



July 11, 2011

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

Re: RIN 3038-AC97 – Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants

Dear Mr. Stawick:

The Committee on Investment of Employee Benefit Assets ("CIEBA") and the American Benefits Council (the "Council") appreciate this opportunity to provide comments to the Commodity Futures Trading Commission ("CFTC") regarding the CFTC's proposed rulemaking entitled "Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants" (the "Proposed Rules") under the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") and the Commodity Exchange Act ("CEA").¹ The Proposed Rules would require Swap Dealers ("SDs") and Major Swap Participants ("MSPs") that are not regulated by a Prudential Regulator² (collectively, "Covered Swap Entities" or "CSEs") to collect margin for certain uncleared swaps.

Concurrently with this letter, we are submitting a comment letter to the Prudential Regulators with respect to their corollary proposal. Due to the numerous similarities between the CFTC's Proposed Rules and the Prudential Regulators' proposal, we incorporate by reference our comment letter to the Prudential Regulators (included as an attachment to this letter) and provide herein two additional comments that are unique to the CFTC's Proposed Rules.

¹ 76 Fed. Reg. 27,621 (May 12, 2011).

² The Prudential Regulators are the Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Farm Credit Administration, and the Federal Housing Finance Agency.

BACKGROUND

CIEBA represents more than 100 of the country's largest pension funds. Its members manage more than \$1 trillion of defined benefit and defined contribution plan assets on behalf of 15 million plan participants and beneficiaries. CIEBA members are the senior corporate financial officers who manage and administer corporate retirement plan assets governed by the Employee Retirement Income Security Act of 1974 ("ERISA"). CIEBA's recent annual survey of members showed an increased emphasis on managing and reducing plan risks and a corresponding increase in usage of swaps to address those risks.

The Council is a public policy organization principally representing Fortune 500 companies and other organizations that assist employers of all sizes in providing benefits to employees. Collectively, the Council's members either sponsor directly or provide services to retirement and health plans that cover more than 100 million Americans.

SUMMARY

We support the CFTC's goals of protecting CSEs and protecting the financial system from systemic risk. Imposing margin requirements in appropriate circumstances will help toward achieving that goal.

However, requiring margin even where parties have limited swap exposure and use swaps primarily for hedging will unnecessarily increase the cost of hedging for many market participants (and make hedging too expensive altogether for some), without providing a measurable benefit to the stability of the U.S. financial system. Many market participants may be left with few options and effectively be precluded from hedging and mitigating risks, such as funding risk for ERISA plans, if margin requirements are unnecessarily strict.

Should the CFTC nonetheless proceed with its broadly crafted proposed margin requirements, we believe the CFTC should take a more permissive approach in allowing financial entities, ERISA plans in particular, to be eligible for margin thresholds for uncleared swaps (credit exposures below which margin is not required). A discussion of ERISA plans' need for and use of uncleared swaps as well as our suggestions for appropriate ways to narrow initial margin requirements with respect to ERISA plans are detailed in the attached letter to the Prudential Regulators. In addition, we ask the CFTC to consider the following two suggestions:

1. The CFTC's alternative approach to calculating initial margin by reference to a similar cleared contract will likely be unworkable and substantially overstate the risk associated with uncleared swaps.
2. The CFTC should phase-in uncleared swap margin requirements only after the clearing system is in place.

These issues are of great importance to our members, to the workers and retirees relying on the ERISA plans, and to the economy. We look forward to working with the CFTC to ensure that the new rules strengthen financial regulations in a manner that enhances retirement security. It is critical that the new rules not be developed in a way that weakens such security.

1. **The Alternative Approach To Calculate Initial Margin By Reference To a Similar Cleared Contract Will Be Unworkable And Overstate The Risks Associated With Uncleared Swaps**

The Proposed Rules would permit CSEs to calculate initial margin in one of two ways: 1) subject to CFTC approval, using an initial margin model that is currently used by a registered Derivatives Clearing Organization ("DCO"), currently used by an entity subject to regular assessment by a Prudential Regulator, or made available for licensing to any market participant by a vendor; or 2) calculating initial margin by identifying a similar cleared swap or cleared futures contracts and multiplying the initial margin that would be required by the DCO for the similar contract by a constant multiplier called a margin multiple. Under the alternative approach, the margin multiples would be 2.0 for a similar cleared swap or 4.4 for a similar cleared futures contract.

