February 22, 2011

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

RE: RIN 3038-AD10, End-User Exception to Mandatory Clearing of Swaps

Dear Mr. Stawick:

The National Council of State Housing Agencies (NCSHA) thanks you for the opportunity to comment on the proposed rule governing the elective exception to mandatory clearing of swaps available for swap counterparties meeting certain conditions under Section 2(h)(7) of the Commodity Exchange Act (CEA), as amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). We urge you to amend the proposed rule to clarify that the end-user exception applies to HFAs and their swap transactions and relax the reporting requirements to ease the administrative burden they would create for HFAs and other end-users.

NCSHA represents state Housing Finance Agencies (HFAs), which issue mostly tax-exempt bonds to finance affordable housing for home buyers and renters. HFAs also administer a wide range of affordable housing and community development programs, including the Low Income Housing Tax Credit, HOME, Section 8, down payment assistance, homebuyer education, loan servicing, homeless assistance programs, and state housing trust funds. The federal government has recently supported the HFAs' efforts to assist in housing and economic recovery by entrusting to them the administration of several new programs, including the Tax Credit Assistance Program, Housing Credit Exchange Program, New Issue Bond Program, Temporary Credit and Liquidity Program, Hardest-Hit Fund, and Emergency Homeowner Loan Program.

We appreciate that the Commodity Futures Trading Commission (CFTC) is seeking comments on the proposed rule's application to HFAs. NCSHA is confident that HFAs would be eligible to elect the end-user exception provided under Section 2(h)(7) of CEA; however, we ask that the CFTC clarify several issues in the final rule in order to verify that HFAs are eligible end-users. We urge the CFTC to exclude explicitly state and local governmental entities, specifically HFAs, from the definition of a "financial entity" as defined in Section 2(h)(7) of CEA. Similarly, we recommend that the CFTC expressly confirm that swaps used by state and local governmental entities, including specifically swaps used by HFAs, "hedge or mitigate commercial risk," as defined in Section 2(h)(7) of CEA.

In addition, NCSHA encourages the CFTC to relax the reporting requirements so HFAs would not have to fulfill the notification and reporting requirements on a trade-by-trade basis. Reporting on a trade-by-trade basis would impose an unnecessary and costly burden on HFAs as eligible end-users.

Finally, we ask that the CFTC clarify how the notification and reporting requirements will affect the approval process for eligible end-users electing the exception from swap clearing. The notification and reporting requirements mandated in statute were not intended to act as regulatory barriers for eligible end-users, and we do not believe the CFTC should impose unnecessary requirements that make hedging prohibitively expensive for eligible counterparties.

Clarify That HFAs Are Not "Financial Entities"

The Dodd-Frank Act prohibits entering into a swap that is required to be cleared unless it is submitted to a designated clearing organization with full daily collateral posting for clearing, unless the swap qualifies for the end-user exception. Under the Dodd-Frank Act, the end-user exception applies when a counterparty is not a financial entity, uses the swap(s) to hedge or mitigate commercial risk, and notifies the CFTC of how it is able to meet its financial obligations associated with the uncleared swaps.

The Dodd-Frank Act defines the term "financial entity" to include swap dealers, major swap participants, commodity pools, certain private funds and employee benefit plans, and "[persons] predominantly engaged in activities that are in the business of banking, or in activities that are financial in nature, as defined in section 4(k) of the Bank Holding Company Act of 1956." While HFAs have never engaged in activities classified as "financial in nature," it is impossible to know whether future federal regulations may classify the activities in which HFAs participate as "financial in nature."

The Federal Reserve Board (Board) has the authority, under Regulation Y, to define those activities that are "financial in nature." In the past, the Board has defined activities engaged in by banks or financial holding companies as "financial in nature"; however, the Board reserves the right to modify the definition of activities that are "financial in nature" in order to address new threats to the nation's constantly-evolving financial system. The Board is currently accepting comments on a proposal to include in Regulation Y a list of new activities that it has determined by statute, regulation, or order to be "financial in nature" under Section 4(k) of the Bank Holding Company (BHC) Act of 1956. Comments to the Board's proposal are due by March 11, 2011.

Because it is unknown at this time whether HFAs will be defined as "financial entities" under Regulation Y, NCSHA requests that the CFTC make clear that state and local governmental entities, specifically HFAs, are not "financial entities" as defined in Section 2(h)(7) of CEA. NCSHA believes that if Congress had not intended for HFAs and other municipal issuers to be eligible for the end-user exception, it would have included them in the definition of a "financial entity."

