

February 22, 2011

VIA ELECTRONIC SUBMISSION

David A. Stawick
Secretary
U.S. Commodity Futures Trading Commission
1155 21st Street, N.W.
Washington, D.C. 20581

Re: Business Conduct Standards for Swap Dealers and Major Swap Participants with Counterparties; Proposed Rule (RIN 3038-AD25)

Dear Mr. Stawick:

On behalf of Hess Energy Trading Company, LLC, and its wholly-owned subsidiaries (collectively "HETCO"), we hereby submit comments on the proposed rule¹ issued by the U.S. Commodity Futures Trading Commission ("Commission" or "CFTC") to implement business conduct standards for swap dealers and major swap participants, as required under Section 731 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act").²

HETCO's comments are limited to the provision in the Proposed Rule that would require swap dealers and major swap participants to have "a reasonable basis to believe that any swap or trading strategy involving swaps recommended to a counterparty is suitable for the counterparty based on information obtained through reasonable due diligence" ("institutional suitability requirement").³ By requiring a swap dealer or a major swap participant to perform an additional subjective review of its counterparty's financial and analytical abilities, whether or not the counterparty is a "special entity," HETCO respectfully submits that the institutional suitability requirement unnecessarily departs from the considered and well-reasoned statutory framework Congress expressly provided in Section 731 of the Dodd-Frank Act. This framework establishes that swap dealers and major swap participants must: (i) confirm that their swap counterparties are eligible contract participants ("ECPs"); and (ii) provide these counterparties – who are presumed to be sophisticated market participants by virtue of their ECP status – with sufficient information to allow them to assess the suitability of entering into specific swap transactions.⁴ Given the requirements that Congress expressly provided for, HETCO believes that the

¹ 75 Fed. Reg. 80,638 (Dec. 22, 2010) ("Proposed Rule").

² Pub. L. No. 111-203 (2010).

³ 75 Fed. Reg. at 80,659 (proposed CFTC Regulation 17 C.F.R. § 23.434(a)).

⁴ Dodd-Frank Act § 731 (to be codified as CEA § 4s(h)(3)).

Commission's Proposed Rule may inadvertently and unnecessarily create ambiguity and uncertainty for market participants.

I. Description of Hess Energy Trading Company and its Interest in the Proposed Rule

HETCO is a Delaware limited liability company established in 1997. HETCO recently organized branches in Paris and the Dubai International Financial Center and operates with three United Kingdom corporations, two of which are registered with the Financial Services Authority, a Cayman Islands exempted company, and a corporation organized in Singapore. All of these entities are used in the continually evolving development and implementation of a worldwide energy trading strategy effectuated by a series of spot and forward purchase and sales agreements, equity, foreign exchange, physical oil storage and chartered vessel transactions from time to time, swaps and other derivatives transactions in crude oil, petroleum products, natural gas and power, and freight transactions.

As a practical matter, HETCO believes that the institutional suitability requirement confuses, in ways that the statutory text does not, the distinction between entering into a swap as a counterparty and advising an entity as to the suitability of a particular swap transaction. HETCO respectfully submits that the parties to a swap, whether or not they are swap dealers, major swap participants, or end-users, typically *negotiate against* their counterparty on the terms of a transaction, rather than *recommending to* a counterparty how a transaction will best serve the counterparty's interests. The institutional suitability requirement is, therefore, incompatible with the way in which most swap counterparties operate in practice and inconsistent with Congress' intent.

Moreover, HETCO believes that any uncertainty caused by the institutional suitability requirement is unnecessary because the statutory framework Congress identified is based upon objective verification and disclosure and would be, on its own, robust and effective. Rather than providing clarity and stability in the swaps markets, HETCO believes that the institutional suitability requirement, as proposed, may be used by counterparties simply as a point of leverage to challenge agreements that, through no fault of either party, have become unprofitable. HETCO's interest in the Proposed Rule is focused on resolving this uncertainty.

II. The Commission Should Adopt Business Conduct Standards in a Manner that is Consistent with the Clear Structure Provided in the Dodd-Frank Act.

