BLACKROCK

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<u>Via electronic submission</u>

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Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, DC 20581

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

Re: **RIN 3038-AD06 / RIN 3235–AK65 / File No. S7–39–10**

Further Definition of "Swap Dealer," "Security-Based Swap Dealer," "Major Swap Participant," "Major Security-Based Swap Participant" and "Eligible Contract Participant" (75 Fed. Reg. 80,174)

Dear Mr. Stawick and Ms. Murphy:

The Commodity Futures Trading Commission ("CFTC") and the Securities and Exchange Commission ("SEC") (collectively, the "Commissions") have requested public comment on certain key definitions in Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank" or the "Act"), *see* Further Definition of "Swap Dealer," "Security-Based Swap Dealer," "Major Swap Participant," "Major Security-Based Swap Participant" and "Eligible Contract Participant," 75 Fed. Reg. 80,174 (Dec. 21, 2010). BlackRock is pleased to be given this opportunity to address these issues of importance to the financial markets and to our business operations.

BlackRock, Inc. is one of the world's leading asset management firms, managing approximately $3.54 trillion on behalf of institutional and individual clients worldwide through a variety of equity, fixed income, cash management, alternative investment, real estate and advisory products. Our client base includes corporate, public, multi-employer pension plans, insurance companies, third-party mutual funds, endowments, foundations, charities, corporations, official institutions, banks, and individuals around the world.

We offer to our clients a range of investment products through separate accounts as well as directly and indirectly through a variety of pooled investment vehicles that are established as separate and distinct legal entities, including without limitation open-end and closed-end mutual funds, exchange-traded funds, collective investment trusts and hedge funds (collectively referred to as "funds"). These funds and separate accounts use a variety of different types of swaps to manage risk and deliver return in most product categories.

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* * * *

We support the Commissions' efforts to monitor systemically important swap users and to ensure that the counterparty credit risk associated with a person's swap or security-based swap ("SBS") positions does not threaten the U.S. financial markets. Our comments primarily address the proposed definitions of Major Swap Participant ("MSP"), Major Security-Based Swap Participant ("MSSP" and, together with MSPs, "Major Participants"), Swap Dealer ("SD") and Security-Based Swap Dealer ("SBSD" and, together with SDs, "Dealers"). We also offer comments on the time frame for registration as well as the sequencing of the Commissions' rulemaking process. We hope the Commissions find that our comments are consistent with the letter and spirit of Dodd-Frank and our intention to contribute to a streamlined, effective and sustainable regulatory framework.

Comments on the Major Participant Definitions

Dodd-Frank defines Major Participants based upon their outstanding swap positions. By statute, Major Participants are those entities that are not Dealers but who maintain substantial positions in swaps or SBS that could cause systemic risk. A person who qualifies as a Major Participant will be regulated more stringently than other buy-side market participants. That person will need to register with the CFTC or SEC, as appropriate, and comply with regulation

intended by Congress to prevent systemic risk, including minimum capital and margin requirements.[1]

1. Systemic Risk Should be Determinative of Major Participant Status

The goal of Major Participant regulation is to prevent systemic risk by regulating entities whose swap positions create systemically important credit risk. Early in the legislative process, Treasury Secretary Timothy Geithner wrote that OTC derivatives dealers, as well as "all other firms whose activities in [OTC derivatives] markets create large exposures to counterparties should be subject to a robust and appropriate regime of prudential supervision and regulation." *See* Letter from Timothy F. Geithner, U.S. Treasury Secretary, to Harry Reid, U.S. Senator (May 13, 2009), http://www.treasury.gov/initiatives/Documents/OTCletter.pdf. The Commissions have incorporated this concept into their rulemaking process. They state that the "major participant definitions apply to the entities that actually 'maintain' substantial positions in swaps and security-based swaps or that have swaps or security-based swaps that create substantial counterparty exposure." 75 Fed. Reg. at 80,201.

A. Asset Managers are not Major Participants

We commend the Commissions for confirming that asset managers that do not enter into swaps for their own accounts are not Major Participants. *See* 75 Fed. Reg. at 80,201. Asset managers invest money for clients, typically in funds or separate accounts. The advised fund or account bears the credit risk associated with any swap positions it holds. In the unlikely event that a fund or account defaults, counterparties do not have recourse to the assets of the asset manager. The Commissions have determined rightly that asset managers are not Major Participants based on the swap positions of the funds and accounts they advise.

However, some ambiguity is introduced by the Commissions' suggestion that aggregation of swap positions among affiliated entities may be appropriate in certain circumstances, such as parent/subsidiary relationships and guaranty arrangements. The Commissions have requested comment on issues that would be raised if, for example, market participants were required to aggregate swap positions. *See* 75 Fed. Reg. 80,201-02. At least with respect to swap positions held in funds or accounts advised by the same asset manager, we believe that aggregation should not be required.

