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Three Lafayette Centre
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Ms. Elizabeth M. Murphy
Secretary, Securities and Exchange Commission
100 F Street N.E.
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Re: RIN 3038 – AD06, RIN 3235 - AK 65 Further Definition of Swap Dealer, Security-Based Swap Dealer, Major Swap Participant Major Security-Based Swap Participant and Eligible Contract Participant; File No. S7-39-10

Ladies and Gentlemen:

MetLife welcomes the opportunity to follow up on our earlier comment letter dated September 24, 2010 in connection with the Advance Notice of Proposed Rulemaking (the "Prior Letter"), to comment on the proposed regulations (the "Proposed Rules" or the "Proposal") further defining the terms swap dealer and major swap participant ("MSP") for purposes of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") included in the release (the "Release") published December 21, 2010 (75 Fed. Reg. 80174) by the Commodity Futures Trading Commission (CFTC) and the Securities Exchange Commission (SEC) (collectively the "Commission.")

Unless otherwise indicated, this letter refers to the sections of Dodd-Frank amending the Commodity Exchange Act ("CEA"), the defined terms thereunder and the rules to be adopted by the CFTC thereunder, but the discussion is intended to relate equally to the parallel regulation by the SEC contemplated under equivalent amendments to the Securities Exchange Act of 1934.

MetLife appreciates the thoughtful and interactive approach the CFTC and SEC have taken in their rulemaking thus far. We are providing these comments to respond to some of the Commission's requests for input as well as to address some critical issue areas in this regulation.

MetLife Background Information. MetLife, Inc. is the holding company of the MetLife family of insurance companies. The MetLife organization is a leading global provider of insurance, annuities and employee benefit programs, serving 90 million customers in over 60 countries. MetLife holds leading market positions in the United States (where it is the largest life insurer based on insurance in force), Japan, Latin America, Asia Pacific, Europe and the Middle East.

The MetLife insurance companies are licensed and subject to regulation in their domiciliary jurisdictions, as well as in each U.S. and international jurisdiction in which they conduct business. In the U.S., state insurance laws and regulations govern the financial aspects of the insurance business, including standards of solvency, statutory reserves, reinsurance and capital adequacy, and the business conduct of insurers. Each insurance subsidiary is required to file reports, generally including detailed annual financial statements, with insurance regulatory authorities in each of the jurisdictions in which it does business, and its operations and accounts are subject to periodic examination by such authorities. Each of the MetLife U.S. insurance companies is subject to risk-based capital (RBC) requirements, and reports its RBC based on a formula calculated by applying factors to various asset, premium and statutory reserve items, as well as taking into account the risk characteristics of the insurer. The major categories of risk involved are asset risk, insurance risk, market risk (including interest rate, credit and equity risk) and business risk. The formula is used as an early warning regulatory tool to identify possible inadequately capitalized insurers for purposes of initiating regulatory action, and not as a means to rank insurers generally. State insurance laws provide insurance regulators the authority to require various actions by, or take various actions against, an insurer whose RBC ratio does not meet or exceed certain RBC levels. The investments of each of the U.S. insurance subsidiaries which back our contractual liabilities are subject to regulation under relevant state insurance laws that require diversification of the insurers' investment portfolios and limit the amount of investments in certain asset categories. The state regulation applicable to MetLife generally limits our U.S. insurers' use of derivatives to hedging, asset replication and limited writing of covered calls.

As a result of its ownership of MetLife Bank, NA, a federally chartered bank, MetLife, Inc. is subject to regulation under the Bank Holding Company Act of 1956 and to inspection, examination, and supervision by the Board of Governors of the Federal Reserve Bank of New York. MetLife, Inc. and MetLife Bank are subject to risk–based and leverage capital guidelines issued by the federal banking regulatory agencies for banks and financial holding companies. The federal banking regulatory agencies are required by law to take specific prompt corrective actions with respect to institutions that do not meet minimum capital standards.

Finally, MetLife, Inc. is a public company, registered under the Securities Act of 1934 and has securities listed on the New York Stock Exchange.

"Swap Dealer"

General. MetLife generally favors the definition of Swap Dealer in the Proposed Rule and believes that it appropriately utilizes traditional concepts, such as the "trader-dealer" distinction to distinguish between market intermediaries and market end-users. The careful identification of Swap Dealers is significant because the type of regulation properly applicable to Swap Dealers, as with the analogous FCMs and broker-dealers in the exchange-traded futures and securities markets, is appropriately focused on risks arising from their market interconnectedness, customer relationships, market-making, and clearing obligations. Conversely, the scope of regulation appropriate for large scale end-users should more narrowly target the market risks potentially arising from the size of their positions.

We particularly commend the following interpretive note by the CFTC on a Swap Dealer's functional role in the market:

> "In sum, to determine if a person is a swap dealer, we would consider that person's activities in relation to the other parties with which it interacts in the swap markets. If the person is available to accommodate demand for swaps from other parties, tends to propose terms, or tends to engage in the other activities discussed above then the person is likely to be a swap dealer. Persons that rarely engage in such activities are less likely to be deemed swap dealers. Release, p. 80177.

This formulation creates a clear conceptual distinction between a market participant that is holding itself out to others as providing a service or being willing and available to transact, thereby facilitating a liquid and orderly market (a dealer) and a market participant that executes swap transactions solely to advance its own investment objectives (an end-user).

We believe it would be beneficial if this interpretive provision were clearly embodied in the definition itself, or at least included in the Commission's adopting release.

Affiliate Transactions. We would like to comment on the Commission's formulation of an appropriate treatment with respect to swap transactions within a consolidated corporate group, as they arise in the context of the Swap Dealer definition. It is sometimes the case that a corporate group will seek to centralize its derivatives trading through a single entity (a "Group Risk Aggregator"), which consolidates the risks of group companies and conducts some or all of the group's derivatives trading. Such arrangements have the benefit of facilitating consolidated risk management within an organization as well as achieving economic efficiencies through reduced transaction costs and collateral requirements. Such Group Risk Aggregators will only enter into derivative transactions with their affiliated group companies and with Swap Dealers or through other registered market intermediaries such as FCMs to facilitate intra-group risk allocation and, as appropriate, pass-through residual risk to the market on behalf of its corporate group. We concur with the Commission's view that:

"In determining whether a particular legal person is a swap dealer ... we preliminarily believe it would be appropriate for the person to consider the economic reality of any swaps and security –based swaps it enters into with affiliates (i.e. legal persons under common control with the person at issue) including whether those swaps ... simply represent an allocation of risk within a corporate group. Swaps between persons under common control may not involve the interaction with unaffiliated persons that we believe is the hallmark of the elements of the definitions that refer to holding oneself out as a dealer or being commonly known as a dealer." Release, p. 80183.

We believe the conclusion that a Group Risk Aggregator is not a Swap Dealer, in accordance with the Commission's interpretive approach above, fully accords with the statutory policy behind regulation of Swap Dealers. Non-Swap Dealer treatment should be available where the Group Risk Aggregator and its affiliates are all members of the same corporate consolidated group, whether or not each is wholly owned by the parent, since through the consolidation there is a common corporate interest in the risks managed. For the sake of certainty, we believe it would be beneficial if this interpretive position were clearly articulated in the definition itself or at the least included in the Commission's adopting release.

On a related matter, we request that the Commission make clear that any swap trade between a Group Risk Aggregator and an affiliated company within the consolidated group should not be viewed as a "Swap" for purposes of the Dodd-Frank rule framework. Such inter-affiliate trades would not in any way impact the financial markets or any third parties. To the extent that an external trade between a Group Risk Aggregator and a third party Swap Dealer resulted from the activity, that external-facing swap would become subject to all applicable Dodd-Frank requirements including clearing (if applicable), capital and margin, and reporting. Regulation of the internal corporate risk-shifting transaction (including by imposing clearing or the other requirements referred to above) would inappropriately penalize the corporate group by doubling up on their transaction costs and otherwise negating the risk management and economic efficiencies achieved by through the use of these internal risk management structures.