The alternative approach will likely prove to be unworkable and substantially overstate the risk of many uncleared swaps. CSEs will likely have a difficult time identifying a "similar" cleared swap or futures contract. As a general matter, a main reason that an uncleared swap will not be cleared is because it is not similar to a cleared product. Even if a CSE identifies a cleared contract that it could consider "similar" to the uncleared swap, it is likely that there would be room for reasonable disagreement either between the parties or between the parties and the CFTC.

Even if an uncleared swap is "similar" to a cleared contract, it is difficult to understand why the CFTC would require double the margin of the similar cleared swap and require 4.4 times the margin of the similar cleared futures contract. The CFTC determined the multiples by assuming a longer liquidation period than is used to calculate the margin for cleared swaps and cleared futures, and, for comparisons to cleared futures contracts, applying an additional 40 percent "cushion."³ The CFTC does not offer, nor does there seem to be any reason why uncleared swaps and "similar" cleared contracts would have such drastically different liquidation periods -- twice as long as similar cleared swaps and 10 times as long as similar cleared futures contracts.

Notably, part of the "cushion" included in the multiple applied to a similar futures contract is intended "to reflect that a 10-day period may be insufficient for some customized products."⁴ Although the CFTC correctly recognizes that the actual liquidation period for particular swaps or categories of swaps will not be the same, the

³ Proposed Rule at 23,738.

⁴ *Id.*

Proposed Rules do not acknowledge that a period shorter than 10 days might also be appropriate.

We ask the CFTC to abandon the 10-day liquidation period for determining the multiples. Instead, as discussed in our letter to the Prudential Regulators, we ask that the CFTC use a 3 to 5 day liquidation period. In the event the CFTC decides to keep its general approach, we ask that the CFTC eliminate the arbitrary 40 percent "cushion" included in the 4.4 multiple for similar cleared futures contracts, which multiple already assumes a liquidation period that is ten times longer than a cleared futures contract.

2. Uncleared Swap Margin Requirements Should Only Take Effect After The Clearing System Is In Place

The CFTC has indicated that it intends to phase in the new Dodd-Frank rules. The CFTC has not issued guidance as to how it intends to phase in these requirements. As discussed, the uncleared swap margin requirements will impose higher margin requirements than those applicable for cleared swaps. If uncleared swap margin requirements take effect prior to clearing requirements, entities that would like to use cleared swaps will have no option but to pay the higher margin requirements under the uncleared swap rules until clearing requirements are in place. Further exacerbating this problem, CSEs not relying on an initial margin model would only be able to calculate initial margin by applying the 4.4 times multiple (which includes a 40 percent "cushion") to the margin required for the "most similar" cleared *futures* contract, because there would be no cleared swaps to use for comparison.

The CFTC must avoid this result. It is imperative that the CFTC delay implementation of the uncleared swap margin rules to coordinate with the clearing system. We ask for a delay of at least 180 days after the clearing rules take effect. Should the CFTC decide otherwise, it will need to provide transparent transition rules designed to impose margin requirements on uncleared swaps similar to those that will be imposed on cleared swaps (at least for liquid swaps that are likely to be cleared).

* * * *

We appreciate your consideration of our views.

Committee on Investment of Employee Benefit Assets

American Benefits Council

cc: The Office of the Comptroller of the Currency
The Board of Governors of the Federal Reserve System
Federal Deposit Insurance Corporation
Farm Credit Administration
The Federal Housing Finance Agency

ATTACHMENT

Comment Letter From CIEBA and ABC to the Prudential Regulators
Margin and Capital Requirements for Covered Swap Entities



The Committee on Investment
of Employee Benefit Assets



AMERICAN BENEFITS
COUNCIL

July 11, 2011

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Re: Comments on Proposed Rules Related to Margin for Uncleared Swaps
Board: Margin and Capital Requirements for Covered Swap Entities
[Docket No. R-1415] (RIN 7100 AD74)
FCA: Margin and Capital Requirements for Covered Swap Entities
(RIN 3052-AC69)
FDIC: Margin and Capital Requirements for Covered Swap Entities
(RIN 3064-AD79)
FHFA: Margin and Capital Requirements for Covered Swap Entities
(RIN 2590-AA45)
OCC: Margin and Capital Requirements for Covered Swap Entities
[Docket No. OCC-2011-0008] (RIN 1557-AD43)