The Major Participant definitions refer to "any person," a term that connotes individual entities, such as trusts and investment funds, without encompassing all entities in such person's "family tree." Dodd-Frank's legislative history also suggests that it would be inappropriate to aggregate the swap positions held in funds or accounts advised by the same asset manager. Senator Kay Hagan asked Senator Blanche Lincoln: "When considering whether an entity maintains a substantial position in swaps, should the CFTC and the SEC look at the aggregate positions of funds managed by asset managers or at the individual fund level?" Senator Lincoln replied that "[a]s a general rule, the CFTC and the SEC should look at each entity on an

[1] For ease of reference for the reader, we have reprinted in an appendix attached to this letter the full text of the statutory provisions of Dodd-Frank which we cite in this letter.

individual basis when determining its status as a major swap participant." 156 Cong. Rec. S5907 (daily ed. July 15, 2010). We strongly recommend that the Commissions adopt in their final rules the position contained in Senator Lincoln's reply to Senator Hagan.

B. The Major Participant Determination Should Look to who Bears the Credit Risk of a Swap Position

The Commissions intend that the Major Participant determination will "focus on the entity that enters into swaps or security-based swaps." *See* 75 Fed. Reg. 80,201. Yet they also state that "all of the managed positions of which a person is the beneficial owner are to be aggregated...for purposes of determining whether such beneficial owner is a major participant." *See* 75 Fed. Reg. at 80,201. This statement raises potential issues and requires clarification with respect to funds and separate accounts.

i. *Funds*

In the context of a fund, the beneficial owner of a swap position should be the fund itself, not each of the individual investors that contribute to or own interests in the fund. Funds are legally distinct entities that, in the words of the statute, "maintain" positions and assume directly the credit risks associated with those positions. If a fund defaults on a swap position, counterparties have recourse to the assets of the fund only. Requiring funds to allocate swap positions to their individual investors would be inconsistent with the Commissions' desire to determine Major Participant status based on counterparty credit risk.

Implementing a Major Participant standard that deems individual investors to be "beneficial owners" of a fund's swap positions would require continuous reporting of fund swap positions to fund investors, which would be unfeasible. As a practical matter, investors in many funds change on a daily basis and asset managers may not know all of a fund's interest holders. The Commissions should confirm in their final rules that they do not intend fund investors to be considered the "persons" who "maintain" swap positions for purposes of the Major Participant definitions.

ii. Separate Accounts

Separate accounts are different. In contrast to funds, separate account clients retain an asset manager to manage a sum of money exclusively for the client. In this case, an individual investor owns the investment positions of a particular account and bears directly the credit risk associated with those positions. We understand the Commissions' reference to beneficial ownership to require that separate account swap positions be attributed to the owner of the separate account. This result would be consistent with the language of the Major Participant definitions, which focus on the "person" whose swap positions create credit risk.

The Commissions are silent on whether they intend a "beneficial owner" regulatory framework under which the owners of accounts will work out compliance arrangements with their asset managers. Such arrangements, however, would appear to be necessary if account owners will rely on asset managers to assist in compliance. Clients may establish separate accounts with multiple asset managers and a manager does not know, and has no ability to learn, the positions in each account. In fact, clients likely prefer that the managers who advise their

separate accounts not communicate with each other about those accounts. Therefore the Commissions should specify that the beneficial owner of a separate account is responsible for its compliance with Major Participant regulation, and may obtain assistance from its asset manager to ensure such compliance.

2. Concerns with the Major Participant Thresholds

In our response to the Commissions' Advance Notice of Proposed Rulemaking on the Major Participant definitions, we urged the Commissions to set the thresholds for designation as a Major Participant at a systemically significant level, based on clear objective criteria that account for factors impacting the credit risk level of swaps. *See* Letter from Joanne Medero, BlackRock, to the Commissions (Sep. 20, 2010), http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=26201&SearchText= ("BlackRock ANPR Letter"). In our view, the proposed rules fall short in each of these categories.

A. The Commissions Should Reconsider the Major Participant Thresholds

The purpose of Major Participant regulation is to prevent the counterparty credit exposure of a single person from causing a financial meltdown and threatening the integrity of the financial system of the United States. As a buy-side entity, a Major Participant would create systemic risk if its swap positions were so large that a default by the Major Participant would cause the collapse of one or more systemically important Dealers. A market participant whose swap or SBS positions could not lead to this result should not, according to Dodd-Frank, be considered a Major Participant.

To help determine which entities should be Major Participants, Congress directed the Commissions to establish two thresholds. One threshold, used in the first and third prong of the Major Participant definition, considers whether a person has a "substantial position" in any major category of swap or SBS. The other threshold, used in the second prong of the Major Participant definition, is based on the entirety of a person's swap portfolio. In either case, the statute requires the positions to be systemically significant.

