prohibited transaction.

In short, we believe that it is absolutely critical that on or before finalization of the Proposed Rules, the CFTC and DOL make a joint formal announcement that no action required by the business conduct standards will make a swap dealer or MSP an ERISA fiduciary. This is far too important an issue for the Proposed Rules to be finalized when there is any uncertainty regarding whether the DOL regulations will be compatible with the CFTC's rules. If the DOL is not prepared to make the announcement when the CFTC is ready to finalize its Proposed Rules, the only workable solution is to delay the finalization of the business conduct standards with

respect to Plans until the DOL is prepared to act. Any other course of action would elevate timing issues over the retirement security of millions of Americans.

Moreover, without the above type of coordination, the CFTC and the DOL would be acting in a manner contrary to the President's Executive Order issued January 18, 2011 (the "Executive Order"), which emphasizes the importance of coordination. In the President's words, coordination means "harmonizing rules" and avoiding "inconsistent" or "overlapping" rules. If it is possible for one agency's rules to require violation of another agency's rules, that is the opposite of coordination.

Counterparty rules. The second primary source of concern is that the rules applicable when a swap dealer or MSP is simply acting as a counterparty are unworkable and will also threaten to end Plans' use of swaps for reasons discussed below. There are two key points in this regard. First, the rules effectively turn all or substantially all swap dealers and MSPs into "advisors", triggering the unworkable requirement that they act in the best interests of both themselves and their counterparty.

Second, even if a swap dealer or MSP is treated solely as a counterparty and not as an advisor, the rules are, for reasons discussed below, unworkable or, at best, highly detrimental to Plans' use of swaps. The solution is straightforward: these "counterparty business conduct rules" do not apply to Plans under the statute. The preamble to the Proposed Rules effectively proves our point. Footnote 106 of the preamble to the Proposed Rules says in effect that the statute is "ambiguous" because Congress could not have intended to say what it said. That is an issue for Congress to resolve. The CFTC has no power to rewrite the statute. Instead of adhering to the statute, the CFTC indicated that it interpreted what Congress must have meant through informal discussions with the public and private sectors. The law must be interpreted based on the language in the statute, not based on informal discussions of what Congress must have meant for the statute to say, nor even on legislative history that is inconsistent with the statute.

THE IMPORTANCE OF SWAPS TO PLANS

Swaps play a critical role for our members' Plans. If new rules regarding business conduct standards for swap dealers make it difficult or more expensive to enter into derivative transactions, Plan fiduciaries might then opt to avoid using otherwise prudent swaps, to the great detriment of millions of Americans' retirement security.

Pension Plans use swaps to manage risk resulting from the volatility inherent in determining the present value of the Plan's liability, as well as to manage, and reduce reliance on, Plan funding from the companies maintaining defined benefit plans. If swaps were to become materially less available or become significantly more costly to pension Plans, funding volatility could increase substantially, creating risks for participants (especially in underfunded plans) and forcing companies in the aggregate to reserve billions of additional dollars to satisfy possible funding obligations, most of which may never need to be contributed to the Plan because the risks being reserved against may not materialize. Those greater reserves would have an enormous effect on the working capital that would be available to companies to create new jobs and for other business activities that promote economic growth.

This volatility issue, both for Plans and their respective company sponsors, is critical and merits further discussion. In a defined benefit pension Plan, a retiree is promised payments in the future. The obligations of a pension Plan include a wide range of payments, from payments occurring presently to payments to be made more than 50 years from now. The present value of those payments varies considerably with interest rates. If interest rates fall, the present value of liabilities grows. So if interest rates drop quickly, the present value of liabilities can grow quickly, creating additional risk for participants and huge economic burdens for the company sponsoring the plan. Swaps are used to address this risk, as illustrated in a very simplified example below (which has been recently updated).