SEF Use. The Commission requests comment (Release p. 80179) on whether membership in or use of a SEF facility by a party should be a factor that should be considered in the analysis of whether an entity is a Swap Dealer. The SEF environment is yet to be fully determined, and it is not yet clear who will be members of, or have access to, these facilities. Since market end-users as well as Swap Dealers will likely transact through SEFs it appears that this should not be a factor in the Swap Dealer analysis. Similarly, end-user clearinghouse membership, should not be a factor in this determination In any event, it appears premature to draw any conclusions at this time as to regulatory characterization in light of the developing market environment.

Definition of "Major Swap Participant"

Swap Categories. The Commission has requested comment on whether the Rate Swap Category should be divided into two categories, one for swaps based on interest rates, inflation rates and

other monetary rates, and a separate category for swaps based on rates of exchange between different currencies and if a separate category is suggested, in what category cross currency rates should be considered. MetLife generally concurs with the demarcation of swaps into four proposed Major Swap Categories and the definition of those categories. It is our fundamental belief that the risk in Cross Currency Swaps is measured by the difference in interest rates in two currencies and should properly be considered in the Rate Swap category. Creation of a separate category for cross currency swaps could lead to confusion, especially if market participants are obligated to bifurcate cross currency swaps between separate Rate and Cross Currency categories. We strongly advocate increasing the limits for the Rate Swap Category to avoid penalizing U.S. firms with large international businesses that want to diversify credit and portfolio risk and prudently risk manage their currency exposures. ***See specific proposal in the next section below for increasing the Rate Swap limits.***

Comments on Substantial Position and other MSP Tests MetLife generally commends the Commission for a balanced and practical approach to establishing a framework for quantifying Substantial Position and Substantial Counterparty Exposure for purposes of establishing MSP status. We have the following comments to the Proposed Rules.

- **Increase of Exposure Limits for the Rate Swap Category Needed**

MetLife is generally supportive of the aggregate uncollateralized outward exposure ("Current Exposure") and aggregate potential outward exposure ("Potential Exposure") Limits set forth in Rule §1.3 (sss) (1)(ii),(iii) and (iv).

However, we are concerned that Current Exposure and Potential Exposure Limits for Rate Swaps, set forth in Rule §1.3(sss)(1)(i)(A) and (B) and Rule §1.3(uuu)(1)(i) and (ii) are insufficiently broad to appropriately measure the derivatives market for all Rate Swap (including cross currency swaps) which exceeded $434 Trillion in Notional Amount as of June 30, 2010[1]. This amount is greater than 90% of all derivatives reported in the ISDA Mid-Year Market Survey.[2] We accordingly recommend that the limits in Rule §1.3(sss)(1)(i)(A) and (B) be increased to $4 billion and $8 billion, respectively with corresponding increases to the limits in Rule §1.3(uuu)(1)(i) and (ii) to $7 billion and $14 billion, respectively. In addition, MetLife recommends that the limits in Rule § 1.3(uuu)(1)(i) and (ii) be increased to reflect the sum of the amounts in Rule §1.3(sss)(1)(i) through(iv) to be consistent with the amounts and methodology specified in Rule §240.3a67-5(a)(1) and (2) of the Proposal.

- **Adjustments to the Definition of Current Exposure Needed**

Under the Proposal's Substantial Position test a party's derivative transaction exposure is netted against the collateral posted to secure such derivative transactions when determining whether or not the Substantial Position Test threshold levels have been met. Additionally, Current Exposure is

[1] See ISDA Mid-Year Market Survey, 2010
[2] Id.

computed on a net basis, taking into account any master netting agreements between the entity and a single counterparty. MetLife strongly endorses the approach proposed in the definition of Current Exposure related to offsets provided by contractual netting arrangements. We believe this methodology for determining Current Exposure correctly implements Congressional intent in Dodd-Frank. Section 1a(33)(B) of the CEA, as amended by Dodd-Frank, clarifies that in defining "substantial position," the Commission should establish a threshold "that [it] determines to be prudent for the effective monitoring, management and oversight of entities whose derivatives activities can significantly impact the financial system of the United States." The same section of Dodd-Frank also instructs the Commission to consider an entity's relative position in uncleared swaps as opposed to cleared swaps and take into consideration the value and quality of collateral held against counterparty exposures. In general, the Proposed Rules succeed in properly capturing this legislative guidance, and appropriately provide a reduction for contractual netting and collateralization requirements, which are already in place to mitigate counterparty risk.

MetLife recommends two additional clarifications to Rule § 1.3(sss)(2) in order to provide full credit for collateral consistent with the netting and credit support agreements in place between market participants and to provide flexibility for market participants to utilize a wide range of collateral that contains haircuts/reductions in value agreed between market participants under credit support agreements between such market participants.

Rule §1.3(sss)(2) provides for the calculation of a person's current exposure on a net basis across all major swap categories.[3] Collateral is utilized in connection with the positions with negative mark-to-market value in a particular major swap category.[4] This proposal assumes incorrectly that counterparties pledge collateral against specific transactions. This assumption does not reflect standard wholesale market practice where as a rule collateral is not posted in connection with any specific trade, but is pledged against the parties' aggregate net exposure under a master agreement pursuant to a bi-lateral credit support agreement. This approach provides for cross-product netting and margining that reduces excessive collateral flows and operational risk associated with the movement of securities collateral. MetLife recommends that such approach be adopted in the Proposed Rule by amending Rule § 1.3(sss)(2) to measure Current Exposure across all major swap categories and allocate any uncollateralized amount pro rata among each major swap category with Current Exposure.[5]

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[3] Rule § 1.3(sss)(2)(iii)

[4] Rule § 1.3(sss)(2)(i)

[5] The following example shows the difference in treatment between the Proposed Rules and the MetLife recommendation: Assume amarket participant ("Party A") that has a collateralized netting agreement with its counterparty that includes a $10 million Threshold and has open positions in three Major Swap Categories resulting in the following exposures: (1) a negative mark-to-market exposure of $20 million in the Rate Swap Category, (2) a positive mark-to market position of $25 million in the Credit Swap Category and (3) negative mark-to-market exposure of $30 million in the Equity Swap Category. Assume further that Party A has pledged $15 million in collateral (Net position including all of Party A's swaps with counterparty of $25 million less the $10 million Theshold). Under the approach suggested by the Proposed Rules, the counterparty would incorrectly appear to have an aggregate $35 million exposure to the Party A. In contrast, under our proposal, the regulatory determination would conform to economic reality, that is, the counterparty exposure to Party A would be calculated as $10 million.

The Commission has requested comment on whether certain types of collateral that cannot be readily valued should be excluded from the test and whether certain haircuts dictated by applicable regulations should be mandated in calculation of Current Exposure. MetLife believes strongly that high quality, fixed-income assets including corporate bonds, asset-backed securities, RMBS and other instruments should be included as Collateral offsets in the MSP Tests to the extent that such assets can be readily valued in normal markets (1) through independent pricing sources, such as Bloomberg and Reuters or (2) by obtaining firm bids from recognized market-makers in the specific asset class. We also believe that market participants should be permitted the flexibility to manage such Collateral using a range of agreed industry–standard haircuts and definitions, such as the Collateral Asset Definitions published by ISDA. MetLife believes that these guidelines provide flexibility to end-users of collateralized derivatives without sacrificing important protections of the financial markets and other market participants.