To set thresholds appropriately, the Commissions should analyze available transaction data from the relevant swap markets and determine the size of swap positions that could create systemic risk. If sufficient information is not available for the Commissions to set thresholds, the Commissions should refrain from establishing thresholds until they have gathered enough information to set appropriate cutoffs. If the Commissions believe such data is available, they should share it with the public and explain the process they used to set the thresholds so that the public may comment on the Commissions' methodology. The Commissions, however, have taken a different approach and have proposed thresholds that could, in our view, require many entities who have sizeable swap positions, but whose default would not create systemic risk, to register as Major Participants. As a result, we believe these thresholds are too low.

i. Prong One – Substantial Position

The "first prong" of the Major Participant definitions requires any person who maintains a "substantial position in swaps for any of the major swap categories" to register as a Major

Participant.[2] For purposes of determining whether a person maintains a "substantial position" in swaps or SBS, the Commissions have proposed the following thresholds:

- Rate swaps (CFTC):
  - $3 billion in daily average aggregate uncollateralized outward exposure; or
  - $6 billion in daily average uncollateralized outward exposure plus daily average aggregate potential outward exposure. *See* Proposed Rule 1.3(1)(sss)(i).

- All other swaps (CFTC) and SBS (SEC):
  - $1 billion in daily average aggregate uncollateralized outward exposure; or
  - $2 billion in daily average aggregate uncollateralized outward exposure plus daily average aggregate potential outward exposure. *See* Proposed Rules 1.3(1)(sss)(ii-iv) (CFTC) and 240.3a67-3(b) (SEC).

In our view, the Commissions have not, as Dodd-Frank requires, made a finding that the proposed thresholds are at the level that would be "prudent for the effective monitoring, management, and oversight of entities that are *systemically important or can significantly impact the financial system of the United States*." Dodd-Frank §§ 721 (New CEA § 1a(33)(B)) and 761(a)(6) (New Exchange Act § 3(a)(67)(B)) (emphasis added). Put another way, the Commissions have not explained why the thresholds they have selected would render a person "systemically important" or significant to the entire "financial system of the United States."

The thresholds proposed by the Commissions appear to use the Tier 1 capital levels of major dealer banks as a proxy for the ability of the financial system to absorb losses associated with the default of a market participant. *See* 75 Fed. Reg. at 80,190 n.104 (observing that Tier 1 capital levels of the six U.S. banks most active in credit derivative dealing activity ranges from $14 billion to $113 billion). However, the Commissions concede that the proposed thresholds are materially below the level at which a single-party default would cause significant losses to the financial system because failures of multiple market participants may occur close in time. *See* 75 Fed. Reg. at 80,190.

These considerations may be relevant to determining whether a particular threshold is "prudent for the effective monitoring, management, and oversight of entities that are systemically important or can significantly impact the financial system of the United States," but the release does not provide sufficient detail about the Commissions' methodology to allow informed comment on their determination. We respectfully request that, before the Commissions adopt final rules, they provide the public greater insight into the information used when proposing the "substantial position" thresholds. We would welcome the opportunity to provide comment on the basis of the Commissions' reasoning.

In addition, our experience as an advisor to funds and other swap market participants suggests that the proposed thresholds are too low. Instead of targeting systemically important firms, these thresholds will capture entities that pose little or no systemic risk and subject them to

[2] The "third prong" of the major participant definition also requires an entity to maintain a "substantial position" in swaps or SBS.

burdensome and costly regulation. To avoid that outcome, market participants may reduce or eliminate their use of swaps to hedge and may hold more risk in their portfolios. Congress did not intend this result and the Commissions should not require it. We share the Commissions' desire to protect the financial system, but believe higher thresholds would not create systemic risk.

ii. Prong Two – Substantial Counterparty Exposure

The "second prong" of the Major Participant definition also seeks to prevent systemic risk; it would apply only to entities "whose outstanding swaps create substantial counterparty exposure that could have serious adverse effects on the *financial stability of the United States banking system or financial markets*." Dodd-Frank §§ 721 (New CEA § 1a(33)(A)(ii)) and 761(a)(6) (New Exchange Act § 3(a)(67)(A)(ii)) (emphasis added). In other words, prong two, like prong one, requires a person's swap positions to pose systemic risk for that person to be characterized as a Major Participant. Prong two, however, accounts for all swap positions in a person's portfolio, regardless of the purpose of the positions or the status of the entity. Under the second prong of the major participant test, the Commissions propose the following thresholds:

CFTC:
- $5 billion in daily average aggregate uncollateralized outward exposure; or
- $8 billion in the sum of daily average aggregate uncollateralized outward exposure plus daily average aggregate potential outward exposure. *See* Proposed Rule 1.3(uuu).

SEC:
- $2 billion in daily average aggregate uncollateralized outward exposure (as defined above); or
- $4 billion in the sum of daily average aggregate uncollateralized outward exposure plus daily average aggregate potential outward exposure. *See* Proposed Rule 240.3a67-5.

