COMMITTEE ON FUTURES AND DERIVATIVES REGULATION

TIMOTHY P. SELBY
CHAIR
90 PARK AVENUE
NEW YORK, NY 10016
Phone: (212) 210-9494
Fax: (212) 922-3894
tim.selby@alston.com

MATTHEW W. MAMAK
SECRETARY
90 PARK AVENUE
NEW YORK, NY 10016
Phone: (212) 210-1256
Fax: (212) 922-3952
matthew.mamak@alston.com

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

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: Business Conduct Standards for Swap Dealers and Major Swap Participants With Counterparties, RIN 3038-AS25 (the "Proposed Business Conduct Rule"), Further Definition of "Swap Dealer," "Security-Based Swap Dealer," "Major Swap Participant" and "Eligible Contract Participant," RIN 3235-AK65 (the "Proposed Definition Rule"), End-User Exception to Mandatory Clearing of Swaps, RIN 3038-AD10 and RIN 3235-AK88 (collectively, the "Proposed End-User Rule") and Confirmation, Portfolio Reconciliation, and Portfolio Compression Requirements for Swap Dealers and Major Swap Participants, RIN 3038-AC96 (the "Proposed Confirmation Rule)

Dear Secretary Stawick and Secretary Murphy:

We write on behalf of the Committee on Futures and Derivatives Regulation (the "Committee") of the New York City Bar Association (the "Association") to provide comments to the Commodity Futures Trading Commission (the "CFTC") and the Securities and Exchange Commission (the "SEC" and, together with the CFTC, the "Commissions") with respect to the above-captioned proposed rules.

The Association is an organization of over 23,000 members. Most of its members practice in the New York City area. However, the Association also has members in nearly every state and over 50 countries. The Committee consists of attorneys knowledgeable about the trading and regulation of futures contracts and over-the-counter derivative products, and it has a practice of publishing comments on legal and regulatory developments that have a significant impact on futures and derivatives markets.

Set forth below are the Committee's comments concerning issues that we believe ought to be addressed in any final rulemaking in relation to the above-captioned proposed rules. These comments are in addition to the points made regarding rulemakings with respect to the Dodd-Frank Wall Street Reform and Consumer Protection Act in our letters dated September 20, 2010 and November 29, 2010.

I. Proposed Business Conduct Rule

We are concerned by the breadth of the proposed standard for disclosure of "material" information by a Swap Dealer or Major Swap Participant ("MSP" and, together with a Swap Dealer, a "Swap Entity") to any counterparty other than a Security-Based Swap Dealer (an "SBSD"), Major Security-Based Swap Participant ("MSSP") or Swap Entity (any such entity being a "non-Swap Entity"). Section 23.431(a)(1) of the Proposed Business Conduct Rule broadly defines the scope of disclosure to include information reasonably designed to allow the non-Swap Entity to assess, among others, "[m]arket, credit, liquidity, foreign currency, legal, operational, and any other applicable risks." Moreover, citing *CFTC v. R.J. Fitzgerald & Co.*, 310 F.3d 1321, 1328029 (11th Cir. 2002), the CFTC proposes applying the *R.J. Fitzgerald*-derived standard for assessing the materiality of information, stating: "[i]nformation is material if there is a substantial likelihood that a reasonable counterparty would consider it important in making a swap related decision."

Because persons who are not Swap Entities are required to be Eligible Contract Participants (in order for them to trade other than on a designated contract market)[1] and, as a result, are presumed to have a certain level of financial wherewithal and/or sophistication, we believe that the required disclosure of material risks need not to be, and accordingly ought not to be, modeled analogously to the standard for disclosure in the securities markets, which of course caters to investors of all levels of sophistication. The differing investor audiences lend themselves to different approaches. Moreover, the existence of substantial statutory disclosure requirements in the securities markets, as opposed to the over-the-counter derivatives market, reflects the Congressional view that the purchase and sale of securities pose special risks to investors. For these reasons, we believe that the affirmative protections resembling those in the securities markets are not appropriate when balanced against the costs and legal risks inherent in attempting to comply with an ambiguous and non-objective requirement. In this regard, we would encourage the CFTC to consider the appropriate size and cost of the disclosure document and we note that form disclosure (such as that used for listed options) may be an appropriate alternative to individualized disclosures.

As another alternative to the proposed requirement in §23.431 to disclose "material" information, we support instead limiting required disclosure to non-Swap Entities to provision of scenario analyses[2] to non-Swap Entities and, in lieu of there being one standard of scenario

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[1] See §23.431(b)(1) of the Proposed Business Conduct Rule which states that the above-cited provisions shall not apply to a transaction initiated on a designated contract market or a swap execution facility. Section 2(e) of the CEA prohibits a non-Eligible Contract Participant to enter into a swap other than on a designated contract market.