Assume that a Plan has $15 billion of assets and $15 billion of liabilities so that the plan is 100% funded and there is thus no shortfall to fund. Assume that interest rates fall by 1 percentage point. That alone would increase liabilities substantially. Based on a real-life example of a Plan whose interest rate sensitivity is somewhat higher than average, we assume a 13% increase in plan liabilities to $16.95 billion. Based on a realistic example, we assume that assets increase to $15.49 billion. Thus, the decline in interest rates has created a $1.46 billion shortfall. Under the general pension funding rules, shortfalls must be amortized over seven years, so that the Plan sponsor in this example would suddenly owe annual contributions to the Plan of approximately $248 million, starting with the current year. A sudden annual increase in cash outlays of $248 million can obviously present enormous business challenges, as well as increased risks for participants due to the Plan becoming underfunded. If a Plan is underfunded and is turned over to the PBGC, the participants will not, in many cases, receive 100% of their promised benefit. Their benefit will be based on PBGC rules, including a limit on total benefits, which could result in a substantial reduction of the originally promised benefit. It is in the best interest of all Plan participants to have a fully funded Plan.

Swaps are a very important hedging tool for Plans. Hedging interest rate risk with swaps effectively would avoid the above underfunded result by creating an asset -- the swap -- that would rise in value by the same $1.46 billion if interest rates fall by 1 percentage point. Thus, by using swaps, Plans reduce the risk of becoming underfunded and Plan sponsors are able to avoid the risk of sudden increases in cash obligations of hundreds of millions of dollars. If, on the other hand, Plans' ability to hedge effectively with swaps is curtailed by the new rules, funding obligations will become more volatile, as illustrated above. This will, in turn, increase risk for participants and force many employers to reserve large amounts of cash to cover possible funding obligations, thus diverting cash from critical job retention, business growth projects, and future pension benefits.

Without swaps, some companies would attempt to manage pension plan risk in other ways, such as through the increased use of bonds with related decreases in returns. One company recently estimated that its expected decrease in return that would result from the increased use of bonds would be approximately $100 million. And this pain would be felt acutely by individuals. Companies that lose $100 million per year may well need to cut jobs and certainly will have to think about reducing pension benefits.

We also note that the bond market is far too small to replace swaps entirely as a means to hedge risks by immunizing Plans. There are not nearly enough bonds available, especially in the long durations that Plans need. In short, a shift from swaps to bonds would be costly, insufficient, and potentially harmful (in terms of volatility) for Plans.

For the reasons discussed above, the issues we raise regarding the business conduct standards are of great importance to our members, to the Plan system generally, to the Plan sponsor companies, and to the economy. We look forward to working with you to ensure that the new rules strengthen financial regulations in a manner that enhances workers' retirement security. It is critical that the new rules not be interpreted in a way that undermines such security.

COORDINATION WITH DOL

The CFTC should ensure that swap dealers would not be considered "fiduciaries" under ERISA due to the application of the business conduct standards

The Proposed Rules include several requirements that would transform swap dealers and MSPs into Plan fiduciaries, with the dire consequences referenced above.

Review of plan's representative. Under Prop. Reg. § 23.450(b), if a swap dealer or MSP is simply entering into a swap with a Plan, the swap dealer or MSP must engage in a swap-by-swap in-depth analysis of whether the Plan's representative is qualified to function as an advisor to the plan. It is clear under the Proposed Rules that the swap dealer may not simply accept representations to that effect, but rather must engage in its own scrutiny of any representations given. Thus, there is a very strong argument that the swap dealer or MSP is effectively rendering advice to the Plan regarding its choice of an advisor. As noted in the preamble to the DOL Proposed Fiduciary Regulations, advice to a plan regarding its choice of an investment advisor is a fiduciary act under such regulations. Thus, the swap dealer or MSP may well be treated as a fiduciary with respect to the Plan, triggering a prohibited transaction. Unless the two sets of proposed regulations are modified, this analysis could result in a cessation of all Plan swaps.

Additionally, under ERISA, only a fiduciary to the Plan can hire or fire another fiduciary. It is the duty of the "lead fiduciary" to ensure that a Plan advisor is qualified to advise a Plan or act on the Plan's behalf. The Proposed Rules infringe upon the lead fiduciary's duties and obligations and create unnecessary duplication in reviewing a Plan representative's qualifications.