We believe the proposed thresholds for the "substantial counterparty exposure" test are similarly too low. They could encompass many market participants, including employee benefit plans and commercial end users, that do not have systemically important swap positions. To prevent this result and the costs associated with it, the Commissions should increase these thresholds.

B. The Commissions Should Clarify how the Thresholds for Outward Exposure will Function

We support the Commissions' decision to use numerical thresholds as one criterion for Major Participant designation. If defined clearly and applied uniformly, such thresholds would contribute to certainty and stability in the swap markets by allowing market participants to readily evaluate their regulatory status. Without guidelines for how parties should value exposure and collateral, however, the opposite result is likely, because market participants will lack certainty about their regulatory status. This could disrupt swap trading in the bilateral swap market.

The proposed rules do not prescribe any particular methodologies for valuing current exposure or posted collateral. Instead, the Commissions advise market participants to use valuation methods that are "consistent with counterparty practices and industry practices generally." 75 Fed. Reg. at 80,189. We appreciate the Commissions' desire to allow market participants flexibility in calculating their exposure. The variety of market participants who use swaps suggests that market participants should have discretion to choose a valuation method suitable to their business.

Nonetheless, the Commissions should approve explicitly one or more methods for calculating exposure and collateral. Such safe harbors are necessary because valuation practices vary widely among industries and counterparties. Market participants need to know that if they use, for example, methodology "X" to calculate their market exposure and that exposure is less than the thresholds ultimately adopted, they will not be Major Participants and their methodology will not be subject to regulatory second-guessing.

C. The Proposed Thresholds Fail to Consider the Reduced Systemic Risk that Results from a Person Entering into Swaps with Multiple Counterparties

We support the Commissions' aim to account for the many factors affecting the risk-profile of a particular swap portfolio. For example, as Congress intended, the Commissions have accounted for the fact that fully collateralized or cleared swaps create less counterparty credit risk than uncollateralized, uncleared swaps. *See* Dodd-Frank §§ 721(a)(16) (New CEA § 1a(33)(B)) and 761(a)(16) (New Exchange Act § 3(a)(67)(B)).[3] The Commissions also have taken into account future exposure as well as current exposure.

However, the thresholds do not consider one critical aspect of systemic risk: concentration of positions. Although the Commissions offer no explanation for how they arrived at their proposed thresholds for "substantial position" and "substantial counterparty exposure," they imply that the thresholds are set below a level that would cause a single Dealer to fail if the Major Participant were to default. Thresholds set in this manner do not account for the fact that if a party enters into swaps with multiple dealers, the risk of a default by that person sparking systemic risk by causing the failure of a single Dealer is reduced.

In their release, the Commissions note that they considered the potential for reduced systemic risk that results from dispersing credit risk to multiple counterparties, but they suggest that having many counterparties might also make a person's swap positions more systemically important because the person would be highly interconnected. *See* 75 Fed. Reg. at 80,188. This would be true only if the magnitude of a person's swap positions are such that a failure by that person would cause multiple counterparties to fail. Otherwise, exposure that could cause one counterparty to fail would be dispersed to multiple counterparties and all would survive.

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[3] *See also* 156 Cong. Rec. S5907 (daily ed. July 15, 2010) (quoting Senator Lincoln: "[W]here a person has uncleared swaps, the regulator should consider the value and quality of such collateral when defining 'substantial position.' Bilateral collateralization and proper segregation substantially reduces the potential for adverse effects on the stability of the market. Entities that are not excessively leveraged and have taken the necessary steps to segregate and fully collateralize swap positions on a bilateral basis with their counterparties should be viewed differently.").

A more nuanced test of Major Participant status would be to use the thresholds as a safe harbor. A market participant whose exposure falls below a threshold would not be a Major Participant. If the person's exposure equals or exceeds a threshold, the person would be a Major Participant only if, after considering other factors, either the CFTC or SEC determines the positions could create systemic risk. When making this second-level determination, the Commissions should consider, among other things, whether the person's swap positions are maintained with diverse counterparties, whether any swap positions in correlated commodities offset each other, and whether the positions are used as hedges or to take a market view.[4]

3. <u>The Exclusion for Employee Benefit Plan Positions Requires Further Clarification</u>

Swap positions "maintained by any employee benefit plan (or any contract held by such a plan) as defined in paragraphs (3) and (32) of section 3 of [ERISA] for the primary purpose of hedging or mitigating any risk directly associated with the operation of the plan" are excluded from the "substantial position" threshold in the first prong of the Major Participant definitions. *See* Dodd-Frank §§ 721(a)(16) (New CEA § 1a(33)(A)(i)(II)) and 761(a)(6) (New Exchange Act § 3(a)(67)(A)(ii)(I)). The CFTC and SEC restate these exclusions in Proposed Rules 1.3(qqq)(1)(ii)(A) and 240.3a67-1(a)(2)(i), respectively, but do not provide additional information about the exclusions' scope. Instead, the Commissions state that they "do not believe that it is necessary to propose a rule to further define the scope of this exclusion." 75 Fed. Reg. at 80,201. We respectfully disagree with the Commissions' conclusion and suggest the following areas for clarification.