The efficiencies of the use of investment assets as collateral have become essential to the pricing of various life insurance company products and the structuring of the asset portfolio that supports that pricing. Presently, MetLife and other life insurers invest a significant portion of their funds in high quality, fixed income assets, including corporate bonds and asset-backed securities in accordance with the investment guidelines and prudential standards prescribed by the insurance regulators. The income generated from these investments is significant to life insurers' business model and continued operation because it allows such insurers to lower the cost of insurance offered to customers. If life insurers are not permitted to continue to post a wide range of Collateral as margin, such insurers would be presented with the dilemma of either reducing their hedging programs or restructuring their investment portfolio Either would be extremely unfortunate. Reducing hedging programs would expose the insurer to avoidable and potentially expensive market risks which could have adverse effects on the insurers business model. Similarly, restructuring a life insurer's investment portfolio would make hedging more expensive. Ultimately, the opportunity cost of limiting the type or value of eligible collateral would be borne by hardworking Americans who rely on life insurers for effective insurance and retirement products that ensure a stable financial future.

- **Adjustments to the Definition of Potential Exposure**

MetLife strongly supports the conversion factors and adjustments for swaps that give reasonable credit for the relative riskiness of certain types of swaps and important risk mitigants such as daily mark-to market margining and netting, In particular, we believe that the Conversion Matrix for Different Swaps and the 0.2 multiplier(80% reduction) for swaps that are subject to daily mark-to-market margining or are cleared by a registered clearing agency or derivatives clearing organization as set forth in Rule §1.3(sss)(3)(iii)(A) of the Proposed Rules represent a balanced approach to these issues. In addition, MetLife recommends that Rule §1.3(sss)(ii)(A)(4) should be revised to limit Potential Exposure to the net present value of premiums for all purchased options instead of applying this adjustment solely to Credit Default Swaps Our proposed change is also consistent

with the language of Rule §1.3(sss)(ii)(A)(3) relating to fully paid options that does not distinguish among types of options.

MetLife supports the Proposed Rule's use of a quarterly cycle to measure the threshold amount of exposure for identifying Major Swap Participants. The 'quarterly cycle' of measurement alleviates the risk of attaining MSP status due to market conditions on a given day. MetLife does recommend however, that the one year reassessment period for a market participant that qualifies as an MSP should be shortened to two consecutive quarters of satisfaction of the MSP Tests in order to no longer be considered as an MSP.

Scope of Designation of MSP Status (Rule §1.3(qqq)(2)). The Proposed Rules provide that, absent exemptive relief from the Commission, when the "Substantial Position Test" is met for a specific Major Swap Category then the MSP requirements are triggered for all of the Swaps that the entity enters into, not just those in the category where the trigger event occurs. MetLife believes that this position runs counter to the clear language and intent of the relevant provisions of Dodd-Frank, which expressly provide that "a person may be designated as a major swap participant for one or more categories of swaps without being classified as a major swap participant for all classes of swaps." It is conceivable that a market participant could pose risk to one segment of the market by reason of its size, thus warranting the imposition of capital and margin on its positions in that segment and other compliance and oversight requirements, while its other business segments, which do not meet the substantial position threshold, would operate without posing similar market risk.[6] Given the financial penalty imposed on a Major Swap Participant by additional capital and margin charges, this is not an immaterial concern, and MetLife respectfully requests the Commission's careful consideration of our view.

Consistent with registration process generally promulgated under the commodities and securities regulation, MSP registration is self-determinative and is entirely standards-based. As noted by the Commission, in connection with the registration requirement, market participants are in a position to assess their activities to determine whether they function in the manner described in the definitions. Given the lack of clarity with respect to the procedure for exemptive relief and the additional costs that would be imposed on the market participants and ultimately on the Commission, we urge the Commission to abandon the blanket MSP designation under the proposed CFTC Rule §1.3(qqq) in favor of a more flexible approach, as expressly contemplated by the statute, and allow each applicant to independently determine the categories of swaps for which it is required to register in accordance with the MSP registration standards.

Exclusions - Hedging or Mitigating Commercial Risk. (Rule §1.3(ttt)) MetLife generally supports the approach taken by the Commission in defining the scope of the hedge exclusion. We believe that the formulation adopted by the Commission, is well understood and represents a good balance between specificity and generality in encompassing an appropriately wide range of

[6] The second test, of substantial counterparty exposure aggregates all positions of a person, in all Major Swap Categories, so would potentially catch a more diversified large end-user.

economic risk reduction practices while appropriately carving out speculative, risk-taking activity. We particularly commend the inclusion of broad qualitative definitional language as alternatives to the more specific (and potentially changeable) accounting standards.

Hedging by Financial End-Users; Hedging of Financial Risks. MetLife favors the determination by the Commission to afford to financial institutions as well as non-financials the ability to exclude their hedging positions from the first "Substantial Position" test. For the reasons set forth in detail in our Prior Letter (copy attached), we believe that this result correctly reflects the statutory policy of Dodd-Frank as well as prior interpretations of the CFTC. In particular, we consider that the treatment of financial institutions as "commercial enterprises":

- is consistent with both existing CFTC Rule §1.3(z) and its codification in Section 737(c) of Dodd-Frank;
- is an extension of the CFTC's existing practice in the regulated futures markets and avoids inconsistent treatment of the same activity in the futures market and in the OTC market;
- gives economically appropriate recognition to the fact that there is no fundamental difference between an insurance company reducing its risk by the use of derivatives transactions and any other commercial enterprise (be it an automaker or an oil company) doing the same thing;
- is supported by the specific exclusion of financial entities from the Dodd-Frank definition of a commercial end-user. Absent that exclusion, the definition would catch all entities hedging or mitigating "commercial risk". We submit that Congress clearly determined that it must expressly exclude financial entities, because the term "commercial risk" encompasses financial risks; and
- properly acknowledges that insurance regulators permit insurance companies to hedge or mitigate risk through the use of derivatives in accordance with the insurance companies' derivatives use plan.

Standards for Hedges. In regard to standards for hedges, the Commission has asked whether a range of qualitative or quantitative tests might be appropriate to limit the scope of hedging, for example effectiveness tests, whether a hedge should be limited to mitigating a single risk or an aggregate risk basis, or whether hedging would be required on a single entity or consolidated basis, whether dynamic hedging or asset optimization strategies should be addressed. MetLife's view is that, within the boundaries proposed in Rule §1.3(ttt), such additional limits are unnecessary and could cut against the statutory policy favoring hedging. We note that while several versions of the financial reform legislation included a narrower hedging standard, the final version adopted was broadly inclusive.

In our view, the hedger's good faith determination that a transaction is risk reductive (i.e. a hedge) of an identified risk or risks should be adequate. It would be appropriate for the hedge determination, including the risks hedged, to be documented so that it could be easily audited by the Commission, an SRO or the end-user's internal or external auditors. This requirement is in fact included in the SEC version of the definition (Rule §240.3a67-4(c)). In particular, while we feel that hedge effectiveness reviews are beneficial and can certainly buttress a hedge characterization,

we do not believe that it is appropriate to mandate an effectiveness testing procedure, let alone of any specific type, for non-registrants, as is proposed by the SEC and suggested by the Commission.[7] Further, we believe prescriptive imposition of particular effectiveness tests is inadvisable. No single quantitative effectiveness test is likely to cover the full range of hedging strategies, and an overly restrictive or prescriptive standard will counter the beneficial intent of the exclusion to not impede bona fide hedging activity.

