



STATE STREET

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February 22, 2011

Via: <http://comments.cftc.gov>

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

**Re: Business Conduct Standards for Swap Dealers and Major Swap Participants  
(RIN 3038-AD25)**

Dear Mr. Stawick:

State Street Corporation (“**State Street**”)<sup>1</sup> appreciates the opportunity to comment on the Commodity Futures Trading Commission’s (the “**Commission**”) proposal (the “**Proposal**”)<sup>2</sup> under Section 731 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“**Dodd-Frank**”) regarding business conduct standards for swap dealers and major swap participants (“**MSPs**”).

Under Dodd-Frank, standardized swaps that are required to be cleared by the Commission must be cleared at a derivatives clearing organization (“**DCO**”) unless an end-user clearing exception applies.<sup>3</sup> All swaps required to be cleared must be traded on a swap execution facility (“**SEF**”) or designated

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<sup>1</sup> With \$21.5 trillion in assets under custody and administration and \$2.0 trillion in assets under management at December 31, 2010, State Street is a leading specialist in meeting the needs of institutional investors worldwide. Our customers include mutual funds, collective investment funds and other investment pools, corporate and public retirement plans, insurance companies, foundations, endowments and investment managers. Including the United States, we operate in 26 countries and more than 100 geographic markets worldwide.

<sup>2</sup> Business Conduct Standards for Swap Dealers and Major Swap Participants With Counterparties, 75 Fed. Reg. 80,638 (the “**Release**”) (proposed December 22, 2010) (amending 17 CFR Pts. 23 and 155).

<sup>3</sup> See Dodd-Frank Section 723.

contract market (“DCM”) if one makes the swap available for trading.<sup>4</sup> The Commission has proposed that swaps executed on a request-for-quote (“RFQ”) basis through a SEF (“RFQ Transactions”) will meet the SEF trading requirement as long as the RFQ facility meets certain minimum standards.<sup>5</sup> As a result, State Street believes that RFQ Transactions should be treated similarly to other SEF transactions for purposes of the Proposal, including by making RFQ Transactions subject to exceptions from certain of the requirements of the Proposal applicable to anonymous SEF transactions as long as the RFQ Transaction is not pre-arranged. In the alternative, the Commission should explicitly permit swap dealers and MSPs to meet certain specific requirements from which anonymized SEF transactions are exempt by relying on standard disclosures made by and representations provided to SEFs, DCOs or their members.

### **I. RFQ Transactions should be treated the same as anonymous SEF transactions for purposes of the Proposal, as long as the swap is not pre-arranged.**

State Street believes that RFQ Transactions should be treated the same as anonymous SEF transactions for purposes of the Proposal, as long as the swap is not pre-arranged. The Proposal exempts swap dealers and MSPs from five sets of requirements (the “SEF Anonymity Provisions”) for swaps entered into on a SEF in which the swap dealer or MSP does not know the identity of the counterparty to the transaction. Under such circumstances, swap dealers and MSPs do not need to:

- verify that their counterparties meet the eligibility standards for an eligible contract participant (“ECP”);<sup>6</sup>
- verify whether their counterparties are “Special Entities;”<sup>7</sup>
- disclose material information about the swap, including information reasonably designed to allow the counterparty to assess material risks of the particular swap;<sup>8</sup>
- meet certain heightened requirements regarding Special Entity counterparties, including that the Special Entity has a qualified independent representative;<sup>9</sup> and

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<sup>4</sup> See *id.* The Commission has started proposing rules related to these requirements. See, e.g., Core Principles and Other Requirements for Swap Execution Facilities, 76 Fed. Reg. 1214 (proposed January 7, 2011) (amending 17 CFR Part 37); End-User Exception to Mandatory Clearing of Swaps, 75 Fed. Reg. 80,747 (proposed December 23, 2010) (amending 17 CFR Part 39); and Process for Review of Swaps for Mandatory Clearing, 75 Fed. Reg. 67,277 (proposed November 2, 2010) (amending 17 CFR Parts 39 and 140).