Two other points should be made here. First, there has been some discussion of the possibility that the "seller exemption" under section 2510.3-21(c)(2)(i) of the DOL Proposed Fiduciary Regulations could apply to prevent a swap dealer or MSP from becoming an ERISA fiduciary by reason of reviewing a Plan's representative. The seller exemption, as written, would have no application here. An entity reviewing a Plan's representative is not acting as a seller. Sellers promote their investment products; sellers do not advise buyers on their choice of an advisor.

Second, as discussed further below, this required review of a Plan's representative raises serious issues separate from the DOL Proposed Fiduciary Regulations.

Providing the daily mark. Section 23.431(c) of the Proposed Rules requires that the swap dealer or MSP provide its counterparty, including a Plan, with the daily mark. Section 2510.3-21 of the DOL Proposed Fiduciary Regulations makes it clear that providing valuation services to a Plan is a fiduciary act (subject to a very limited valuation exception that would

clearly not apply). This creates an irreconcilable conflict. A swap dealer or MSP entering into a swap with a Plan would automatically become an ERISA fiduciary by reason of complying with the Proposed Rules; as noted above, that would make any swap with a Plan a prohibited transaction.

Again, the seller exemption under the DOL Proposed Fiduciary Regulations would have no application here. It is not part of a seller's function to provide appraisal services. And appraisal services provided after contract execution have no relationship to selling.

Risk analysis. Under Prop. Reg. § 23.431(a), if a plan enters into a swap with a swap dealer or MSP, the swap dealer or MSP must provide the plan with "material information concerning the swap in a manner reasonably designed to allow the [plan] to assess…[t]he material risks of the particular swap,…[t]he material characteristics of the particular swap,…and…[t]he material incentives and conflicts of interest that the swap dealer or [MSP] may have in connection with the particular swap." Moreover, in the case of a high-risk complex bilateral swap, the swap dealer or MSP must provide the plan with:

> a scenario analysis designed in consultation with the [plan] to allow the [plan] to assess its potential exposure in connection with the swap. The scenario analysis shall be done over a range of assumptions, including severe downturn stress scenarios that would result in significant loss.

Prop. Reg. § 23.431(a). The definition of a high-risk complex bilateral swap is not entirely clear, but it appears likely broad enough to sweep in many swaps commonly entered into by Plans. Even if the swap is not a high-risk complex bilateral swap, but it is a bilateral swap that is not available for trading on a designated contract market or swap execution facility, the swap dealer or MSP must provide the Plan with a scenario analysis upon request.

Unless the seller exemption in the DOL Proposed Fiduciary Regulations is expressly interpreted to apply here, a swap dealer or MSP that complies with the above would be a fiduciary under the DOL Proposed Fiduciary Regulations, thus creating a prohibited transaction. The swap dealer or MSP (1) would be providing a Plan with individualized investment advice regarding investment risks, (2) the advice "may be considered" by the Plan, and (3) the swap dealer or MSP would receive compensation under the swap agreement. Some have argued that the swap dealer or MSP's advice is not really advice, but rather the provision of objective data. This argument is misplaced for two reasons. First, risk analyses are not rote exercises based on universally accepted facts; they are highly subjective and will vary greatly, as demonstrated by the fact that the Proposed Rules recognize that the scenario analyses may be based on confidential proprietary information. Prop. Reg. § 23.431(a)(1)(iv). Second, the DOL Proposed Fiduciary Regulations do not contain any general exception for advice based on factual data. On the contrary, the existence of very specific exceptions for specified factual data raises a strong inference that no such general exception applies.

As noted, the Proposed Rules and the DOL Proposed Fiduciary Regulations must be coordinated to avoid the devastating effects described above. In this regard, it is critical that prior to finalization of the Proposed Rules, the CFTC and the DOL issue a joint statement that

the DOL's regulations will state that no action required by reason of the CFTC's regulations will transform a counterparty into a fiduciary under ERISA.