A. The Phrase "Hedging or Mitigating" Should be Defined Broadly

In the context of the exclusion for positions held to reduce commercial risk, the Commissions have properly interpreted "hedging or mitigating" to include activities that extend beyond positions recognized as hedges for accounting purposes.[5] The Commissions should confirm that "hedging or mitigating" will enjoy the same broad interpretation in the context of the plan exclusion. This would be consistent with principles of statutory interpretation, which require that when a statute uses the same term multiple times, the term be given the same meaning each time it appears. *See, e.g., Gustafson v. Alloyd Co.*, 513 U.S. 561, 570 (1995).

In addition, the Commissions should confirm that the express statutory language defining the scope of the plan exclusion itself is broader than the commercial risk exclusion. Specifically, the commercial risk exclusion applies only to "positions held for hedging or mitigating commercial risk," while the plan exclusion applies to positions held for "the *primary purpose* of hedging or mitigating any risk directly associated with the operation of the plan." Dodd-Frank §§ 721(a)(16) (New CEA § 1a(33)(A)(i)) and 761(a)(6) (New Exchange Act § 3(a)(67)A)(ii)) (emphasis added). The Commissions should give full effect to the "primary purpose" language,

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[4] For additional details on the factors the Commissions should consider, *see* BlackRock ANPR Letter at 10-11.

[5] The CFTC also believes "hedging or mitigating" includes positions that would not be considered bona fide hedging for purposes of an exemption from position limits under the CEA. *See* 75 Fed. Reg. at 80,195.

which suggests plans may exclude swap positions even if they serve a purpose in addition to hedging or mitigating.

B. The Commissions Should Explain Which Positions are "Maintained" by a Plan

Dodd-Frank's legislative history shows that Congress intended Dodd-Frank would "avoid doing any harm to pension plan beneficiaries." 156 Cong. Rec. S5906 (daily ed. July 15, 2010) (quoting Sen. Lincoln). The plan exclusion – one of very few exclusions in Dodd-Frank – is one way of achieving this goal. However, the statute does not specify what positions are considered to be "maintained" by a plan. If the Commissions fail to clarify this language, plans may not know whether their positions qualify for the exclusion. Uncertainty could prevent plans from entering into swap transactions to hedge their risks, which could endanger investment returns and create more risk to the financial system.

ERISA requires that plan assets be held in trust. The trust enters into transactions, including swap transactions, on behalf of a plan. Plan fiduciaries often invest plan assets in pooled investment vehicles such as registered investment companies, private funds and bank maintained collective trust funds (collectively, "pooled funds"). Pooling assets utilizes economies of scale and other efficiencies to reduce investment costs and increase plan returns, but the assets are still held in trust on behalf of a plan.

The Commissions should clarify that the swap and SBS positions held by pooled funds that are established and regulated to hold ERISA plan assets, will receive the benefit of the plan exclusion. Otherwise, the Commissions will be limiting the ability of plans to pool assets and avail themselves of the efficiencies such pooling provides. This would harm plan beneficiaries and undermine the intent of Congress.

4. Legacy Portfolios in Run-off Mode Should not be Major Participants

The Commissions have requested comment on whether certain entities that maintain legacy portfolios of credit default swaps but are not entering into additional swaps or SBS should be excluded from the Major Participant definitions. We note, however, that the Commissions refer only to monoline insurance activities and credit derivative product companies. There are other types of entities with large legacy portfolios, now strictly in run-off, of credit default swaps and other types of swaps or SBS and who have no other ongoing business activities other than managing the run-off and orderly liquidation of those legacy positions and other amortizing assets. Such entities include, but are not limited to, special purpose vehicles formed in connection with the restructuring of problem portfolios resulting from the financial crisis.

We are of the view that all such "legacy portfolio" entities should be exempt from regulation as Major Participants. They may be unable to comply with capital and margin requirements and many of the other proposed compliance requirements would be either irrelevant to or unfeasible for a liquidating portfolio. Moreover, because the portfolios of such entities, albeit substantial, are in run-off mode, submitting them to such regulation would not appear to serve any significant regulatory or policy objective, but, particularly to the extent they are unable to comply, could adversely (and in some cases materially) affect the expectations of their investors, counterparties

and other creditors, such as by potentially subjecting the legacy portfolio entities to penalties or triggering defaults or termination events in their legacy portfolios.

We request that such an exclusion also clarify that any of the following, if entered into by a legacy portfolio entity, would be considered part of the legacy portfolio, and not new transactions: (i) novations from one counterparty to another, where the legacy portfolio entity is the remaining party; (ii) amendments of legacy swaps or SBS, and (iii) swaps or SBS to hedge existing exposures in the legacy portfolios. The need for such novations or for amendments frequently can arise in the ordinary course of the administration of such portfolios and in some cases could be required by credit covenants or other document requirements. Finally, we agree with the suggestion of the Commissions that such excluded entities be required to provide the Commissions with position information of the type that registered Major Participants would be required to provide, with such conforming changes as may be appropriate.