Hedging a Swap. MetLife believes that the inclusion of swaps held to hedge or mitigate the risk of non-hedging swap positions in calculating an entity's "substantial position" in a swap category, as set forth under the proposed CFTC Rule 1.3(ttt)(2)(ii), would inappropriately limit the scope of the hedging exclusion contemplated by Congress. Where a market participant enters into a swap for the purpose of mitigating the risk of another swap position, the speculative nature of the hedged swap would not alter the risk-reducing nature of the hedge and should not be the exclusive basis for including the hedge in the overall exposure calculation. Consequently, we believe that consistent with public policy recognized by Congress, CFTC Rule 1.3(ttt)(2)(ii) should provide that *any* swap held to hedge or mitigate the risk of another swap position shall be deemed to be held for the purpose of "hedging or mitigating commercial risk", irrespective of the nature of that other position, and excluded from the overall exposure for the purposes of the "substantial position" determination. [8]

Hedging Affiliate Risk. There are a number of contexts within which hedging of affiliate risk may legitimately occur. In the case of insurers, under the insurance laws, insurers are limited to hedging their own risks. This could however include indirect risks, such as risks held in subsidiaries of the insurer. In both regulated and non-regulated corporate groups, parent companies frequently hedge risks within their consolidated group. Further, it is possible for a corporate group to use a Group Risk Aggregator, as described previously to centralize hedging activites for the corporate group. The aggregator in this context is assuming risk from its affiliates and laying it off to dealers, so its activities could be described variously as hedging its own risk of the assumed positions, the risk of the affiliates or the risk of the corporate group as a whole. Although it would be appropriate to require documentation of the relationship and risk transfer arrangements in such a situation to constitute an auditable record of the hedge characterization, we submit that in their economic nature these transactions are risk reductive, Such risk management and transfer structures in which an affiliate is hedging the risks of its affiliates or consolidated group should be treated as hedging for purposes of the MSP definition.

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[7] Since the hedge exclusion is part of the jurisdictional determination, any effectiveness testing requirement embedded in the rule would necessarily be imposed on non-registrants, since status or non-status under the MSP definition would not be determinable without its application.

[8] The practical consequence of not treating the hedging swap as a hedge would be to require treatment of **both** swaps toward "substantial position" for the purposes of the first leg of the MSP Test. Treatment of the hedging position as a hedge, on the other hand would not change the treatment of the hedged swap or result in a subtraction from the entity's "substantial position" for purposes of this test. Both swaps would be counted toward the "substantial counterparty exposure and substantial position tests of the second and third legs of the MSP Test in either case.

Financial Entity Subject To Capital Requirements Established By An Appropriate Federal Banking Authority. The third leg of the MSP statutory definition, repeated in the Proposed Rule (§1.3(ppp)(1)(c)), excludes from its coverage "entities subject to a capital requirement established by an appropriate Federal banking agency". Thus, Congress has determined that any systemic risk posed by such entity's leverage is dealt with through application of a federal bank capital regime in lieu of the MSP regulatory requirements.

Under Federal Banking law, bank holding company (BHC) and financial holding company (FHC) systems are subject to consolidated prudential banking regulation including capital requirements and leverage ratios. In addition, companies that become subject to regulation as "systemically important financial institutions" ("SIFIs") will be subject to similar Fed regulation on a consolidated basis under Section 165 of Dodd-Frank. Since the subsidiaries of BHCs, FHCs and SIFIs will become subject to these requirements by virtue of the consolidated regulation, we request that the Commission clarify, either in the final rule or the related release that this carve-out should apply to (1) persons which are members of a BHC system or FHC system which is subject to regulation and capital requirements on a consolidated basis under federal banking law as well as (2) persons which are individually or as part of a consolidated group subject to regulation as SIFIs by the Federal Reserve under Title I of Dodd-Frank, [9]

Highly Leveraged. The Commission has adopted the approach of defining "highly leveraged" by suggesting two alternative simple balance sheet tests based on a GAAP ratio of liabilities to equity of either 8–1 or 15-1, the latter based on a threshold test used in Title I of Dodd-Frank, which would be applicable to bank holding companies or non-bank financial companies only if it determined that the company posed a "grave threat" to financial stability. The tests proposed, which are based on banking law considerations, simply do not work when applied to life insurance companies.

Life insurance companies are structurally and financially very different from banks. For example, life insurers are not vulnerable to the type of "run-on-the bank" scenario faced by commercial banks, with their significant exposure to withdrawal from demand deposits and other short term liabilities, since life insurers' liabilities to their policyholders tend to be longer and not easily liquidated. The length of life company liabilities makes for greater financial stability.

The life insurance industry is regulated by the various states based upon schemes of regulation which have been developed and refined over the past 100 or more years and have withstood the test of time and proved effective through periods of tremendous economic stress. Notably, despite the great size and national importance of the life insurance industry, Congress has chosen to respect this state regulatory approach and to rely upon each state's industry tailored regulation, rather than impose a single federal scheme of regulation. This regulation, in particular, addresses the solvency

[9] If thrift holding companies become subject to capital requirement and leverage ratios when they become subject to Federal Reserve oversight, they should receive the same treatment as we are proposing for BHCs, FHCs, and SIFIs.

of insurers, the adequacy of capital through the imposition of RBC requirements, and requires appropriate reserving for liabilities and prudent investment policy (including generally limitations on the prudent use of derivatives).

We note the remarks of the National Association of Insurance Commissioners in their comment letter dated February 18, 2011, pp. 7-8 regarding the appropriateness of the application of the proposed "highly leveraged" tests to state-regulated insurers, which points out that the proposed leverage tests do not fit insurer business models and could result in false positives for otherwise healthy and solvent insurers, and could even be counterproductive in some instances.

We do not believe that the policy of Congress expressed in Dodd-Frank would be well served by subjecting otherwise healthy, stable and non-risky life insurers, whose level of leverage and prudential regulation has proved appropriate to the conduct of their business and which meet insurance regulatory requirements, to an additional level of capital regulation based on a leverage standard that is inappropriate to their business model.

Finally, we are concerned that application of an inappropriate leverage standard to insurers, creating "false positives" under the third leg of the MSP test, could in effect make insurers, which are predominantly hedgers, unable to utilize the hedge exclusion under first part of the MSP test, under which a person's "substantial position" does not include hedging positions. This is because, if insurers are found to be "highly leveraged" under the third MSP test, their many hedge positions would be lumped with non-hedging positions (if any) in calculating of a substantial position under leg 3 of the rule. This unintended effect on insurers, notwithstanding that they are well capitalized, regulated and stable, is hardly what Congress intended when it set up the "highly leveraged" test, to bring hedge funds (the type of entities typically referred to as "highly leveraged institutions" in the banking literature)[10] under regulation.

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[10]See for example, the following discussion from the BIS: "In its previous work on HLIs the Basel Committee outlined the following characteristics of such institutions: (i) they are subject to very little or no direct regulatory oversight. In the case of HLIs, this limited regulatory oversight results from such entities being structured as limited partnerships, investors being either institutions or sophisticated high net worth individuals and the securities issued taking the form of private placements. Moreover, a significant proportion of HLIs operate through offshore financial centres. (ii) HLIs are generally subject to very limited disclosure requirements, compared with regulated financial institutions and/or publicly traded companies, and are not subject to rating by credit-rating agencies. (iii) such institutions often take on significant leverage, where leverage is the ratio between risk, expressed in some common denominator, and capital. IOSCO, for the purposes of its report used a similar classification. It was recognised at the time of those reports that 'highly leveraged institution' was not an ideal characterisation of all of the unregulated counterparties with which they were concerned. This remains the case but the term HLI has been retained in this report for continuity" , Bank of International Settlements, Review of issues relating to Highly Leveraged Institutions, March 2001. http://www.bis.org/publ/bcbs79.htm It appears that a definition could be developed which captures the non-public, non-transparent and often lightly capitalized nature of these investment vehicles. In any event, it does not appear that either public companies or regulated insurers which file publicly available annual and quarterly financial statements should be included in such a category.

Accordingly, MetLife suggests that the Commission either:

(1) specifically deem not be "highly leveraged" entities which are subject to prudential regulation and a RBC regime under regulatory requirements (including under state insurance law) other than the bank capital requirements referenced in the statutory MSP definition (or in the alternative, establish a RBC level to be determined which life insurers could satisfy to avoid application of the highly leveraged test);
(2) revert to a qualitative definition which is targeted explicitly at currently unregulated hedge fund vehicles; or
(3) set its GAAP "highly leveraged" standard at a higher and more refined level; to be determined in light of the business specific needs of different industries,

Implementation Period. MetLife believes that two months is a wholly inadequate period for a new MSP registrant to come into full compliance with applicable Dodd-Frank compliance rules. Significant IT builds, investments in personnel and development of compliance documentation and processes will be required to achieve full compliance. MetLife believes that one year would be an adequate period for a new MSP to come into full compliance with the rules.