THE DEFINITION OF "RECOMMEND" NEEDS TO EXCLUDE ACTIONS TAKEN AS A COUNTERPARTY.

Under Prop. Reg. §§ 23.434 and 23.440, if a swap dealer or MSP "recommends" a swap or trading strategy to a Plan, the swap dealer or MSP has (1) a duty to act in the best interests of the Plan, and (2) a duty to have a reasonable basis to believe that the swap is suitable for the Plan.

So the question is: under what circumstances would a swap dealer or MSP be treated as "recommending" a swap or trading strategy. The preamble to the Proposed Rules states that a:

> recommendation would include any communication by which a swap dealer or major swap participant provides information to a counterparty about a particular swap or trading strategy that is tailored to the needs or characteristics of the counterparty, but would not include information that is general transaction, financial, or market information, swap terms in response to a competitive bid request from the counterparty.

In our view, if the swap dealer or MSP clearly informs the Plan in writing that the swap dealer or MSP is functioning as a counterparty and not as an advisor, nothing communicated to the Plan by the swap dealer or MSP should be treated as a recommendation within the rules. At a minimum, this should be true if the Plan has an advisor with respect to its swaps that is sufficiently regulated, such as a bank, an SEC-registered investment advisor, an insurance company, a registered municipal advisor, or a similarly qualified advisor (such as a QPAM, INHAM, or other ERISA service provider). But the Proposed Rules contain no such exemption. On the contrary, the Proposed Rules are naturally read to turn common-place selling—e.g., "this is appropriate for you because it addresses your need to hedge your interest rate risk"—into a "recommendation", triggering a duty of the swap dealer or MSP to act in the best interests of the plan. In fact, the definition of "recommend" in the Proposed Rules is so broad that the scenario analyses and other risk information required by the Proposed Rules themselves would require all swap dealers and MSPs to provide recommendations, a result clearly not intended.

It is critical that swap dealers and MSPs acting solely as counterparties or potential counterparties (and clearly disclosing that) not be treated as making recommendations. By making a recommendation, a swap dealer or MSP must act in the best interests of the plan. One party clearly cannot act in the best interests of the other party. Their interests are by definition adverse.

One other issue would arise if a swap dealer or MSP were treated as making a recommendation. If a swap dealer or MSP were treated as making a recommendation, the swap dealer or MSP must seek extensive information about a Plan and must obtain at least enough information to conclude, for example, that the Plan is "capable of absorbing potential losses related to the recommended swap." This is a significant problem. If Plans need to provide their counterparty with financial information in order to enter into a swap, that would severely disadvantage Plans by giving their counterparty a large information advantage in negotiations.

The information may also include benefit liabilities, which could raise issues for Plan participants.

It is important to note that the above problems attributable to a swap dealer or MSP being treated as making a recommendation exist without regard to the DOL rules. These are independent problems that can only be solved through modifications of the Proposed Rules.

OTHER COUNTERPARTY ISSUES

The Act added a new section 4s(h)(5) to the Commodity Exchange Act (the "CEA") which sets forth certain business conduct standards that the CFTC may impose on swap dealers and MSPs that simply offer to or enter into a swap with a "Special Entity" (as such term is defined in the Act) ("Counterparty Business Conduct Standards"). We offer the following comments on the Proposed Rules implementing that provision.

The Counterparty Business Conduct Standards should not apply to Plans

The Act provides that swap dealers and MSPs must comply with the Counterparty Business Conduct Standards with respect to "a counterparty that is an eligible contract participant within the meaning of subclause (I) or (II) of clause (vii) of section 1a(18) of this Act." Therefore, the Counterparty Business Conduct Standards only apply to a counterparty that is:

> (vii) (I) A governmental entity (including the United States, a State, or a foreign government) or political subdivision of a governmental entity; [or]
>
> (II) A multinational or supranational government entity.