5. The Commissions Should Provide Greater Time for Registration Once a Person Qualifies as a Major Participant

Under the proposed rules, a person must register as a Major Participant within two months after the end of the fiscal quarter in which its swaps activities exceed the Commissions' thresholds. *See* Proposed Rule 1.3(qqq)(2). The Commissions seek comment as to whether this is an adequate amount of time to complete the registration application. We submit that it is not.

The proposed timeline overlooks the fact that complying with Major Participant regulation could require significant business adjustments. So far the Commissions have proposed some, but not all, of the substantive requirements to which Major Participants will have to adhere. A Major Participant that is a fund, for example, would have to follow new procedures for entering into swaps. Developing and implementing these procedures may take substantially longer than two months.

It may take Major Participants that are funds even longer to comply with Major Participant regulation if the Commissions do not clarify certain aspects of their proposals. For example, rules proposed by the CFTC would mandate, among other things, that every MSP establish a "risk management unit." *See* Business Conduct Standards for Swap Dealers and Major Swap Participants With Counterparties, 75 Fed. Reg. 80,638 (Dec. 22, 2010). Many funds are not divided into business units and some do not employ any staff. Instead, funds rely on their asset managers to provide a range of compliance and risk management services. The Commissions' proposed rules do not make clear, as they should, that funds that are Major Participants will be able to rely on their asset managers or others for these services. If the Commissions do not allow funds to rely on their asset managers for services related to compliance with Major Participant requirements, funds would need enough time to reconfigure their business operations to meet Commission standards, if they could do so at all. We respectfully request that the Commissions provide 8 months for market participants to complete the registration process and come into compliance with applicable rules.

Comments on Dealer Definitions

Dodd-Frank also regulates Dealers—the primary liquidity providers to the swap and SBS markets. Under Dodd-Frank, a person who "(i) holds itself out as a dealer in swaps [or SBS]; (ii) makes a market in swaps [or SBS]; (iii) regularly enters into swaps [or SBS] with counterparties as an ordinary course of business for its own account; or (iv) engages in any activity causing the person to be commonly known in the trade as a dealer or market maker in swaps [or SBS]" must register and be regulated as a Dealer. Dodd-Frank §§ 721(a)(21) (New CEA § 1a(49)) (for swap dealers) and 761(a)(21) (New Exchange Act § 3(a)(71)) (for security-based swap dealers).[6] Dodd-Frank excludes from the definition of a Dealer "a person who enters into swaps [or SBS] for such person's own account, either individually or in a fiduciary capacity, but not as part of a regular business." Dodd-Frank §§ 721 (New CEA § 1a(49)(C)) and 761 (New Exchange Act 3(a)(71)(C)).

For the same reason that asset managers are not Major Participants, they also will not qualify as Dealers. Asset managers do not enter into swaps for their own accounts but instead advise other entities and accounts on a range of financial matters. The status of funds, however, is less clear. There should be no question that a fund would not meet parts (i), (ii) or (iv) of the SD definition as funds do not hold themselves out as dealers or market makers in swaps or SBS. Part (iii) of the Dealer definition, however, could be construed to apply to funds, because funds do enter into swaps with counterparties for their own accounts.

The Commissions state that persons who enter into swaps as part of a "regular business" would be "those persons whose function is to accommodate demand for swaps from other parties and enter into swaps in response to interest expressed by other parties. Conversely, persons who do not fulfill this function should not be deemed to enter into swaps as part of a 'regular business' and are not likely to be swap dealers." 75 Fed. Reg. at 80,177. Funds are not in the business of making markets in swaps or engaging in other types of dealing activities. Funds use swaps to hedge their investment positions and to take a directional view of particular markets. The Commissions should clarify that funds that use swaps for these purposes are not entering into swaps "as part of a regular business" and are not SDs or SBSDs.

Comment on the Sequence of Rulemaking

We are mindful of the heavy regulatory burden Dodd-Frank imposes on the Commissions and appreciate the challenges faced by the Commissions in implementing Dodd-Frank. But the sequence in which the Commissions, particularly the CFTC, have approached the Major Participant and Dealer rulemakings has not provided all interested parties with adequate notice of the substance of the proposals.[7] In this regard, we share the concerns expressed in the letter filed on January 18, 2011 by the Asset Management Group of SIFMA. *See* Letter from Timothy W. Cameron, Asset Management Group, to the CFTC (Jan. 18, 2011), http://comments.