<u>Application of Major Participant Definitions to Managed Funds, Positions of Separate Accounts and Affiliated Entities.</u>

Managed Funds. MetLife concurs with the Commission's preliminary determination that

> "the major participant definitions should not be construed to aggregate the accounts managed by asset managers or investment advisors to determine whether the asset manager or investment advisor itself is a major participant. The major participant definitions apply to entities that actually 'maintain' substantial positions in swaps and security-based swaps or that have swaps ... that create substantial counterparty exposure." Release, p. 80201.

Insurance Company Separate Accounts. In connection with the operation of the Proposed Rules, MetLife seeks confirmation of its view that segregated life insurance company separate account assets should not be aggregated with the life insurance company general account assets, nor should separate account derivatives transactions attributed to the life insurance company carrying the separate account in administering the Proposed Rules.

A life insurance company separate account is not a separate legal entity. However, life insurance companies frequently will establish separate accounts, as permitted by state insurance law, in connection with the issuance of certain annuities and life insurance policies. While there are numerous variations in the types and characteristics of separate accounts, generally speaking, in a separate account (i) specific assets back specific liabilities to policyholders; (ii) because assets are segregated, the performance of those assets (both positive and negative) is passed through directly to the policyholder; (iii) the assets of a separate account are insulated from the claims of general creditors in the event of an insolvency of the insurance company.

As a result, the legal status of separate account assets is quite different from that of the life insurer's general account assets. In general, the income, gains and losses of the assets of one separate account are insulated from the income, gains and losses of the insurer's general account assets and of the assets of other separate accounts. In addition, the assets of a separate account are not chargeable with liabilities arising out of the insurer's other business, including general account liabilities and liabilities of other separate accounts.

Consistent with the insulated treatment afforded under state separate account and insolvency law, as a rule, MetLife's ISDA agreements and futures customer agreements for our U.S. life insurance company separate accounts are entered into on behalf of identified separate accounts and expressly limit recourse of the dealers and FCMs to the separate account assets, without any guaranty or set off rights *vis a vis* any other separate account assets, any third party investment manager or the life insurer's general account assets.

Further, we note that CFTC rules have long recognized the distinct existence of insurers' separate accounts. Specifically in CFTC Rule §4.5, which excludes certain sponsors of collective investment funds from commodity pool operation treatment, there is a unambiguous bifurcation between the insurer, which could, absent the exclusionary provisions of Rule §4.5, theoretically be regarded as a commodity pool operator and its separate account. Rule §4.5 clearly treats the separate account as a distinct account based upon the segregation of separate account losses and gains from those of the insurance company "qualifying entity" separate from the insurers (see in particular Rule §§ 4.5(a)(2) and (b)(2)).

Accordingly, we believe that absent other factors, separate account assets should not be aggregated with the general account assets or with other separate accounts of life insurers for purpose of application of the Proposed Rules and that their separate status under the relevant insurance law and market practice should be respected.

Aggregation of Affiliated Company Swap Positions. In the Release (pp 80201-2), the Commission takes the tentative interpretive view, not expressly stated in the Proposed Rules, that, in the case where a parent is the majority owner of a subsidiary entity, " the major swap participant tests may appropriately aggregate the subsidiary's swaps at the parent for the purpose of the substantial position analyses." This view is stated to be upon the basis that the parent receives the benefit of the subsidiary transactions, as well as a concern that an entity could seek to evade MSP status by allocating swaps around in multiple entities in an enterprise.

MetLife submits that it is not appropriate to require aggregation of subsidiaries' swaps at the parent level unless the parent is providing a guarantee or credit support for the subsidiaries' obligations. Risk should properly be measured at the level of the entity or entities incurring the risk, and the regulations should respect the legal and economic terms on which the swap was executed.

The effect of the Proposed Rule under the Commission's interpretation would be that all of the companies in a consolidated corporate group would be aggregated upward and treated for

purposes of MSP regulation as a single person, notwithstanding that they are separate legal entities (separate "persons"), who contract independently and without credit support with counterparties and who may be subject to separate and different regulatory schemes which render them unable to flow funds freely upstream or to enter into transactions for benefit of affiliates except at arm's length.

For example, MetLife Inc. is a financial holding company, with a holding company structure including both domestic and offshore insurance subsidiaries, and a national bank. Each of our operating subsidiaries is subject to its own regulation under the law of its jurisdiction of formation, including limits on inter-corporate transactions with affiliates, its own business plan and, in many cases strict limitations on its ability to upstream assets to its parent. Each of our entities engages in derivatives under its own ISDA master agreements and futures clearing agreements and most conduct their derivatives activities on a stand-alone basis, without guarantees or credit supports from a parent company and without cross affiliate netting. The type of regulatory re-characterization that the Commission would require is wholly inconsistent with this rigid legal and contractual structure. Absent evidence to the contrary, we believe that the rules as adopted should recognize that complex business corporate organizations which are structured in multiple entities, are so structured for valid substantive business reasons unrelated to their derivatives trading activity.

Second, the Commission's interpretation is flatly contrary to the definition of "person" in Section 1a(38) of the CEA, as amended by Dodd-Frank, which sets forth the standard definition of a juridical person as including "individuals, associations, partnerships, corporations and trusts" without any reference to special treatment of subsidiaries. The definitions of "person" in the Securities Act of 1933 (Section 2(2)) and the Securities and Exchange Commission Act of 1934 (Section 3(a)(9)) are in critical point similar, that is, they recognize a company or other juridical or statutory entity as a separate person and do not support conflation with subsidiaries. Further, we note that the term "person" is embedded in the statutory definition of MSP; "the term major swap participant means ***any person*** [emphasis added] who is not a swap dealer" and meets one of the three statutory tests.

Finally, the Commission's position creates enormous potential complexity where international organizations are involved, potentially pulling into the regulatory scheme entities with no or limited involvement in U.S. markets and disparate regulatory schemes.

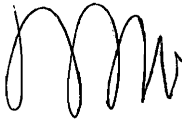
In our view, the natural and statutory definition of "person" as a discrete juridical person should be followed and respected in the rule framework, with a presumption that an entity that operates and is accepted in the financial market as a separate credit entity, without guaranty or credit support from its parent, owner or other affiliated person, is an appropriate registrant for MSP purposes. In the event that a guarantor or credit support provider is present, it could be appropriate to aggregate the positions of the guaranteed subsidiary or affiliate at the guarantor level. To preserve flexibility, we believe that two or more members of a consolidated corporate group should have the option to

determine that it is appropriate to aggregate their Swap positions and make a single MSP filing at the parent level or to make individual filings and comply individually.

* * *

MetLife is pleased to be able to continue to participate through the comment process in the framing of this critical new regulatory framework. Please feel free to contact either of us at our email addresses above if you have any questions regarding this comment letter.

Respectfully,



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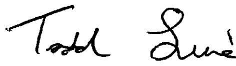
Associate General Counsel



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September 20. 2010

Via E-Mail
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Re: MetLife Comment on Core Definitions in Title VII of the Dodd-Frank Act; CFTC Release No. 34-62717; SEC File No. S7-16-10

Dear Mr. Stawick and Ms. Murphy:

We welcome the opportunity to offer our preliminary conceptual comments on the core definition of "major swap participant" in connection with your proposed rulemaking under Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd Frank"). The appropriate policy resolution of the issues posed as the Commodity Futures Trading Commission ("CFTC"), Securities Exchange Commission ("SEC") (collectively, "Commission") as well as the federal banking regulators is of critical importance to the U.S. economy at large and to those financial firms, such as MetLife, Inc. ("MetLife"), potentially affected and their stakeholders.