As discussed above, since Plans do not fall within either (I) or (II) above, swap dealers and MSPs should not need to comply with the Counterparty Business Conduct Standards when entering into trades with Plans. We strongly object to the recharacterization of the statutory requirements of section 4s(h)(5). The plain language of the Act clearly provides that the Counterparty Business Conduct Standards apply only to certain governmental Special Entities. By applying the Counterparty Business Conduct Standards to all Special Entities, the CFTC has extended its regulatory reach significantly beyond the scope of the statute. In addition, the statutory exclusion of Plans from the Counterparty Business Conduct Standards is a proper policy outcome since Plans already have similar or greater protections under ERISA with respect to each of the requirements.

In addition, to impose the Counterparty Business Conduct Standards on Plans, which are heavily regulated by ERISA with respect to the same issues, would create exactly the type of "redundant" and "overlapping" regulations that the President is critical of in his recent Executive Order. At a minimum, the Counterparty Business Conduct Standards should not apply to a Plan that has an advisor with respect to its swaps that is sufficiently regulated, as noted above, such as a bank, an SEC-registered investment advisor, an insurance company, a registered municipal advisor, or a similarly qualified advisor (such as a QPAM, INHAM, or other ERISA service provider).

In short, in applying the Counterparty Business Conduct Standards to Plans, the Proposed Rules disregard the statute in favor of informal speculation as to Congressional intent, and are clearly inconsistent with the Executive Order. The Proposed Rules need to be modified to exclude Plans from these new Counterparty Business Conduct Standards.[1]

Application of the Counterparty Business Conduct Standards; reasonable representations regarding a Plan advisor should be sufficient

If the CFTC retains its current position that, contrary to the statute, all of the Counterparty Business Conduct Standards apply to ERISA plans, it is critical that those standards apply in a manner that is workable.

Section 23.450(b) of the Proposed Rules requires any swap dealer or MSP that enters into a swap with a Plan to make certain determinations about a Plan's representative. Section 23.450(d) of the Proposed Rules permits a swap dealer[2] to rely on written representations with respect to the Special Entity but only if (i) the swap dealer has a reasonable basis to believe that the representations are reliable, assessed in the context of a particular transaction; and (ii) the representations include "sufficiently detailed" information, for which the "relevant considerations" include: the relationship between the Special Entity and the representative; the representative's capability; its use of consultants; its level of experience (including for the relevant asset class); and other items. We believe that these requirements, with the lengthy list of items that must be addressed in the representations and considered by the swap dealer, are very harmful to Plans for several reasons.

First, these Proposed Rules would give undue influence to swap dealers in dealing with representatives. Fundamentally, we believe that swap dealers acting in a counterparty role should not have the ability to disqualify a representative that has been carefully selected by a Plan's fiduciary and is trusted by a Plan. The ability of swap dealers to disqualify representatives—without regard to whether the ability is used— would give them enormous leverage; a representative that does not want to be disqualified would be tempted to relax its negotiating position so as to retain its role. We note that section 23.450(e) requires a swap dealer to report a rejection of a representative to the dealer's Chief Compliance Officer. We do not believe this provides Plans with meaningful protection. Our concern arises from the extensive structural leverage dealers have over representatives. Reporting a negative result to an officer of the dealer would not have a material effect on that leverage.

Second, swap dealers may refuse to face the risks associated with determining the capability of a representative and cease trading with Plans. Swap dealers would face potential litigation risk if they approved a representative who is subsequently determined to be lacking

[1] Subclause (VII) of the business conduct standards explicitly applies to Plans. As discussed more extensively in the Council's September 8 letter to the CFTC (and the Securities and Exchange Commission), we believe that it is entirely consistent to require Plans to be subject to subclause (VII) but not the other subclauses of the business conduct standards.

[2] Section 23.450(d) does not apply to MSPs although it is not clear why MSPs are excluded. We believe that MSPs should be able to rely on a representation from a Special Entity in the same way that a dealer is able to do so.

needed expertise, even if such lack of capability had no effect on the transaction. In addition, swap dealers and MSPs would be subject to litigation from representatives whom they have chosen to disqualify.