The Committee on Investment of Employee Benefit Assets (“CIEBA”) and the American Benefits Council (the “Council”) appreciate this opportunity to provide comments to the joint notice of proposed rulemaking entitled “Margin and Capital Requirements for Covered Swap Entities” (the “Proposed Rules”) under the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”) by the Office of the

Comptroller of the Currency (“OCC”), Board of Governors of the Federal Reserve System (“Board”), Federal Deposit Insurance Corporation (“FDIC”), Farm Credit Administration (“FCA”), and the Federal Housing Finance Agency (“FHFA”) (each, an “Agency” and, collectively, the “Agencies”).¹ The Proposed Rules would require Swap Dealers (“SDs”), Security-Based Swap Dealers (“SBSDs”), Major Swap Participants (“MSPs”), and Major Security-Based Swap Participants (“MSSPs”) regulated by one of the Agencies (“CSEs”) to collect margin for all non-cleared swaps and security-based swaps.²

CIEBA represents more than 100 of the country’s largest corporate sponsored defined benefit pension funds. Its members manage more than \$1 trillion of defined benefit and defined contribution plan assets on behalf of 15 million plan participants and beneficiaries. CIEBA members are the senior corporate financial officers who manage and administer corporate retirement plan assets governed by the Employee Retirement Income Security Act of 1974 (“ERISA”). CIEBA’s recent annual survey of members showed an increased emphasis on managing and reducing plan risks and a corresponding increase in usage of swaps to address those risks.

The Council is a public policy organization principally representing Fortune 500 companies and other organizations that assist employers of all sizes in providing benefits to employees. Collectively, the Council’s members either sponsor directly or provide services to retirement and health plans that cover more than 100 million Americans.

SUMMARY

Swaps play a critical role for our members’ plans. ERISA plans use swaps to manage risk and to reduce the volatility of the funding obligations imposed on the companies maintaining the plans. Congress recognized that pension plans which utilize swaps to hedge risks associated with the operation of plans do not pose systemic risk to the financial system. For example, Dodd-Frank carves out swaps used by ERISA plans for hedging or mitigating risk from the “substantial position” thresholds used to define MSPs and MSSPs.³

ERISA plans face unique risks that require, in many instances, customized hedging strategies for which cleared swaps either may not be available and/or may not be well-suited. For example, in a defined benefit ERISA plan, a retiree is promised payments in the future. The payment obligations of an ERISA plan span payments occurring presently to payments promised more than 50 years from now and everything in between (including durations that do not match standardized products expected to be

¹ 76 Fed. Reg. 27,564 (May 11, 2011).

² Unless otherwise specified, we use the term “swap” to generically refer to both swaps and security-based swaps.

³ Dodd-Frank §§ 721(a)(16), adding new § 1a(33) to the Commodity Exchange Act (“CEA”), and 761(a)(5), adding new § 3(a)(67) to the Securities Exchange Act of 1934 (“Exchange Act”).

available for clearing). The present value of payments to be made in future years, which is used to help determine required contributions by plan sponsors, will vary considerably depending on interest rates. Because of the unique and long-term durations of ERISA plan obligations, even minor changes in interest rates can have a material impact on the funded status of the plan. Customized interest rate hedging strategies (including swaptions) are necessary to effectively hedge these unique interest rate exposures in order to maximize the financial soundness of the plan thereby protecting the retirement assets of the participants (as well as to minimize the financial impact on plan sponsors). Currency and even sometimes equity swaps may also be regularly customized for ERISA plans in order to create hedges designed to mitigate the underlying ERISA plan exposures. Moreover, hedging needs can vary widely from plan to plan because each ERISA plan has unique demographics, plan design features and investment policies. There is no question that, even after swaps clearing is well-established, uncleared swaps will give ERISA plans hedges that better match their underlying risk exposures to interest rates, currencies and equities. ERISA plans therefore will be greatly affected by the requirements the Agencies adopt for uncleared swaps margin.