Section 731 of the Dodd-Frank Act adds section 4s to the Commodity Exchange Act ("CEA") and provides detailed provisions related to the registration and regulation of swap dealers and major swap participants.⁵ CEA Section 4s(h) imposes new business conduct standards on swap dealers and major swap participants that vary depending on: (1) whether the swap dealer or major swap participant is advising another entity or acting as a counterparty to a swap; and (2) whether or not the counterparty is a "special entity" (e.g., a government agency, a

⁵ Dodd-Frank Act § 731 (to be codified as CEA § 4s).

pension plan, etc.).⁶ Congress imposed the most extensive requirements where a swap dealer is acting as an advisor to a special entity. In these cases, the swap dealer must “make reasonable efforts . . . to make a reasonable determination that any swap recommended by the swap dealer is in the best interests of the Special Entity”⁷ In contrast, Congress required a swap dealer that is acting as a counterparty to a non-special entity: (1) to verify that the counterparty is an ECP; (2) to communicate in a “fair and balanced” manner; and (3) to disclose certain specified information regarding the characteristics, risks, valuation, and any potential conflicts of interest associated with a swap.⁸ In making this distinction, Congress appeared to rely on its expectation – as it had done previously – that participants that meet the financial criteria of an ECP set forth in the CEA are substantial and sophisticated entities. These entities, therefore, are capable of analyzing and managing their risk effectively, particularly when their counterparties are obligated to communicate fairly and provide meaningful disclosures regarding the underlying transactions.

Notwithstanding Congress’ well-thought-out legislative guidelines, the Commission has proposed a regulatory approach that would appear to collapse into one the distinct categories of participants and activities clearly and objectively defined in the statute. Under the Proposed Rule, *every* swap dealer and major swap participant would be required to have “a reasonable basis to believe that *any* swap or trading strategy involving swaps *recommended* to a counterparty is *suitable* for the counterparty based on information obtained through reasonable due diligence”⁹ This requirement comingles the concepts of advising another entity and acting as a counterparty in a swap transaction. The Proposed Rule also blurs the distinction between activities involving special entities, which are subject to heightened standards of “appropriateness,” and transactions with non-special entities that would be subject to less burdensome verification and disclosure requirements. As a result, HETCO believes that the Proposed Rule may confuse market participants, and lead to uncertainty in practice.

Although Congress provided the Commission with the authority to supplement the statutory requirements “in the public interest, for the protection of investors, or otherwise in furtherance of [the CEA],”¹⁰ it implicitly intended for any changes to remain consistent with the basic framework established in the statute, which relies on sophisticated counterparties (*i.e.*, ECPs) transacting on a fully-informed and largely unrestricted basis (*i.e.*, based on fair communication and adequate disclosure). A Proposed Rule that essentially shifts the burden of analysis from the counterparty to the swap dealer or major swap participant is inherently inconsistent with the statutory text and Congress’ intent. Congress was not silent as to how business conduct standards should apply.¹¹ On the contrary, it established an explicit legislative

⁶ Dodd-Frank Act § 731 (to be codified as CEA § 4s(h)).

⁷ Dodd-Frank Act § 731 (to be codified as CEA § 4s(h)(4)(C)).

⁸ Dodd-Frank Act § 731 (to be codified as CEA § 4s(h)(3)).

⁹ 75 Fed. Reg. at 80,659 (proposed CFTC Regulation 17 C.F.R. § 23.434(a)).

¹⁰ Dodd-Frank Act § 731 (to be codified as CEA § 4s(h)(3)(D)).

¹¹ Connecticut Nat’l Bank v. Germain, 503 U.S. 249, 254 (1992) (“Courts are to presume that a legislature says in a statute what it means and means in a statute what it says.”).

structure that deliberately subjects certain types of activities and categories of market participants to greater oversight. HETCO respectfully requests that the Commission reconsider the institutional suitability requirement in the context of Congress' intent.

Furthermore, HETCO believes that the Proposed Rule may underestimate the uncertainty and commercial burden associated with the institutional suitability requirement. In the Proposed Rule, the Commission states that it "has considered that many swap dealers and major swap participants already are, or will be, subject to institutional suitability obligations by virtue of their status as banks, broker-dealers or security-based swap dealers."¹² However, the definition of "swap dealer" is broad and may include many market participants that are not already subject to some form of business conduct standards. To the extent that the institutional suitability requirements reach participants like HETCO, these requirements likely will significantly affect the way in which HETCO, and other similarly situated market participants transact in the swaps markets. Accordingly, HETCO requests that the Commission reconsider its approach to the Proposed Rule in light of these potential unintended consequences.

III. Conclusion

HETCO respectfully requests that the Commission reconsider its approach to the Proposed Rule and the institutional suitability requirement to align these requirements more closely with the language of the Dodd-Frank Act. As proposed, HETCO believes that the institutional suitability requirement will create uncertainty for HETCO and other similarly situated market participants that is unnecessary and easily avoided if the Commission simply adopts the framework Congress provided.

HETCO welcomes the opportunity to discuss these issues further with the Commission and its Staff. Please contact us at (202) 862-2200 if you have any questions regarding HETCO's comments.

Respectfully submitted,



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¹² 75 Fed. Reg. at 80,647.

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cc: Chairman Gensler
Commissioner Dunn
Commissioner Chilton
Commissioner Sommers
Commissioner O'Malia
Daniel Berkovitz, General Counsel