For ease of reference, this letter refers to the sections of Dodd Frank amending the Commodity Exchange Act ("CEA"), the defined terms thereunder and the rules to be adopted by the CFTC thereunder, but the discussion is intended to relate equally to the parallel regulation by the SEC contemplated under equivalent amendments to the Securities Exchange Act of 1934.

MetLife Background.

Business. MetLife has been in the business of providing insurance for over 140 years, and is a leading provider of insurance, employee benefits and financial services with operations throughout the United States and the Latin America, Europe and Asia Pacific regions. Through its subsidiaries and affiliates, MetLife, Inc. reaches more than 70 million customers around the world and its financial products and services are offered to over 90 of the top 100 FORTUNE 500® companies. MetLife is the largest life insurer in the United States (based on life insurance in-force). The MetLife companies offer life insurance, annuities, auto and home insurance, retail banking and other financial services to individuals, as well as group insurance and retirement and

savings products and services to corporations and other institutions. MetLife's products and services are offered globally, through agents, third-party distributors such as banks and brokers, and direct marketing channels.

Regulation. MetLife's largest insurance company, Metropolitan Life Insurance Company, is licensed to transact insurance business in, and is subject to regulation and supervision by, all 50 states, the District of Columbia, Guam, Puerto Rico, Canada, the U.S. Virgin Islands and Northern Mariana Islands. Each of MetLife's insurance subsidiaries is licensed and regulated in each U.S. and international jurisdiction in which it conducts business.

In the U.S., state insurance laws and regulations govern the financial aspects of the insurance business, including standards of solvency, statutory reserves, reinsurance and capital adequacy, and the business conduct of insurers. Each insurance subsidiary is required to file reports, generally including detailed annual financial statements, with insurance regulatory authorities in each of the jurisdictions in which it does business, and its operations and accounts are subject to periodic examination by such authorities. Each of the Company's U.S. insurance subsidiaries is subject to risk-based capital (RBC) requirements, and reports its RBC based on a formula calculated by applying factors to various asset, premium and statutory reserve items, as well as taking into account the risk characteristics of the insurer. The major categories of risk involved are asset risk, insurance risk, interest rate risk, market risk and business risk. The formula is used as an early warning regulatory tool to identify possible inadequately capitalized insurers for purposes of initiating regulatory action, and not as a means to rank insurers generally. State insurance laws provide insurance regulators the authority to require various actions by, or take various actions against, insurers whose RBC ratio does not meet or exceed certain RBC levels.

The insurance contracts written by MetLife in the U.S. are generally subject to prior filing with and approval by state insurance regulators, as well as to rate regulation in some contexts.

The investments of each of the Company's U.S. insurance subsidiaries which back our contractual liabilities are subject to regulation under relevant state insurance laws that require diversification of the insurers' investment portfolios and limit the amount of investments in certain asset categories. The state regulation applicable to MetLife generally limits our U.S. insurers' use of derivatives to hedging, asset replication and limited writing of covered calls.

As a result of its ownership of MetLife Bank, NA, a federally chartered commercial bank, MetLife, Inc. became subject to regulation as a bank holding company and financial holding company on February 28, 2001. As such, it is subject to regulation under the Bank Holding Company Act of 1956 and to inspection, examination, and supervision by the Board of Governors of the Federal Reserve Bank of New York. MetLife, Inc. and MetLife Bank are subject to risk–based and leverage capital guidelines issued by the federal banking regulatory agencies for banks and financial holding companies. The federal banking regulatory agencies are required by law to take specific prompt corrective actions with respect to institutions that do not meet minimum capital standards. At December 31, 2009, MetLife, Inc. and MetLife Bank were in compliance with the aforementioned guidelines.

General

The version of Title VII of Dodd Frank enacted by Congress reoriented the new swap regulatory regime for financial market end users, by separating mandatory clearing and transparency requirements from the new regulatory scheme relating to Major Swap Participants (MSPs).

Under Section 723 of Title VII (new Section 2(c)(1)(h) of the CEA), all financial entities, other than those smaller institutions which may be exempted by the Commission, will be required to clear their non-customized swap trades through a derivatives clearing organization ("DCO") rather than trading bilaterally as before. This requirement will apply whether or not the financial entities are MSPs or Swap Dealers and whether or not they are engaging in hedging activity.[1] In addition, the trading of financial end-users, both cleared and uncleared, will be subject to transaction reporting and consequent regulatory oversight under the new real-time public reporting requirements under Section 727 of Dodd Frank (new Section 2(a)(13) of the CEA).

The adopted statutory structure clarifies that the policy mandate under the MSP provisions is to identify and appropriately regulate that category of market end users whose swap activities pose a systemic risk to the market and the broader economy. Such end-users are to be designated as "major swap participants" subject to business conduct regulation, capital requirements and margin requirements for their non-cleared swaps. MetLife submits that there is now no practical need for the Commission to designate financial end users as MSPs in order to bring their trades into a cleared environment or to obtain transparency with respect to their trading activity.

The MSP Provision. Under Section 721(a)(2) of Dodd Frank (new Section 1a (33) of the CEA) there are three alternative ways for a non-dealer to be characterized as a major swap participant. The person must be **either**:

(1) a person who maintains a "substantial position" in any major swap category, **excluding** positions held for "hedging or mitigating" "commercial risk" or the positions of a pension plan held for the primary purpose of hedging or mitigating any risk directly associated with the operation of the plan (a "Category 1" MSP) ; **or**

(2) a person whose outstanding swaps (whether or not for hedging) create "substantial counterparty exposure" that could have serious adverse effects on the financial stability of the United States banking system or financial markets (a "Category 2" MSP); **or**

(3) a financial entity that is "highly leveraged relative to the amount of capital it holds" , is not subject to capital requirements established by an appropriate federal banking agency **and** has a "substantial position" (whether or not for hedging) of swaps in any major swap category (a "Category 3" MSP).

[1] We note that during the course of the legislative debate over financial reform, the Chairman of the CFTC advocated strongly for the mandatory clearing of financial institutions trading volume, due to size of their participation in the over-the-counter derivatives markets. This policy recommendation was reflected in the final legislation.

"Substantial position" as used in Category 1 and Category 3 is to be defined at a "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 U.S. financial system. In setting the definition, the Commission must consider whether the contract is cleared or uncleared, and may take into consideration the value and quality of collateral held against counterparty exposures"

Regarding these criteria for regulation in the context of Dodd Frank, we have four initial observations before addressing the specifics of the definitions.

1. For each MSP Category, a determination of whether an end-user's swap positions are of a magnitude to pose a risk to the U.S. banking system or financial system is key to the regulatory decision as whether to regulate that end-user as an MSP. This focus, which is on the risk posed by the person's derivative positions, as a "substantial position" under Category 1 or Category 3 or as "substantial counterparty exposure" under Category 2, is to be distinguished from the identification, under Title I of Dodd Frank, of systemically important companies. Under Dodd Frank, an entity or enterprise subject to regulation as systematically important under Title I may nevertheless not be required to be regulated under Title VII, since its derivatives positions may not be sufficiently sizeable or risky to meet the Title VII criteria.

2. Congress has recognized clearing and collateralization as risk mitigants and potential offsetting factors in the risk determination. Quantitative thresholds established for determining what is a "substantial position" and what constitutes "substantial counterparty risk" should therefore be at levels at which such systemic risk is likely to be present as the result of the bankruptcy or failure to perform of a market end-user (for example through causing the failure of a major dealer, DCO or clearing member), taking into consideration the risk mitigation benefits of netting, collateral, and clearing.

3. Congress generally recognized that the use of swaps to manage business risk is socially beneficial and potentially not generative of systemic risk, through the carve-outs from the "substantial position" definition in Category 1 as well as in the commercial end-user hedging exclusion from mandatory clearing. The "commercial risk" and hedging and risk mitigation concepts should accordingly be given an appropriately broad definition under Category 1 of the MSP definition.