We support the Agencies' goals of protecting CSEs and protecting the financial system from systemic risk. Imposing margin requirements in appropriate circumstances will help toward achieving that goal. However, requiring initial margin of highly regulated, highly creditworthy, low leveraged and prudently managed counterparties such as ERISA plans which use swaps primarily for hedging will unnecessarily increase the cost of hedging for such market participants without providing a measurable benefit to the stability of the US financial system. Accordingly, we have the following comments on the proposed regulation.

SPECIFIC COMMENTS

CSEs Should Not Be Required to Collect Initial Margin from ERISA Plans Because ERISA Plans Are Not Risky Counterparties

We support the Agencies' approach that would permit CSEs to establish initial margin thresholds for certain counterparties' uncleared swaps. However, the imposition of initial margin on highly creditworthy, minimally leveraged (if at all), heavily regulated and prudently managed ERISA plans appears only to serve as an inappropriate financial penalty on them for seeking to secure retirement benefits for union and salaried retirees through the use of swaps. The imposition of initial margin requirements for uncleared swaps of ERISA plans is not required by Dodd-Frank and in our view advances no policy objective. Because there is virtually no risk that ERISA plans will fail to be able to make all payments due to CSEs, margin requirements will not provide additional protection for CSEs. Further, punitive margin requirements will not encourage clearing because ERISA plans will choose cleared swaps anyway when they are the most effective and efficient manner to hedge, using uncleared swaps when cleared swaps are unavailable.

Dodd-Frank requires the Agencies to establish risk-based margin requirements for uncleared swaps (discussed in part A below). For the reasons described below in part B, ERISA plans present virtually no counterparty risk and, therefore, should not be required to post initial margin for uncleared swaps under a risk-based regime.

A. *Dodd-Frank Does Not Require CSEs to Collect Margin From Counterparties That Do Not Pose Risks*

Dodd-Frank requires the Agencies to impose initial and variation margin requirements for all uncleared swaps (paragraph (2) of CEA § 4s(e) and Exchange Act § 15F(e)) with respect to SDs, SBSDs, MSPs, and MSSPs.⁴ The Agencies are required to adopt these requirements jointly, in consultation with the Commodity Futures Trading Commission (“CFTC”) and the Securities and Exchange Commission (“SEC”).⁵ Paragraph (3) of CEA § 4s(e) explicitly requires that the margin requirements adopted by the Agencies be risk-based requirements:

To offset the greater risk to the [CSE] and the financial system arising from the use of swaps that are not cleared, the requirements imposed under paragraph (2) shall -- (i) help *ensure the safety and soundness* of the [CSE]; and (ii) be appropriate for the *risk associated with the non-cleared swaps* held as a [CSE].⁶

The statutory directive in CEA § 4s(e)(3) (quoted above) that initial and variation margin requirements be *risk-based* modifies the requirement in CEA §4s(e)(2) that margin requirements be imposed for *all* uncleared swaps. Thus, it is clear from the statutory text that Congress intended the Agencies (and the CFTC and the SEC) to establish risk-based margin requirements. Indeed, the Agencies themselves state repeatedly in the preamble to the Proposed Rules that they are implementing a “risk-based approach” as required by Dodd-Frank.⁷

Importantly, while Dodd-Frank directs the Agencies (and the CFTC and the SEC) to adopt *requirements* for risk-based margin for *all* uncleared swaps, Dodd-Frank does not mandate that initial and variation margin be *collected* for *all* uncleared swaps. The directive to take a risk-based approach in determining margin requirements contradicts the notion that margin must be collected in all cases. The Agencies agree, citing the risk-based mandate as the rationale for not requiring all counterparties to post initial and

⁴ Dodd-Frank §§ 731, adding new CEA § 4s(e)(2)(B); and § 764, adding new Exchange Act § 15F(e)(2)(B).

⁵ Dodd-Frank §§ 731, adding new CEA § 4s(e)(2)(A) and 764, adding new Exchange Act § 15F(e)(2)(A).

⁶ Dodd-Frank §§ 731(e)(3)(A), adding new CEA § 4s(e)(3)(A) and 764(e)(3)(A), adding new Exchange Act § 15F(e)(3)(A) (emphasis added).