[2] §23.431(1)(i) of the Proposed Business Conduct Rule requires provision of scenario analyses upon request of a non-Swap Entity.

analysis for ordinary swaps and a different one for "high-risk complex bilateral swaps,"[3] we suggest combining the standards and requiring the provision of robust market risk scenario analyses, defined in scope, in advance of all swaps between Swap Entities and non-Swap Entities. The requirements for such scenario analyses should allow for a more objective interpretation. For example, in analyzing interest rate sensitivity, the rule could mandate an analysis of interest rate conditions up to a certain number of standard deviations away from the expected interest movements based on historical interest rate movements. Such objective standards would provide a higher degree of certainty for the marketplace in determining how to comply with these proposed requirements, thereby limiting the need for judicial interpretation.

We are concerned that the proposed requirement in §23.433 that communication be in a "fair and balanced manner based on principles of fair dealing and good faith," while mandated by the Dodd-Frank Act, lacks appropriate detail and creates uncertainty and risks from a compliance perspective. We recommend that the regulators consider using safe harbors containing objective standards as a means to satisfy the statutory requirements.

With respect to the proposed requirement in §23.434 that there be reasonable grounds to believe that a recommendation is "suitable," we support the concept underlying the provisions in §23.434(b)(1) providing for circumstances in which a Swap Entity is deemed to have satisfied this requirement. We would, however, for reasons of logical consistency, suggest that §23.434(b)(1)(i) and (iii) expressly apply to MSPs as well as Swap Dealers. We believe this to be an unintentional oversight because the first paragraph of §23.434(b)(1) expressly lists MSPs. We also would suggest, in light of the reasoning behind the Eligible Contract Participant status, that the CFTC consider whether a counterparty's status as such should be sufficient to form, pursuant to §23.434(b)(1)(i), a "reasonable basis to believe that the counterparty is capable of evaluating, independently, the risks related to a particular swap or trading strategy."

Similarly, with respect to proposed §155.7's requirement that, for a bilateral swap, there be a "reasonable relationship" to best terms available on a derivatives contract market or swap execution facility, we would recommend a carve-out similar to that in §23.434(b)(2)(i) to account for the sophisticated nature of the Eligible Contract Participant counterparties.[4]

II. Proposed Definition Rule

The Proposed Definition Rule details the *de minimis* exemption to registration as a Swap Dealer or SBSD (Swap Dealer and SBSD together being a "Dealer").[5] A particular benefit of a *de minimis* exemption is it provides certainty to parties that may only occasionally

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[3] See §23.431(a)(1)(ii) of the Proposed Business Conduct Rule.

[4] As the CFTC notes in the Proposed Rule, these "best terms" requirements would effectively apply to parties utilizing the "end-user" exemption. With respect to parties utilizing the end-user exemption pursuant to the Proposed End-User Rule, the requirements to demonstrate financial wherewithal and sophistication are above and beyond those required of even an Eligible Contract Participant.

[5] See proposed §1.3(ppp)(4) and 3a71-2.

enter into a swap but which, on a strict, conservative construction of the standards proposed by the Commissions for a Dealer, otherwise might be construed as a Dealer requiring registration, while not intending to be or engaged in any swap dealing business. We have received feedback from a wide variety of market participants that the proposed *de minimis* exemption is quite low. A higher threshold for the *de minimis* exemption is a simple way to avoid the inadvertent capture of such entities in the requirement to register as a Dealer. We would encourage the Commissions to provide a meaningful *de minimis* exemption which is consistent with the spirit of the Dodd-Frank Act.

Unintended complications arise when implementing the classifications of MSPs and MSSPs (MSPs and MSSPs together being "Swap Participants"). For instance, a party maintaining a "substantial position" in one or more of the major swap categories will have to separate its security-based swaps from its other swaps and further separate swaps within those two categories in order to determine whether the party is a Swap Participant.[6] One example of the difficulties encountered when categorizing swaps as the Proposed Definition Rule would require, is with respect to credit default swaps ("CDS") referencing a broad index of securities. Although on initial analysis, it seems clear that such an instrument would only be counted toward the test for MSP status, because such an instrument typically settles when there is a credit event with respect to an individual security we are concerned that it conceivably could be construed as a security-based swap counting towards the test for MSSP status.

Various market participants have expressed their concerns to us that separating swaps and security-based swaps into subcategories will be costly and inconsistent with the manner in which participants analyze their swaps and security-based swaps. We urge the Commissions to add an additional definitional test based on overall, uncategorized exposure that will give the majority of market participants a simple benchmark for determining their inclusion or exclusion from the relevant definitions.