6 The Dealer definitions are reproduced in the appendix to this letter.

7 Seven months into the rulemaking process, the CFTC has proposed dozens of regulations to regulate the swap market. The CFTC has not, however, proposed a definition for the term "swap."

cftc.gov/PublicComments/ViewComment.aspx?id=27177&SearchText=. To ensure that all interested market participants have the opportunity to meaningfully comment on the substantive Major Participant and Dealer regulations, we respectfully urge the Commissions to reopen or, as appropriate, extend all comment periods on proposed substantive regulations for Major Participants and Dealers for 60 days after the Commissions adopt final definitions for these market participants.

Conclusion

BlackRock supports the Commissions' efforts to mitigate systemic risk through regulatory oversight of those entities whose use of swaps and SBS could threaten the financial integrity of the United States. Implementing Dodd-Frank effectively will help prevent future financial crises and lead to more stable and prosperous financial markets.

We support many aspects of the Commissions' proposed definitions of Major Participants and Dealers. For example, the Commissions' decision to focus the Major Participant inquiry on the entity creating credit risk is both appropriate and consistent with Dodd-Frank. We appreciate the Commissions' discussion of asset managers and decision not to consider asset managers to be Major Participants based on the swaps activities of the funds and accounts they advise. We also support the Commissions' decision to propose numerical thresholds for purposes of determining "substantial position" and "substantial counterparty exposure."

Other areas of the proposed rules would benefit from further consideration. The proposed Major Participant definitions will subject to regulation entities that have large, but not systemically important, swap and SBS positions. If adopted in their current form, these definitions would force these entities to choose between curtailing their swap activity, potentially at the expense of their clients or business, and complying with a costly new compliance regime.

The lack of certainty surrounding many aspects of the proposed rules adds to our concerns. We urge the Commissions to refine their proposals to provide safe harbors so that market participants will know they can rely on certain methodologies to value their swap or SBS exposure. In addition, the Commissions should speak directly to the employee benefit plan exclusion in the Major Participant definitions so that these important market participants will know the parameters of the exemption provided to them by Congress. Similarly, the Commissions should provide additional guidance on the applicability of the third prong of the Dealer definitions. Regulatory certainty will promote the development of liquid, deep and efficient swap markets. The Commissions should do all they can to encourage this result.

Lastly, the Commissions should ensure that the Major Participant and Dealer rulemaking processes are conducted in a transparent and fair manner that gives all interested parties ample opportunity to comment. The Major Participant and Dealer definitions should have been released before any proposed rules governing these new swap market participants. Although the Commissions have chosen to proceed differently, they should reopen or extend comment periods on any substantive Market Participant or Dealer proposed rules for another 60 days.

We appreciate the opportunity to comment on these proposals. If you have any questions or would like further information, please do not hesitate to contact me.

Sincerely,

Joanne Medero

Appendix: Definition of Major Swap Participant, Major Security-Based Swap Participant, Swap Dealer and Major Security-Based Swap Dealer

1. Major Swap Participant (Dodd-Frank Section 721(a)(16), New CEA § 1a(33))

2. Major Security-Based Swap Participant (Dodd-Frank Section 761(a)(6), New Exchange Act § 3(a)(67))

3. Swap Dealer (Dodd-Frank § 721(a)(19), New CEA § 1a(49)(C))

4. Security-Based Swap Dealer (Dodd-Frank § 761(a)(6), New Exchange Act 3(a)(71)(C))

Appendix A – Definition of Major Swap Participant and Major Security-Based Swap Participant

1. Major Swap Participant (Dodd-Frank Section 721(a)(16), New CEA § 1a(33)):

MAJOR SWAP PARTICIPANT.—

(A) IN GENERAL.—The term 'major swap participant' means any person who is not a swap dealer, and—

(i) maintains a substantial position in swaps for any of the major swap categories as determined by the Commission, excluding—

(I) positions held for hedging or mitigating commercial risk; and

(II) positions maintained by any employee benefit plan (or any contract held by such a plan) as defined in paragraphs (3) and (32) of section 3 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1002) for the primary purpose of hedging or mitigating any risk directly associated with the operation of the plan;

(ii) whose outstanding swaps create substantial counterparty exposure that could have serious adverse effects on the financial stability of the United States banking system or financial markets; or

(iii) (I) is a financial entity that is highly leveraged relative to the amount of capital it holds and that is not subject to capital requirements established by an appropriate Federal banking agency; and

(II) maintains a substantial position in outstanding swaps in any major swap category as determined by the Commission.

(B) DEFINITION OF SUBSTANTIAL POSITION.—For purposes of subparagraph (A), the Commission shall define by rule or regulation the term 'substantial position' at the threshold that the Commission determines to be prudent for the effective monitoring, management, and oversight of entities that are systemically important or can significantly impact the financial system of the United States. In setting the definition under this subparagraph, the Commission shall consider the person's relative position in uncleared as opposed to cleared swaps and may take into consideration the value and quality of collateral held against counterparty exposures.