⁷ *E.g.* Proposed Rules at 27,567.

variation margin for all uncleared swaps.⁸ As CFTC Commissioner Scott O’Malia recently stated, Congress “instructed the regulators to only impose margin on an uncleared swap that is appropriate for the risk of that swap. The final Commission and prudential regulator rules should do the same.”⁹

The Agencies’ Proposed Rules would permit certain types of counterparties not to post initial and variation margin below credit-based thresholds, and propose that those thresholds should be unlimited for certain counterparties that pose no risk. Likewise, the CFTC’s Proposed Rules relating to “non-financial entities” would only require that the parties to a transaction have a credit support agreement and determine initial and variation margin levels, if any, by agreement. This approach is entirely consistent with Dodd-Frank in imposing margin requirements, and does not require the CSE to collect margin where the CSE’s counterparty presents little risk unless the parties themselves otherwise agree. The Agencies incorrectly exclude ERISA plans from this lowest risk end user category.¹⁰ Unless ERISA plans are treated in the same manner that other counterparties that present little risk are treated in the Proposed Rules, we believe that the Agencies will not have met the “risk-based” directive in Dodd-Frank.

The Agencies have used the definition of “financial entity” from the clearing exemption as a guidepost for margin requirements for uncleared swaps (which definition the Regulators deviate from in any event) in the Proposed Rules. We believe that this approach does not meet the ‘risk-based’ directive for uncleared margin requirements. Nothing in Dodd-Frank requires or even suggests that uncleared margin should be based on whether or not a counterparty is a “financial entity.” In contrast to the uncleared swap margin provision, the impetus for the clearing exemption was the cost concerns of commercial end users; nothing in Dodd-Frank or its legislative history suggests that ERISA plans were included in the financial entity definition (and not exempted from the clearing mandate) because they are risky counterparties.¹¹

⁸ See Proposed Rules at 27,567 (The risk-based categories of end users, which have different margin requirements “reflect the Agencies’ preliminary belief that distinctions can be made between types of derivatives counterparties that are useful in distinguishing between the risks posed by each type.”).

⁹ Remarks of CFTC Commissioner Scott O’Malia, “Not All-End Users Are Created Equal” (May 11, 2011), <http://cftc.gov/PressRoom/SpeechesTestimony/opaomalia-6.html>.

¹⁰ ERISA plans should be treated the same as “non-financial end users” in the proposed rules. We do not contend that ERISA plans are not “financial” entities in the sense that the term “financial end user” would generically include entities whose primary business is financial in nature. The Proposed Rules, however, provide a special definition of the term “financial end user” that may exclude some entities whose primary business is financial in nature (*e.g.* endowments, insurance companies, and real estate investment trusts) and would include other entities whose primary business is not (*i.e.* foreign governmental entities). Although the Regulators purport to rely on the structure of the exemption from the mandatory clearing requirement, they in fact deviate from that provision. The Regulators’ choice of terminology is not a reason for excluding ERISA plans from the lowest risk category and the Regulators are not required to (and should not choose to) follow the structure of the clearing exemption, which is not by its terms risk-based.

¹¹ Although there is a risk-based notion embedded in the clearing exemption (*e.g.*, the exemption only applies for swaps used primarily for hedging commercial risk), legislative history indicates that the clearing exemption was intended to ensure that swaps did not become prohibitively expensive (*i.e.*, because of margin requirements) for commercial businesses. For example, Senator Chambliss stated that “[t]he

We believe a better gauge of Congress' view on measuring the risk posed by swaps used by ERISA plans is the statutory exclusion in the definitions of MSP and MSSP of swaps used by ERISA plans to hedge or mitigate plan risks. Consistent with the solid financial standing of ERISA plans, Dodd-Frank explicitly excludes from the major participant analysis positions maintained by any ERISA plan "for the primary purpose of hedging and mitigating any risk directly associated with the operation of the plan."¹² As the CFTC and SEC have noted, the major participant definitions "focus on the market impacts and risks associated with an entity's swap and security-based swaps positions."¹³ We ask that the Agencies similarly exclude ERISA plans from initial margin requirements with respect to uncleared swaps.

