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February 22, 2011

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

Re: Proposed Rules - Business Conduct Standards for Swap Dealers and Major Swap Participants With Counterparties

Dear Mr. Stawick:

The University of Texas System ("System") appreciates the opportunity to comment on the Commodity Futures Trading Commission's (the "Commission") proposed rules concerning business conduct standards for swap dealers and major swap participants with counterparties. (75 FR 80637) The System is a regular and sophisticated participant in the swap markets, successfully employing swaps for over a decade as cost efficient and effective risk management tools in connection with hedging certain risks related to the System's $7.4 billion of outstanding debt. Given the importance of effectively managing this debt portfolio for our constituents, the more than 200,000 University of Texas students and taxpayers in the State of Texas, the System is very interested and engaged in ensuring that the proposed rules do not adversely affect our ability to access useful and effective risk management products.

Our comments focus on (a) clarifying the circumstances under which an advisory relationship may arise between a Special Entity (as defined in proposed Section 23.401) and a swap dealer and (b) memorializing in the final rules the Commission's view that a Special Entity's representative need only be independent of the swap dealer, not independent of the Special Entity. In addition, we recommend the Commission revise the regulations so that large, sophisticated debt issuers can, with appropriate safeguards and adhering to best practices, rules and standards, continue to have access to swaps and similar financial products.

Proposed § 23.440—Requirements for Swap Dealers Acting as Advisors to Special Entities

The current formulation of the rule provides an overly broad set of circumstances and therefore uncertainty, under which an advisory relationship would arise between a swap dealer and a Special Entity. If swap dealers are faced with uncertainty regarding compliance with business conduct rules, given the penalties for non-compliance, we anticipate that swap dealers may be forced to enact policies that could limit or exclude Special Entities' access to the swap markets and in doing so, would severely limit access to useful risk management products.

Proposed Section 23.440(b)(1) would require a swap dealer to act in the "best interest" of any Special Entity for which it "acts as an advisor." A swap dealer would be deemed to act as an "advisor" to a Special Entity where such dealer "recommends a swap or trading strategy that involves the use of swaps to a Special Entity" (see proposed Section 23.440(a)). The proposed rule provides a very limited exclusion for instances where a swap dealer provides a Special Entity with (a) information that is general transaction, financial, or market information or (b) swap terms in response to a competitive bid request from the counterparty (see proposed Section 23.440(a)).

The exclusions set forth in Section 23.440(a) are helpful, but overlook circumstances which should not give rise to an advisory relationship. Specifically, the System finds informal and course-of-business communications between a swap dealer and a Special Entity where current market ideas and structures are presented and discussed invaluable. Despite the intention of both parties that an advisory relationship is not intended, due to imposition of fiduciary-like obligations on swap dealers, the willingness of swap dealers to engage with Special Entities may be reduced. The imposition of advisor liability on a swap dealer that is proposing structures and ideas to a Special Entity, even customized ideas, could have a detrimental impact on the willingness of swap dealers to invest in the production of useful proposals for such Special Entities. Not only would swap dealers be discouraged from producing customized structures and ideas for Special Entities, but Special Entities would be compelled to assume a disadvantaged market position because some information may prove to be inaccessible and reduce market liquidity in the types of derivatives commonly used by Special Entities. The System believes strongly that the transacting parties should have the flexibility to determine if and when an advisory relationship arises.

In addition, even if the transacting parties intend that an advisory relationship not arise and instead intend to transact pursuant to proposed Section 23.450 (requirements for swap dealers acting as counterparties to Special Entities), the swap dealer's compliance with proposed Section 23.450 or its general obligations under proposed Section 23.402 (general provisions), Section 23.430 (verification of counterparty eligibility) and Section 23.431 (disclosure of material information) could give rise to a presumption that a recommendation has been made to the Special Entity causing swap dealer to have acted as an "advisor."[1] The net effect of the disclosure and reporting obligations and the lack of narrow conditions under which a swap dealer becomes an advisor would be tantamount to placing all swap dealers in an automatic fiduciary-like relationship with any Special Entity with whom they engage in a swap transaction.