Finally, the requirements under the Proposed Rules are overly detailed and cumbersome. Plans that invest funds for tens of thousands of participants enter into a large amount of swaps and it would be inefficient to require their counterparties to conduct such extensive due diligence each time a new transaction was proposed, especially if the Plan representative remained the same. In fact, as discussed further below, requiring a separate inquiry with respect to each swap, as is clearly required under the Proposed Rules, would cripple Plans' ability to implement the time-sensitive swaps that are needed to effectively hedge their risks.

Instead of the inefficient and counterproductive set of rules currently proposed, we urge the CFTC to provide that such Counterparty Business Conduct Standards shall be treated as satisfied in the case of Plans if once, at the beginning of a trading relationship between a Plan and a swap dealer or MSP (or, if later, the beginning of a representative's relationship with a Plan):

- The swap dealer or MSP receives the following written representations from a Plan fiduciary (which may be the plan representative) that, to the reasonable knowledge of such entity:
    - The representative has sufficient knowledge to evaluate swap transactions and risks;
    - The representative is not subject to a statutory disqualification under ERISA, the Commodity Exchange Act, or the Securities Exchange Act of 1934, to the extent applicable;
    - The representative does not have a relationship with the swap dealer or MSP that would give rise to a prohibited transaction under ERISA with respect to the swap;
    - The representative shall undertake to act in the best interests of the Plan as required by ERISA;
    - The representative shall provide all disclosures that are appropriate under ERISA;
    - The representative shall review the price and appropriateness of each swap pursuant to the investment guidelines established by the Plan;
    - The representative is a fiduciary under ERISA with respect to each swap for which it provides advisory services to the plan; and
    - The Plan fiduciary shall notify the swap dealer or MSP if any of the above has changed.
- The swap dealer or MSP has no actual knowledge that any of the representations is incorrect and has not received a notification that any of the representations has changed. (This rule would apply continuously, not just at the commencement of the relationship.)[3]

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[3] In analogous situations, regulators have permitted reliance on similar certifications. For example, under Rule 144A, under the Securities Act, a seller of securities is entitled to rely on a certification by an executive officer of the purchaser that the purchaser meets the conditions

- The swap dealer or MSP makes the disclosure regarding the capacity in which it is acting, as discussed below.

"Material Business Relationships" for Plans should be established under ERISA

Pursuant to the requirement that the representative be independent of the swap dealer or MSP, section 23.450(c)(3) of the Proposed Rules effectively prohibits a swap dealer or MSP from having a "major business relationship" with a Plan's representative and requires the representative to disclose to a Plan any compensation it has received from a swap dealer or MSP with which a Plan is entering into a swap. As noted above, we urge the CFTC to provide that a "major business relationship" does not exist if the relationship between the dealer or MSP and the Plan is a relationship that would not give rise to a prohibited transaction under ERISA. There is extensive regulation under ERISA of the relationship between an advisor and counterparties; these ERISA rules scrupulously prevent advisors from having a relationship with a counterparty that could influence the advisor's advice to a Plan. These ERISA rules have been developed over time and address the specific needs of Plans and of the market. There is no reason to super-impose a new and burdensome new set of regulations on this relationship, i.e., "redundant" and "overlapping" rules in the words of the Executive Order.

If the "material business relationship" rules remain applicable to Plans, we urge the CFTC at a minimum to clarify the disclosure requirement so that it only relates to compensation received in connection with the related swap. Many plans use representatives that are large financial institutions that routinely conduct business worldwide with many swap dealers and MSPs. Requiring representatives to determine all compensation it has received from a swap dealer or MSP in connection with all other transactions worldwide would impose staggering administrative burdens, and likely in the end is simply impracticable. In addition, even if this compensation information were obtained, it would not be of any meaningful significance to a Plan, since it is inevitable that large market participants will have extensive relationships with each other. Therefore, we urge the CFTC to clarify that the information regarding compensation required to be provided to Plans should be restricted to the swap transaction under consideration by the Plan.