B. Because ERISA Plans Pose Virtually No Counterparty Risk, They Should Not Be Subject to Risk-Based Margin Requirements

The proposed margin requirements for uncleared swaps were intended to limit systemic risk by "reduc[ing] the ability of firms to take on excessive risks through swaps without sufficient financial resources to make good on their contracts."¹⁴ For a variety of reasons detailed in this letter, ERISA plans do not cause systemic risk.¹⁵ Below are just some of the reasons:

- ERISA plans are required to be prudently diversified. In entering into swaps for plans, ERISA requires that plan fiduciaries act solely in the interest of the plan's participants and beneficiaries and with the care, skill, prudence, and diligence that a prudent person familiar with such matters would use.¹⁶
- "Investment managers" for ERISA plans are required to be regulated entities (registered investment advisers, banks, or insurance companies) that are (1) subject to the highest standard of care under US law, (2) liable for significant

entire point of exempting some [businesses] from the clearing mandate was to ensure that they do not bear the burden of increased margin costs, but [the uncleared margin] language would indirectly subject these businesses to the expense of margins imposed on their dealer counterparties--counterparties that will be forced to recoup this cost in the form of fees, and businesses will be forced to pass their costs on to consumers." Congressional Record--Senate, S5881, July 15, 2010.

¹² Dodd-Frank §§ 721(a)(16), adding new CEA § 1a(33)(A)(i)(II) and 761(a)(6), adding new Exchange Act § 3(a)(67)(A)(ii)(I).

¹³ "Further Definition of 'Swap Dealer,' 'Security-Based Swap Dealer,' 'Major Swap Participant,' 'Major Security-Based Swap Participant' and 'Eligible Contract Participant,'" Joint Proposed Rule, 75 Fed. Reg. 80,174, 80,185 (Dec. 21, 2010)

¹⁴ Proposed Rules at 27,567.

¹⁵ See, e.g., Franzen, D. (2010), "Managing Investment Risk in Defined Benefit Pension Funds," *OECD Working Papers on Insurance and Private Pensions*, No. 38, OECD Publishing. Franzen writes that "[t]here is consensus that opposite banks, pension funds do not pose a systemic risk." *Id.* at 22. Franzen's statement is based in part on the fact that private pension funds are highly regulated, they are not for-profit businesses, and "pension funds have – at least in principal – a sponsor as guarantor and protector." *Id.*

¹⁶ ERISA section 404(a)(1)(B).

financial penalties for failure to comply with relevant provisions of ERISA, and (3) liable in many instances for the acts of other fiduciaries.¹⁷

- ERISA plan assets are required to be held in trust for future payment, subject to the oversight of a trustee which is typically a US regulated bank.¹⁸
- Because of the regulatory structure that applies to ERISA plans, ERISA plans typically have minimal leverage (if at all).
- ERISA plans are subject to stringent funding requirements pursuant to the Pension Protection Act of 2006.
- ERISA plans are financially transparent; they typically have third-party custodians report their net asset value to dealers on a monthly basis and are required by law to report their holdings annually to the Department of Labor.¹⁹
- ERISA plans are not operating entities subject to business-line risks and competitive challenges.
- There is no provision under any law for ERISA plans to file for bankruptcy or reorganization to avoid their financial obligations to counterparties. Even the filing of bankruptcy by an ERISA plan sponsor or the involuntary termination of the plan does not relieve a plan of its financial obligations to counterparties.
- ERISA plans are typically (and correctly) not treated the same as unregulated investment entities in CFTC regulations. For example, Rule 4.5 excludes certain ERISA plans from registration as commodity pool operators. The CFTC has relied on ERISA's "pervasive" regulation of plans and plan fiduciaries as a reason it does not need to regulate these plans.²⁰ Similarly, pension trusts are exempt from registration as "investment companies" with the SEC.²¹
- Based on a survey of over a dozen major dealers by one of our members, ERISA plans have met their swap obligations to dealers despite the bankruptcy of Fortune 500 plan sponsors, the market crash of 2008, and every other significant financial event since the adoption of ERISA in 1974.

Certain end users subject to comprehensive regulatory oversight, such as ERISA plans,²² which are subject to prudence and diversification requirements, professional management standards, transparency requirements, and limits on leverage should be excluded from any requirement imposed on CSEs to collect initial margin. ERISA plans should not be treated the same as other financial end users, such as hedge funds and other largely unregulated investment entities that are not subject to strict prudence or

¹⁷ ERISA sections 3(38) (investment manager requirements), 404(a) (fiduciary standards), 405 (co-fiduciary liability), 409 (fiduciary liability), 502 (ERISA enforcement).