Finally, the Committee notes that a substantial number of traditional commodity pools, including most hedge funds, would fail to qualify as eligible contract participants for purposes of over-the-counter foreign currency trading if Rules 1.3(m)(5) and (6) are adopted as proposed. Currency forwards, which are not traded on an exchange, have long been part of trading strategies employed on behalf of commodity pools. The proposing release states that commodity pools would be required to look through all levels of investors to determine whether any *direct or indirect* investor is not an ECP. One indirect non-ECP – no matter how remote – would result in the pool being a non-ECP for purposes of forward foreign currency trading. Publicly offered commodity pools offered to retail investors most certainly would not qualify as ECPs under the

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[6] The need to calculate "substantial exposure" stems from the second of three proposed tests for Swap Participant status, each outlined in the Proposed Definition Rule: (i) an entity that maintains a "substantial position" in a major swap category (citing Section 1a(33)(A)(i) of the Commodities Exchange Act (the "CEA") and Section 3(a)(67)(A)(ii)(I) of the Securities Exchange Act (the "Exchange Act")); (ii) an entity whose outstanding swaps create "substantial counterparty exposure that could have serious adverse affects on the financial stability of the United States banking system or financial markets" (Section 1a(33)(A)(ii) of the CEA and 3(a)(67)(A)(ii)(II) of the Exchange Act); and (iii) a highly leveraged financial entity maintaining a substantial position in a swap category (Section 1a(33)(A)(iii) of the CEA and 3(a)(67)(A)(ii)(III) of the Exchange Act).

rule as proposed. Such a result would disrupt the trading strategies employed by professional advisors on behalf of public and private commodity pools. Moreover, documentation governing FX transactions, some of which has been in place for many years, would have to be revised or replaced.

The Committee appreciates the directive given to the Commissions by Congress mandating additional oversight of off-exchange trading in foreign currency by retail investors. In order not to render large commodity pools non-ECPs, the Committee recommends that the final rule make clear that they are not within the intended scope of the provisions designed to protect retail investors.

III. Proposed End-User Rule

Entities issuing securities under Section 12 of the Exchange Act are required to file reports under Section 15(d) of the Exchange Act to provide a swap data repository or the relevant Commission, as applicable, a statement of whether "an appropriate committee of the board of directors (or equivalent body) has reviewed and approved the decision not to clear the swap or security-based swap."[7] Each of the Commissions, in footnotes to their respective proposing release, has indicated that the board committee could adopt policies and procedures to review and approve decisions not to clear swaps, on a periodic basis or subject to other conditions determined to be satisfactory to the board committee. Because it is generally not practical for any board committee to expressly approve each swap or security-based swap, we believe that the regulators should expressly address the issue of delegation of board authority in final rules. For instance, the final rules might indicate that the board committee may delegate decision making authority not to clear swaps or security-based swaps to officers of the end-user, provided that the transactions meet certain pre-defined parameters (*e.g.*, with respect to the type, size and frequency of a particular transaction). The concept of delegation is consistent with existing corporate law and should be considered to be a permissible activity under the final rules.

IV. Proposed Confirmation Rule

The Proposed Confirmation Rule also mandates in §23.502(a) the reconciliation of swap portfolios between Swap Entities. Section 23.502(a)(5) requires the resolution of discrepancies of more than 10% within one business day. We query how this requirement would operate in the event that it is not possible to resolve such a discrepancy within the mandated one business day time period. We note that, subsequent to the publication of the proposed §23.502(a), a proposal for §23.504(e) was published which clarifies that valuation disputes between Swap Entities existing for more than one business day must be reported to the CFTC.[8] We recommend that §23.502 be conformed so that it is consistent in this respect with §23.504(e).

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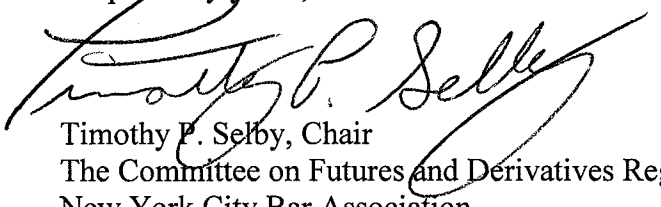
[7] See §39.6(b)(6)(ii).

[8] Swap Trading Relationship Documentation Requirements for Swap Dealers and Major Swap Participants, RIN 3038-AC96.

We appreciate the opportunity to present our views to you on this matter of importance to us as practitioners of derivatives law and regulation and our members are available to discuss any of the above at your convenience.

Respectfully yours,



Timothy P. Selby, Chair
The Committee on Futures and Derivatives Regulation,
New York City Bar Association

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Committee on Futures and Derivatives Regulation
Timothy P. Selby, Chair

Samuel F. Abernethy
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Lauren Ann Teigland-Hunt
Joel Telpner
David Trapani
Sherri Venokur §

Adjunct Members
Richard Miller
Rita Molesworth
Stephen Obie *
Michael Sackheim
Howard Schneider
Lore Steinhauser *

* These members of the Committee did not participate in this comment letter.
§ These members comprise the Ad Hoc Working Group.