Disclosures regarding the capacity in which a swap dealer acts should be streamlined

Section 23.450(f) of the Proposed Rules requires any swap dealer or MSP to disclose to a Plan the capacity in which it is entering into a swap and the material differences between the capacities in which such swap dealer or MSP deals with the Plan in other contexts and with

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necessary to establish that the purchaser is a qualified institutional buyer ("QIB"). Rule 144A (d)(1)(iv). The Adopting Release for Rule 144A states that: "[u]nless circumstances exist giving a seller reason to question the veracity of the certification, the seller would not have a duty of inquiry to verify the certification." We believe these procedures have worked well in the securities markets and we urge the CFTC to adopt a similar standard, which would be more efficient and more helpful to Plans than the standard set forth in the Proposed Rules.

respect to this particular swap. We urge the CFTC to make two points clear: (1) that the disclosure about the swap dealer or MSP's capacity and its other dealings with the Plan can be made on an "omnibus" basis for multiple swaps and (2) that disclosure regarding a swap dealer's or MSP's other relationships with the Plan need only be made with respect to the swap in question.

Capacity. The Proposed Rules recognize that nearly all swaps are executed under ISDA Master Agreements which contain representations and covenants and contemplate the ability to make some of the proposed representations in such Master Agreements.[4] We urge the CFTC to allow swap dealers and MSPs to represent the capacity in which they are acting with respect to the Plan in the Master Agreement, which could be changed with respect to an individual swap if a swap dealer or MSP were to act in a different capacity. As Plans generally deal with swap dealers and MSPs in the same capacity (as counterparties), we believe that this would be an effective and non-burdensome way to make such representations, and we note that the CFTC has already contemplated this for other representations.

The Proposed Rules require the “capacity disclosure” to occur prior to “the initiation of a swap”. We are not sure what that means. We believe that requiring inclusion in the Master Agreement would be clear and would achieve the purpose of the statute very effectively.

Other Relationships. Swap dealers and MSPs are typically large financial entities that often have many different lines of business and may therefore have many different types of relationships with a Plan. Requiring swap dealers and MSPs to list all such relationships every time they act as a counterparty to a Plan, and for the Plan to review such disclosures, would be a very significant administrative burden. In addition, since such relationships are often completely independent of a swap transaction, this information would not be meaningful to the Plan, especially in a context where the swap dealer or MSP is clearly acting as a counterparty (and has already represented so, as per the above paragraph). Therefore, we urge the CFTC to clarify that the disclosure regarding other relationships would only need to be made if the swap dealer or MSP is also acting in another capacity with respect to the swap.

SWAP DEALERS AND MSPs SHOULD NOT BE PERMITTED TO USE REPRESENTATIONS AGAINST THE PLAN OR ITS REPRESENTATIVE

The Proposed Rules require Plans to make representations regarding the suitability of their representative (section 23.450(d)). We urge the CFTC to state explicitly that these representations do not give any party any additional rights, such as rescission or monetary compensation. For example, if, due to changing economic conditions, a swap between a swap dealer and a Plan has become very disadvantageous for the swap dealer, the swap dealer should not be able to void the swap, or make any other type of claim against the Plan or its representative, by asserting that one or more of the representations made by the Plan or its representative were incorrect. The Counterparty Business Conduct Standards, which were meant to protect Plans and other Special Entities, should not be turned into a weapon that can be used against Plans or their representatives.

[4] See footnote 27 of the preamble to the Proposed Rules.

This approach would be consistent with other regulations. For instance under Rule 144A, if the certification as to a party's QIB status is reasonably obtained, the recipient of the certification may treat its counterparty as a QIB. A subsequent determination that the certification was wrong will not retroactively void the QIB institution status of the counterparty. We urge the CFTC to establish a similar standard for representations by Plans.

INABILITY TO HEDGE RISKS EFFICIENTLY

There are many situations where market exposures or a Plan's market needs dictate that swaps occur very quickly. This is particularly true with respect to a program of interest rate hedges. In these situations, there is simply no time for all of the extensive business conduct requirements to apply on a swap-by-swap basis. If a swap needs to be executed by the end of the day to protect a plan from interest rate risk, there is no time, and no need, for, for example:

- The swap dealer or MSP to evaluate the trading purposes of the plan;
- The swap dealer or MSP to provide information regarding the material risks of the swaps;
- The swap dealer or MSP to determine if a scenario analysis is required and, if so, provide it;
- The swap dealer or MSP to provide information regarding its material incentives or conflicts of interest; and
- The swap dealer or MSP to thoroughly review the plan's advisor.