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[1] For example, a dealer would be reasonable to conclude out of an abundance of caution that disclosures tailored to a particular swap transaction so that a Special Entity could evaluate the transaction's material risks could be viewed as advice. The "scenario analysis designed in consultation with the counterparty" referenced in proposed rule Section 23.431(a)(1)(ii) could also be reasonably viewed by a dealer taking a conservative approach as constituting advice. Even the dealer's diligence regarding an independent representative qualifications as provided for in proposed rule Section 23.450(b)(3) and the dealer's conclusion regarding the representative's execution of its own duties regarding fair pricing the appropriateness of the swap for the counterparty could require such a level of knowledge of the Special Entity's organization, risk profile and strategy as to fall within the scope of what could be reasonably viewed as advice.

We believe that the uncertainty regarding the application of the "best interest" standard may cause certain swap dealers to be averse to entering into swap transactions with Special Entities. If dealers choose to cease transacting with Special Entities, Special Entities will face increased financing and risk management costs relative to similarly situated market participants not within the definition of "Special Entity."

Accordingly, we suggest the following:

1. The Commission should clarify in the final rules that a swap dealer's compliance with its obligations under Section 23.450 or its compliance with its general obligations for all swap transactions with Special Entities shall not in and of itself give rise to an advisory relationship.

2. The Commission should adopt a certification process whereby swap dealers would be permitted to rely on an affirmative certification from a Special Entity that such Special Entity intends that an advisory relationship not arise between it and the swap dealer. The Commission could make this option available to certain "sophisticated" swap market participants, such as entities with a certain minimum threshold of assets under management, debt outstanding, or a certain level of frequency executing swaps.

3. The Commission should clarify that communications between a swap dealer and a Special Entity shall not give rise to an advisory relationship if:

    a. the communications have been made in response to such Special Entity's solicitation of information from the dealer and,

    b. in connection with any swap transaction arising from such communication, the dealer shall have received a certification from the Special Entity that such Special Entity intends that an advisory relationship not arise between it and the swap dealer.

Proposed § 23.450—Requirements for Swap Dealers and Major Swap Participants Acting as Counterparties to Special Entities

For a Special Entity and a swap dealer to qualify a transaction under Section 23.450, such swap dealer must have a reasonable basis to believe that the Special Entity has a representative that, among other criteria, is independent of the swap dealer or major swap participant (see Section 23.450(b)(3)). The Commission acknowledged that the "formulation of the duty is intended to clarify that "independent" as it relates to a representative of a Special Entity means independent of the swap dealer or major swap participant, not independent of the Special Entity" (see p. 75 FR 80652). We request that the Commission add further strength to this statement (and the legislative intent referenced in proposed rule release footnote 115) by incorporating a statement into the final rules clarifying that, for purposes of Section 23.450, the Special Entity's representative need not be independent of the Special Entity and may be an employee,

officer, agent, associate, trustee, director or affiliate of the Special Entity (so long as such representative is independent of the swap dealer).

Requiring a Special Entity to use external financial advisors when executing swap transactions imposes additional costs and some large, sophisticated issuers like The University of Texas System do not need the additional expense of a financial advisor to successfully utilize swaps and related instruments. Not only are there additional costs incurred when employing the services of an external financial advisor, but their use provides no guarantee to the successful utilization and execution of swap structures for a Special Entity as evidenced by certain headline cases involving municipal swaps where external financial advisors were involved.

We are grateful for the opportunity to comment on these important rules. As an entity that has effectively used swaps for over a decade to hedge and manage various financial risks, we see value in continued access to these important risk management tools. We are concerned that the proposed regulations could detrimentally alter the relationship between the System and its swap dealers. We appreciate the Commission's effort to craft rules that protect the interests of Special Entities without hindering their ability to employ swaps prudently and effectively and urge the Commission to amend the proposed regulations to address the concerns outlined in this letter.

Sincerely,

Scott C. Kelley

Scott C. Kelley
Executive Vice Chancellor
for Business Affairs

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cc: Chancellor Francisco G. Cigarroa, M.D.