4. Dodd Frank does not mandate imposing a duplicate scheme of capital, margin and other prudential regulation upon entities already subject to market appropriate capital and trading restrictions and regulation.

The following analysis discusses each of the relevant statutory provisions of the MSP definition and suggests how the definitions could appropriately implement the purpose of Title VII.

Discussion of MSP Elements

Category 1 – Exclusion of positions held for "hedging or mitigating commercial risk". The legislative history of Dodd Frank shows that the use of derivatives to hedge or mitigate business risks is beneficial and should not be inappropriately limited or penalized under the legislation.[2] The inclusion of Category 1 indicates that Congress did not intend businesses managing their risk to be subjected to regulation as MSPs absent other indicia of risk from their derivatives activity. Thus Category 1 requires that a person must have a "substantial position" in any swap category, *"excluding positions held for hedging or mitigating commercial risk,"* for MSP status under that Category to arise.

The logical starting point for defining a Category 1 hedge under the CEA would be the definition of bona fide hedging in Reg. 1.3(z)[3] and the CFTC's history of interpretation of that rule. By its very terms, Reg. 1.3(z) requires that hedging transactions be "economically appropriate to the reduction of risks in the conduct and management *of a commercial enterprise*" *[emphasis added]*. The CFTC has flexibly applied this terminology over time to reflect development of the commodity markets from a predominantly agricultural market in physical commodities to a market in which financial exposures are hedged and managed by a wide range of market users, including financial businesses.[4] From the CFTC record it is clear that "hedging" through use of futures has

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[2] In a July 15, 2020, colloquy between Senator Dodd, Chairman of the Senate Banking Committee and Senator Lincoln, Chair of the Senate Agriculture, Nutrition and Forestry Committee states that:

> "It is also important to note that few end users will be major swap participants, as we have excluded ''positions held for hedging or mitigating commercial risk'' from being considered as a ''substantial position'' under that definition....
>
> It is also the intent of this bill to distinguish between commercial end users hedging their risk and larger, riskier market participants. Regulators should distinguish between these types of companies when implementing new regulatory requirements."

[3] "Reg. 1.3 (z) ***Bona fide hedging transactions and positions*** **(1)** ***General definition***. Bona fide hedging transactions and positions shall mean transactions or positions in a contract for future delivery on any contract market, or in a commodity option, where such transactions or positions normally represent a substitute for transactions to be made or positions to be taken at a later time in a physical marketing channel, and ***where they are economically appropriate to the reduction of risks in the conduct and management of a commercial enterprise [emphasis added]***, and where they arise from:
(i) The potential change in the value of assets which a person owns, produces, manufactures, processes, or merchandises or anticipates owning, producing, manufacturing, processing, or merchandising,
(ii) The potential change in the value of liabilities which a person owns or anticipates incurring, or
(iii) The potential change in the value of services which a person provides, purchases, or anticipates providing or purchasing ....
(3) ***Non-enumerated cases***. Upon specific request made in accordance with §1.47 of the regulations, the Commission may recognize transactions and positions other than those enumerated in paragraph (z)(2) of this section as bona fide hedging in such amount and under such terms and conditions as it may specify in accordance with the provisions of §1.47. . ."

[4] For general background, see "The CFTC's Hedging Definition – Development and Current Issues" by Blake Imel, Ronald Hobson and Paula Tosini, November 1985 ("CFTC Hedging Paper"); and the Hedging Definition and

been viewed by the CFTC as well as Congress as an activity that can validly be conducted by financial businesses.[5]

It follows that for purposes of Category 1, the term "commercial risk" should be defined to include the risks of financial as well as non-financial businesses. CFTC Reg. 1.3(z). is a flexible notion, linked to the development of futures markets and their use to hedge business risk. [6] Given the CFTCs history of treating financial business as "commercial enterprises" and hedgers under the CEA with respect to their activities in the regulated futures markets, it would be incongruous for the CFTC to conclude that the same activities, conducted over the counter, are not commercial. [7]

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the Use of Financial Futures and Options: Problems and Recommendations for Reform," Report of the Financial Products Advisory Committee of the Commodity Futures Trading Commission, June 1987. For specific instances of the applicability of the hedging exemption to financial entities, see, e.g., CFTC Interpretive Letters 94- 21, January 24, 1994 (CPO exemption granted to private investment limited partnership), 95-27 (CPO exemption granted for real estate fund hedging interest rate risk with financial futures), 97-30, April 21,1997 (CBOE market maker hedging its positions in the futures market) and other letters issued pursuant to request under Reg. 1.47 and 1.3(z)(3).

Under CFTC Reg. 4.5, certain financial entities which operated pooled investments may obtain exemption from CPO status. This exemption expressly includes, among a limited group, insurance companies with respect to futures activity conducted in their separate accounts. The exemption for some time required insurance companies claiming exclusion from regulation as CPOs to make representations with respect to the status of the separate account futures activity as "bona fide hedges" within the meaning of Reg. 1.3(z). It is noteworthy that the CFTC was directed to create this exemption, including the limitation that the futures be used by the excluded entity solely for hedging purposes, by the Senate Committee on Agriculture, Nutrition, and Forestry in the Committee Report relating to the 1982 amendments to the Commodity Exchange Act ("CEA") See S.Rep No. 384, 97th Cong., 2d Sess. 80 (1982) , quoted at pp. 27-28 of the CFTC Hedging Paper.

Other contexts under the CEA where hedging treatment has been relevant to financial firms include the use of the hedge definition for FCM net capital requirements (where hedged positions are subject to lower haircuts) and hedge exemptions from speculative limits on futures exchanges, for which financial institutions are eligible, as to which financial businesses routinely make hedge representations.

[5] The codification of the Rule 1.3(z) definition in Section 737(c) of Dodd Frank (CEA Section 4(c)(2)) does not appear to alter the situation. We believe that insurer hedging activity should continue to be regarded as bona fide hedging under this section as well, to the extent applicable.

[6] The CFTC's own website Glossary defines "commercial" as "an entity involved in the production, processing or merchandising of a commodity". Under the CEA, the term "commodity" is defined to include, in addition to a long list of physical commodities (excluding onions but now including movie rights) other goods and articles, ***and "all services, rights and interests in which contracts for future delivery are presently or in the future dealt in" (emphasis added)***, Given that a wide list of financial interests including bonds, interest rates, foreign currency, equity and debt indexes and credit characteristics are now the subject of contracts traded in the regulated futures markets, entities that trade and use these financial interests in their business are clearly "commercial" within the CFTC definition.

[7] A more recent document is further indicative that the CFTC has not viewed the term "commercial" in a way that would exclude financial end-users. In a preliminary release relating to the most recent restructuring of the CFTC's COT or "commitments of traders" report, the CFTC observed that the distinction between commercial and

From an economic standpoint, insurers and other financial service businesses, such as MetLife, are commercial enterprises, indistinguishable as to the hedging of their business risks from industrial, merchandising and other business organizations which might claim the hedge exclusion. Insurers create commercial financial products (insurance contracts or policies) which are sold to individual consumers, pension plans and other customers through a wide range of marketing channels across the country and globally. An insurer uses derivatives, whether swaps or traditional exchange traded futures, to reduce and manage risks associated with these contractual obligations, as well as risks related to its investment portfolio backing its insurance liabilities, the relation of its assets to its liabilities, and foreign currency risks relating to foreign investments and operations. Insurer usage is fundamentally the same as that of any non-financial business enterprise (be it an automaker or an integrated global oil company) which offers products and services, in commerce, to retail and institutional markets and hedges its requirements, commitments and exposures arising out of that business in the derivatives markets.

The structure of the so-called commercial end-user exemption from mandatory clearing under new CEA Section 2(c)(1)(h)(7) also supports our position. That exemption has two relevant requirements, first, that the entity claiming the exemption be hedging or mitigating "commercial risk" and second, that the entity not be a financial entity. The addition of the second element reveals Congress's view that financial end users have commercial risks relating to their lines of business that they might hedge.