It is critical that the Proposed Rules be modified (1) to permit all business conduct requirements to be satisfied upfront at the beginning of a trading relationship between a Plan and a swap dealer or MSP, and/or (2) to permit a Plan to waive application of the business conduct standards. The business conduct standards were intended to protect Plans. It would be sadly ironic if a Plan were exposed to far greater risk by reason of being unable to hedge its risks effectively because of the time-consuming nature of the business conduct requirements.

Underlying this point (and much of this comment letter) is a key theme. We are not aware of a single Plan that sees any benefit flowing from the business conduct requirements. Plans by law must have their own experts and have no interest in counsel from their counterparties. Thus, the business conduct requirements can only present the problems identified in this letter; with regard to the issue addressed in this section, the time-consuming nature of the business conduct requirements would simply prevent timely and effective hedging of risk.

KNOW YOUR COUNTERPARTY RULE SHOULD BE DELETED

Under the "know your counterparty" rules in section 23.402(c), a swap dealer or MSP must seek to obtain facts necessary to, for example:

- Effectively service the counterparty;
- Implement any special instructions from the counterparty; and

- Evaluate the previous swaps experience, financial wherewithal and flexibility, trading objectives and purposes of the counterparty.

This rule has several key flaws:

- The rule has no basis in the statute.

- The rule seems to be transforming the swap dealer or MSP into a service provider in ways we do not understand. The swap dealer or MSP is a Plan's counterparty, not an entity that "services" the Plan.

- The rule indicates that swap dealers need to obtain financial information from Plans. If plans had to provide financial information to their counterparties, Plans would have a severe negotiating and informational disadvantage.

The know your counterparty rules should be deleted.

SPECIAL ENTITIES

Collective investment vehicles should not be Special Entities

We urge the CFTC to clarify that the definition of "Special Entity" does not include collective investment vehicles in which Plans invest and that collective investment vehicles would not become Special Entities as a result of investment by Special Entities in such vehicles. Examples of such vehicles include bank collective trust funds that consist of assets of unrelated pension plans[5] and investment funds that are more than 25% held by ERISA plans and thus subject to ERISA.[6] If the CFTC does not clarify that collective investment vehicles are not Special Entities, it would create significant confusion in the market. Swap dealers and MSPs could not be certain if their counterparties require the same protections as Special Entities. In addition, swap dealers and MSPs would have to conduct thorough analyses of counterparties to determine if they contained any Special Entity assets (no matter how minor), as they would otherwise be at risk of violating the business conduct rules. While we recognize that, for instance, master trusts holding the assets of one or more funded plans of a single employer may fall within the definition of Special Entity, we believe that it would go against the statutory intent to regulate all collective investment vehicles as Special Entities. Therefore, we urge the CFTC to provide clarity to the markets.

. . .

It is critical that Plans continue to be able to use swaps to provide retirement security and health benefits to millions of Americans across the country. Plans are unique, heavily regulated entities that are required by law to act prudently in the sole interest of Plan participants and that

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[5] See, e.g., Section 3(c)(11) of the Investment Company Act of 1940; Section 3(a)(2) of the Securities Act of 1933; and CFTC Regulation 4.5 (each providing applicable exclusions for bank collective trust funds).

[6] See ERISA "Plan asset regulation"; 29 CFR § 2510.3-101.

do not need extra layers of unnecessary requirements that would adversely affect participants. It is critical that the new law not be interpreted in such a way as to eliminate important tools that Plans now use to obtain mitigate risks with respect to their Plan assets and liabilities.

We thank the Commission for the opportunity to comment on the Proposed Rules.

American Benefits Council   Committee on Investment of Employee Benefit Assets