<sup>5</sup> Core Principles and Other Requirements for Swap Execution Facilities, 76 Fed. Reg. 1214 (proposed January 7, 2011) (amending 17 CFR Part 37). As an example of the minimum requirements, under the Commission’s proposal regarding SEFs, an RFQ system would be required to transmit a request for quote to at least five potential counterparties in the system.

<sup>6</sup> See Proposed Rule 23.430(c).

<sup>7</sup> See *id.* Dodd-Frank creates a separate category of swap counterparties called “Special Entities,” which includes state and local governments, federal agencies, employee benefits plans and government plans under ERISA, and endowments. Dodd-Frank § 731; Commodity Exchange Act § 4S(h)(2)(C).

<sup>8</sup> See Proposed Rule 23.431(b).

<sup>9</sup> See Proposed Rule 23.450(g). In particular, the proposed heightened duties and requirements require swap dealers and MSPs that offer swaps to or enter into swaps with Special Entities to have a reasonable basis to believe that a Special Entity has an independent representative that meets certain criteria, including that the representative (i) has sufficient knowledge to evaluate the transaction and risks; (ii) is not subject to a statutory disqualification; (iii) is independent of the swap dealer or MSP; (iv) undertakes a duty to act in the best interests of the Special Entity it represents; (v) makes appropriate and timely disclosures to the Special Entity; (vi) evaluates, consistent with any guidelines provided by the Special Entity, fair pricing and the (...continued)

- comply with certain prohibitions regarding entering into swaps with municipal entities within two years of making a contribution to an official of the municipal entity.<sup>10</sup>

The Release indicates Congress' and the Commission's rationale for these exceptions: that certain business conduct requirements are only appropriate where "swap dealers and [MSPs] have a pre-trade relationship with their counterparty, where that relationship includes discussions and negotiations that would allow a swap dealer or [MSP] to make appropriate disclosures and conduct due diligence."<sup>11</sup> The Proposal indicates that these requirements "would not apply [to anonymous swap transactions] because there would be no basis on which to make those disclosures or opportunity to engage in discussions."<sup>12</sup> State Street believes that this same rationale applies to RFQ Transactions, so long as the trade is not pre-arranged. RFQ systems are not inherently anonymous; however, RFQ Transactions, like anonymized SEF transactions, are not necessarily characterized by individualized pre-trade relationships for which the full panoply of business conduct protections are necessary or appropriate.

## **II. Alternatively, the Commission should clearly permit swap dealers and MSPs to rely on standard disclosures and representations provided to SEFs or DCOs or their members for RFQ Transactions.**

If the Commission does not treat RFQ Transactions like anonymous SEF transactions, State Street believes swap dealers and MSPs should be able to meet certain of the SEF Anonymity Provisions through reliance on standard disclosures made by, and representations provided to, SEFs, DCOs or their members. These disclosures and representations could be developed either by the Commission or the relevant SEF or DCO.

### *A. Counterparty Eligibility and Special Entity Counterparty Requirements*

Section 2(e) of the Commodity Exchange Act requires non-ECPs to enter into swaps only on designated contract markets and, as a result, prohibits non-ECPs from entering into transactions on SEFs. In addition, Proposed Rule 37.702(a) under the Commission's proposal regarding SEFs would require

(continued...)

appropriateness of the swap; and (vii) in the case of employee benefit plans subject to ERISA, is a fiduciary. In addition, the swap dealer or MSP must determine whether the representative is subject to pay-to-play restrictions, if applicable.

<sup>10</sup> See Proposed Rule 23.451(b)(2)(iii). State Street believes that the Proposal's "know your counterparty," recordkeeping and similar requirements in Proposed Rules 23.402(c) and (d) implicitly would not apply to anonymous SEF transactions and, as a result, also should be considered a SEF Anonymity Provision for purposes of this letter. To the extent that the Commission disagrees, State Street believes that any swap dealer or MSP should be able to meet these two requirements by relying on the fact that the DCM or SEF on which a swap is executed must have this information.