(C) SCOPE OF DESIGNATION.—For purposes of subparagraph (A), a person may be designated as a major swap participant for 1 or more categories of swaps without being classified as a major swap participant for all classes of swaps.

(D) EXCLUSIONS.—The definition under this paragraph shall not include an entity whose primary business is providing financing, and uses derivatives for the purpose of hedging underlying commercial risks related to interest rate and foreign currency exposures, 90 percent or more of which arise from financing that facilitates the purchase or lease of products, 90 percent or more of which are manufactured by the parent company or another subsidiary of the parent company.

2. **Major Security-Based Swap Participant (Dodd-Frank Section 761(a)(6), New Exchange Act § 3(a)(67)):**

MAJOR SECURITY-BASED SWAP PARTICIPANT.—

(A) IN GENERAL.—The term 'major security-based swap participant' means any person—

(i) who is not a security-based swap dealer; and

(ii)(I) who maintains a substantial position in security-based swaps for any of the major security-based swap categories, as such categories are determined by the Commission, excluding both positions held for hedging or mitigating commercial risk and positions maintained by any employee benefit plan (or any contract held by such a plan) as defined in paragraphs (3) and (32) of section 3 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1002) for the primary purpose of hedging or mitigating any risk directly associated with the operation of the plan;

(II) whose outstanding security-based swaps create substantial counterparty exposure that could have serious adverse effects on the financial stability of the United States banking system or financial markets; or

(III) that is a financial entity that—

(aa) is highly leveraged relative to the amount of capital such entity holds and that is not subject to capital requirements established by an appropriate Federal banking agency; and

(bb) maintains a substantial position in outstanding security-based swaps in any major security-based swap category, as such categories are determined by the Commission.

(B) DEFINITION OF SUBSTANTIAL POSITION.—For purposes of subparagraph (A), the Commission shall define, by rule or regulation, the term 'substantial position' at the threshold that the Commission determines to be

prudent for the effective monitoring, management, and oversight of entities that are systemically important or can significantly impact the financial system of the United States. In setting the definition under this subparagraph, the Commission shall consider the person's relative position in uncleared as opposed to cleared security-based swaps and may take into consideration the value and quality of collateral held against counterparty exposures.

(C) SCOPE OF DESIGNATION.—For purposes of subparagraph (A), a person may be designated as a major security- based swap participant for 1 or more categories of security-based swaps without being classified as a major security-based swap participant for all classes of security-based swaps.

3. **Swap Dealer (Dodd-Frank § 721(a)(19), New CEA § 1a(49)(C)):**

SWAP DEALER.—

(A) IN GENERAL.—The term 'swap dealer' means any person who—

(i) holds itself out as a dealer in swaps;

(ii) makes a market in swaps;

(iii) regularly enters into swaps with counterparties as an ordinary course of business for its own account; or

(iv) engages in any activity causing the person to be commonly known in the trade as a dealer or market maker in swaps,

provided however, in no event shall an insured depository institution be considered to be a swap dealer to the extent it offers to enter into a swap with a customer in connection with originating a loan with that customer.

(B) INCLUSION.—A person may be designated as a swap dealer for a single type or single class or category of swap or activities and considered not to be a swap dealer for other types, classes, or categories of swaps or activities.

(C) EXCEPTION.—The term 'swap dealer' does not include a person that enters into swaps for such person's own account, either individually or in a fiduciary capacity, but not as a part of a regular business.

(D) DE MINIMIS EXCEPTION.—The Commission shall exempt from designation as a swap dealer an entity that engages in a de minimis quantity of swap dealing in connection with transactions with or on behalf of its customers. The Commission shall promulgate regulations to establish factors with respect to the making of this determination to exempt.

4. **Security-Based Swap Dealer (Dodd-Frank § 761(a)(6), New Exchange Act 3(a)(71)(C))**

SECURITY-BASED SWAP DEALER.—

(A) IN GENERAL.—The term 'security-based swap dealer' means any person who—

(i) holds themself out as a dealer in security-based swaps;

(ii) makes a market in security-based swaps;

(iii) regularly enters into security-based swaps with counterparties as an ordinary course of business for its own account; or

(iv) engages in any activity causing it to be commonly known in the trade as a dealer or market maker in security-based swaps.

(B) DESIGNATION BY TYPE OR CLASS.—A person may be designated as a security-based swap dealer for a single type or single class or category of security-based swap or activities and considered not to be a security-based swap dealer for other types, classes, or categories of security- based swaps or activities.

(C) EXCEPTION.—The term 'security-based swap dealer' does not include a person that enters into security- based swaps for such person's own account, either individually or in a fiduciary capacity, but not as a part of regular business.

(D) DE MINIMIS EXCEPTION.—The Commission shall exempt from designation as a security-based swap dealer an entity that engages in a de minimis quantity of security- based swap dealing in connection with transactions with or on behalf of its customers. The Commission shall promulgate regulations to establish factors with respect to the making of any determination to exempt.