Moreover, we submit that Congress's use of "hedging and mitigating" commercial risk language in Category 1 indicates that Congress intends that an expansive view to be taken of the hedge exclusion. If Congress had intended a narrow definition it would have either used the term "hedging" alone or utilized the "bona fide hedging" definition of CFTC Reg. 1.3(z) or Dodd Frank Section 737(c). That fact that Congress did not do so and in fact added the words "and mitigating" plainly indicates that this exclusion intends an expansive definition of hedging and can also encompass non-speculative derivatives positions used to manage economic risk, including potentially diversification and synthetic asset strategies, such as the conservative "replication" strategy permitted under state insurance laws.

Finally, MetLife urges the Commission to take into consideration the special, pervasive regulatory scheme applicable to insurance companies such as those in the MetLife group. In particular, we submit that our regulation limits the nature and quantity of the risks we can take through the use of derivatives, through limitations on both the type and quantity of our derivatives positions, and that such uses must relate specifically to our regulated insurance business. Thus, the positions taken by insurers to hedge or mitigate risk should be included under the Category 1

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non-commercial was, in usage in their reporting structure, essentially equivalent to the distinction between hedging and speculation, In this context, it appears that the term "commercial" refers to a connection between the transactions and a business conducted by a person (i.e. commercial trades or hedges) whereas the term "speculation" (non-commercial") is unconnected to the needs of a business enterprise. In any event the "commercial" terminology did not distinguish between types of business enterprises. CFTC Notice of Comprehensive Review of the Commitments of Traders Reporting Program, 71 FR 35627 (June 21, 2006)

hedge exclusion.[8]

Category 1 and 3 - "Substantial Position". This threshold is intended to quantify swap positions which are themselves systemically risky, in that they could "significantly impact the financial system of the United States". The types of systemic impacts which might be caused in this context would most likely arise if an end-user failed to meet its obligations, causing the failure of a DCO, major clearing member or systemically important swap dealer. As such, we submit that the "substantial position" limit should be set based on appropriate considerations of possible systemic risk effects of the derivative positions.

Consequently, we urge that "substantial position" not be calculated on a notional or gross basis. Notional and gross position sizes are not a good indicator of the systemic risk posed by swap positions, given the prevalence of contractual netting arrangements and other risk mitigants. The "substantial position" definition should thus be based on appropriate exposure concepts and measurement methodology which take into consideration such factors as contractual netting and collateralization. International and U.S. financial regulators use such measures, and we suggest that methodology such as those adopted by the Bank of International Settlements in the Basel II accords would be most appropriate in this context. Such a risk measure would also accord with the methods market participants currently use in calculating exposures, including the contractual netting and collateralization arrangements employed.

In setting the definition for "substantial position" the Commission is directed to take into consideration the person's relative position in uncleared as opposed to cleared swaps. This is indicative that Congress intends exposure to cleared swaps to at least be considered in the context of the "substantial position" for MSP Categories 1 and 3, whereas clearing is not mentioned in the context of "substantial counterparty exposure" for Category 2. Given the statutory policy preference for clearing as a risk mitigant, it would be rational for the Commission to calculate "substantial position" in a manner that resulted in a lesser "charge" for cleared trades, perhaps even no charge.

Collateralization. The statute states that the Commission may take into consideration the value and quality of collateral held against counterparty exposures. MetLife believes that the Commission should treat collateral or margin provided by a party to its counterparty or a clearinghouse or exchange as reducing its exposure for purposes of the "substantial position" calculation, provided that the collateral is marked to market regularly, has a readily observable price, and is traded in a liquid market.

For financial institutions such as insurers, the continued ability to utilize high quality liquid securities such as investment grade corporate bonds and mortgage backed securities, in addition to cash, governments and agencies, as collateral for their swap transactions is a critical concern

[8] To the extent a distinction needs to be made, the insurance business is distinguishable to a great degree from the derivatives usage in pooled investment vehicles which offer a simple pass through (with or without the use of leverage) of investment fund performance to investors.

both in cleared and uncleared contexts. We recognize that appropriate haircuts would need to be developed and applied to some collateral securities both in the satisfaction of counterparty and exchange collateral/margin requirements and in application of the "substantial position" definition.

Category 2 - "Substantial Counterparty Exposure". MetLife submits that this term should also be defined in reference to systemic risk considerations and calculated in the same manner as "Substantial Exposure," that is, by giving effect to netting and collateral provided, but in this case excluding the exposure of regulated DCOs. This is because, in the OTC market, a counterparty exposure would normally derive from the creditworthiness of the bilateral party with which a person trades directly. Counterparty exposure is reduced when a person clears through a DCO. Category 2 of the MSP definition is intended to identify end-users (both hedging and speculative) whose swaps "create substantial counterparty exposure that could have serious adverse effects on the financial stability of the US banking system or financial markets".

In addition to a quantitative assessment of risk, the Commission might also seek to identify, for purposes of Category 2, qualitative factors which might bear on the riskiness of a person's arrangements with counterparties. Such factors might include the lack of standard market documentation, including master netting and collateral agreements or the type of very substantial "springing" collateral arrangements that were a major factor in the failure of AIG Financial Products Company.

Category 3 Criteria. A Category 3 MSP will be a financial entity which has "substantial positions", is "highly leveraged relative to the amount of capital it holds" and is not "subject to capital requirements established by an appropriate Federal banking authority". As with Category 2, MSP status may arise under this Category, whether or not the person engages in hedging. In this case, the primary additional factor of systemic risk identified as giving rise to MSP status is high leverage. While other types of financial entities may be operated in such a way as to pose this type of risk, the categories of entity normally identified as highly leveraged are unregulated investment vehicles such as hedge funds.

Highly Leveraged. We submit that the concept of "highly leveraged relative to the amount of capital it holds" should not be a mechanical concept but should relate to the types of risk potentially posed by a financial entity. Use of a simple balance sheet test or resort to the capital rules relevant to banks might be ultimately be determined to be workable. However, application of overly simplistic tests to diverse entities with different risk profiles might result in the regulatory net capturing an excessive number of non-systemically risky entities, burdening them with additional economic costs and constraints (including being commercially disadvantaged vis a vis competitors which are not MSPs) unjustified by any reasonable assessment of risk. We therefore urge careful development of this standard, supported by appropriate economic and financial analysis, including without limitation, review of leverage levels and standards prevailing in differing financial market sectors, and the risk posed by different business models and structures, to avoid such unintended consequences.

Subject To Capital Requirements Established By An Appropriate Federal Banking Authority. Entities subject to such requirements would not be treated as MSPs under Category 3. Thus, Congress has determined that any systemic risk posed by such entity's leverage is dealt with through application of a federal bank capital regime, in lieu of the MSP regulatory requirements. We submit that this carve-out should apply to (1) persons included in a bank holding company system which is subject to regulation and capital requirements on a consolidated basis under federal banking law as well as (2) persons which are individually or as part of a consolidated group subject to regulation (including potentially capital requirements) by the Federal Reserve under Title I of Dodd Frank, since the applicable federal banking requirements make regulation as MSPs under Category 3 unnecessary and burdensome.

Swap Dealer. While we are not commenting generally on the Swap Dealer definition, we believe that it should not be drawn to include companies that enter into derivatives only to aggregate or intermediate risk for their group companies and transact with third parties only in this limited capacity.

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The creation of a appropriate regulatory framework around the Title VII Dodd Frank provisions is of critical important to MetLife as an end-user of the over-the-counter derivatives markets. We are pleased to be afforded the opportunity to make this initial submission and look forward to continuing opportunities to participate as the rulemaking process proceeds. Please feel free to contact me at my email address above if you have any questions regarding this comment letter.

Respectfully

Jennifer J. Kalb