Similarly, State Street believes that implicit in the SEF Anonymity Provisions is the requirement to notify counterparties to swaps that are required to be cleared that they have the sole right to select the DCO for clearing the swap and provide "fair and balanced" communication. See Proposed Rule 23.432(a), 23.433. To the extent that this is not the case, State Street believes that any swap dealer or MSP should be able to meet this requirement by relying on a generic disclosure document created by the Commission, discussed *infra*.

<sup>11</sup> Release at 80,641.

<sup>12</sup> Release at 80,641.

SEFs to ensure that all its members meet the definition of ECP.<sup>13</sup> As a result, requiring a swap dealer or MSP to ensure that its counterparty to an RFQ Transaction is an ECP is redundant. Therefore, State Street believes that the Commission should allow swap dealers and MSPs to rely on a counterparty's membership in a SEF to satisfy its requirement to verify that any counterparty engaging in a RFQ Transaction on that SEF is an ECP.

In addition, State Street believes that the Commission should allow swap dealers and MSPs to reasonably rely on a confirmation from a SEF that it has obtained representations from each of its members as to whether it is or is not a Special Entity and, with respect to any counterparty that is a Special Entity, that it has an independent representative that meets the criteria set forth in the Proposal. Requiring individual swap dealers and MSPs to get such representations will complicate the RFQ trading process and is inefficient in light of the central role SEFs will have in the trading of standardized swaps. In addition, SEF documentation could include a disclosure about the capacity in which swap dealer and MSP counterparties to RFQ Transactions are acting, obviating the need for this disclosure by the swap dealer or MSP under Proposed Rule 23.450(f).

#### *B. Disclosures Regarding Swap Risks and Material Conflicts of Interest*

Proposed Rule 23.431(a)(1) would require swap dealers and MSPs to provide material information concerning swaps to counterparties in a manner reasonably designed to allow the counterparty to assess the material risks of the particular swap. Proposed Rule 23.431(a)(2) would require swap dealers and MSPs to provide material information concerning swaps to counterparties in a manner reasonably designed to allow the counterparty to assess the material characteristics of the particular swap.<sup>14</sup> Both requirements would be excepted by the SEF Anonymity Provisions and, as a result, State Street believes that counterparties to RFQ Transactions should be similarly excepted from them. State Street does not believe that swaps traded on an anonymous basis or through an RFQ facility on the same SEF require differing levels of disclosure to a counterparty.

However, should the Commission choose not to except RFQ Transactions, State Street believes that a swap dealer or MSP should be able to satisfy these requirements by relying fully on standardized documentation. Such documentation could consist of both generic disclosures about swap trading and specific disclosures regarding specific swaps. With respect to generic disclosure, State Street recommends that the Commission develop generic disclosure documents similar to the generic disclosure documents used for futures, options and retail foreign currency transactions, as mentioned in the Proposal.<sup>15</sup> More specific disclosure should be provided by the DCO clearing the swap.

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<sup>13</sup> Core Principles and Other Requirements for Swap Execution Facilities, 76 Fed. Reg. 1214 (proposed January 7, 2011) (amending 17 CFR Part 37).

<sup>14</sup> This includes the material economic terms of the swap, the terms relating to the operation of the swap and the rights and obligations of the parties during the terms of the swap.

<sup>15</sup> See Release at 80,644.

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We would be happy to discuss the foregoing at your convenience.

Sincerely,

A handwritten signature in cursive script, appearing to read "David C. Phelan".

David C. Phelan

cc: Jeffrey N. Carp, State Street Corporation, EVP and Chief Legal Officer  
Stefan M. Gavell, State Street Corporation, EVP and Head of  
Regulatory, Industry and Government Affairs