Clarify That Swaps Used by HFAs "Hedge or Mitigate Commercial Risk"

The Dodd-Frank Act defines a swap that hedges or mitigates commercial risk as one that is economically appropriate for reducing certain business risks, including the potential change in the value of assets, liabilities, services, or fluctuations in foreign exchange or interest rates. HFAs typically use swaps to hedge their interest rate risk in connection with the issuance of tax-exempt housing bonds. The CFTC should provide an explicit verification that swaps used by state and local governmental

entities, including specifically swaps used by HFAs, "hedge or mitigate commercial risk," as defined in Section 2(h)(7) of CEA.

Pursuant to state statutes, official swap guidelines, and swap policies, HFAs do not enter into derivative transactions for speculative purposes, nor do they make a market in swaps or trade in swaps for the purpose of profit-making through speculation. HFAs engage in swap transactions that are necessary to provide the lowest cost financing to the beneficiaries of their bond issues. They typically hold those swaps until maturity. NCSHA recommends that the CFTC clarify that swaps entered into by HFAs hedge or mitigate commercial risk and consequently meet the requirements necessary to qualify for the end-user exception.

The Clearing Requirements Will Increase HFAs' Cost of Capital

HFAs issue tax-exempt bonds to finance affordable housing for lower income homeowners and renters. To provide affordable mortgages at attractive rates and tailored to the needs of their individual communities, HFAs often use "plain vanilla" interest rate hedging swaps. HFAs are able to provide lower cost, fixed rate mortgages to lower income families by using swaps to a fixed rate in combination with variable rate bonds to produce lower interest rates than those available for fixed rate bonds. However, HFAs might use any of several methods that allow them to keep their costs down and operate efficiently and flexibly, including repackaging municipal bonds into tax-exempt instruments with characteristics different from the bonds as originally issued, embedding more sophisticated interest rate formulas into tax-exempt bonds, and employing products to help HFAs manage their fund investments.

HFAs enter into swap contracts that are generally not subject to clearing or margin requirements, which allows them to keep costs low, choose from a larger variety of swaps, and avoid the costly posting of collateral. If HFAs are required to meet swap margin and clearing requirements, they will see their cost of capital increase substantially. These increased costs will then be passed on to the beneficiaries of HFA bond issues.

The Trade-by-Trade Reporting Requirement is Unnecessary and Administratively Burdensome

The proposed rule's trade-by-trade reporting requirement is overly burdensome and much greater than is necessary to meet the standards set forth in Section 2(h)(7) of CEA. The rule should only require the limited notification requirements mandated by Section 2(h)(7) of CEA, as well as those measures the CFTC feels are necessary to prevent abuse of the end-user exception.

NCSHA is confident that the statutory requirement to notify the CFTC how the electing counterparty "generally meets its financial obligations" can be adequately satisfied through a single filing with the CFTC. At the very least, NCSHA's members would prefer to notify the CFTC of the collateral provisions of their non-cleared swaps on a periodic basis with respect to all swaps entered into during the period. It violates the intent of the Dodd-Frank Act for the CFTC to adopt rules that administratively prevent otherwise eligible entities from taking advantage of the statutory exception.

Clarify the CFTC's Authority to Deny Eligible Counterparties the Ability to Elect the End-User Exception

NCSHA requests that the CFTC clarify how the notification and reporting requirements will affect the approval process for eligible end-users electing the exception from swap clearing. It is unclear, in the proposed rule, whether the CFTC will deny a counterparty the right to elect the end-user exception

on the basis of "insufficiently meeting the CFTC's notification and reporting requirements." NCSHA does not believe the CFTC has the authority to reject eligible counterparties from electing the end-user exception on the basis of a failure to meet the reporting or notification standards set forth by the CFTC. However, if the CFTC determines that it is authorized to reject a counterparty's election based on "insufficient reporting or notification," NCSHA requests that the CFTC provide a detailed list of the criteria it deems as necessary for a counterparty to sufficiently meet the CEA's notification and reporting requirements.

Thank you for your consideration of our comments. Please do not hesitate to contact me if we can provide additional information.

Sincerely,

Garth B. Rieman
Director, Housing Advocacy and Strategic Initiatives