¹⁸ ERISA section 403(a).

¹⁹ See Form 5500.

²⁰ See Commodity Pool Operators; Exclusion for Certain Otherwise Regulated Persons From the Definition of the Term "Commodity Pool Operator," Final Rules, 50 Fed. Reg. 15,868, 15,869 and 15,873 (1985); 58 Fed. Reg. 6,371, 6,373 (1993).

²¹ Section 3(c)(11) of the Investment Company Act of 1940 ("Investment Company Act").

²² This would also include other financial end users including registered investment companies under the Investment Company Act.

transparency requirements and use derivatives to gain risk exposure rather than primarily as a hedging tool. As CFTC Commissioner Scott O'Malia recently stated:

Financial end-users are hedge funds, private equity funds, endowments, and other financial entities that do not generate revenue from commercial activity, but take speculative positions in the market. Retirement end-users consist of entities whose sole obligation is to preserve capital and generate returns for the retirement benefit of others. This category includes ERISA plans and pension funds. They generally use the swaps market to hedge the fixed income exposure associated with their bond portfolios and to gain customized exposure to certain asset classes.²³

Accordingly, we request that the Agencies not require CSEs to collect initial margin from ERISA plans in recognition (i) of the unique attributes of ERISA plans as heavily regulated, minimally (if at all) leveraged, prudently managed entities, (ii) that ERISA plans do not pose systemic risk and (iii) that ERISA plans are possibly the safest counterparty for a CSE.

The Definition of “Low-Risk Financial End User” Should Be Based on the Leverage Ratio of a CSE’s Counterparty.

The Proposed Rules would create margin requirements for financial end users that differ based upon whether the swap counterparty is a “high-risk” or “low-risk” end user. “High-risk financial end users” would be all financial end users that do not fall within the definition of low-risk. “Low-risk financial end users” would be eligible for credit-based margin thresholds, which would permit a CSE not to collect margin if the financial end user’s uncleared swaps exposure is below the threshold. A “low-risk financial end user” would be a financial end user that:

- i) does not have significant uncollateralized swaps exposure;²⁴
- ii) predominantly uses swaps to hedge or mitigate the risks of its business activities, including balance sheet, interest rate, or other business risks; *and*
- iii) is subject to capital requirements established by one of the Agencies or a state insurance regulator.²⁵

²³ Remarks of CFTC Commissioner Scott O'Malia, “Not All-End Users Are Created Equal” (May 11, 2011), <http://cftc.gov/PressRoom/SpeechesTestimony/opaomalia-6.html>.

²⁴ The definition of “low-risk financial end user” uses the term “significant swaps exposure.” Proposed Rule § __.2(n)(1). “Significant swaps exposure” is defined by reference to “uncollateralized” exposures. Proposed Rule § __.2(v). Proposed Rules at 27,587, 27,588.

²⁵ Proposed Rule § __.2(n). Proposed Rules at 27,587.

As written, the “high-risk financial end user” definition would include ERISA plans, which are highly credit-worthy and minimally leveraged (if at all) and which do not present systemic risk to the financial system or to any CSE. The “low-risk” financial end user definition would, confusingly, exclude highly creditworthy, minimally leveraged counterparties while including certain highly leveraged, low creditworthy financial counterparties.

The financial crisis of 2008 was in large part attributable to leverage. Some highly rated regulated entities subject to capital requirements were later determined to be “high-risk” precisely because of the leverage they utilized. A low leveraged, highly creditworthy counterparty which uses swaps to hedge or mitigate its risks, such as an ERISA plan, poses less risk to a CSE (even with a large position in swaps) than a highly leveraged low creditworthy counterparty which enters into swaps for speculative purposes.

Accordingly, we recommend that the Agencies permit “high-risk financial end users” to be defined by reference to their leverage ratio. For example, the CFTC in its proposed MSP definition and the SEC in its proposed MSSP definition defined “highly leveraged” entities as having a ratio of total liabilities to equity, under US generally accepted accounting principles in excess of 8 to 1 or 15 to 1 (to be determined in the final rule) at the close of business on the last business day of the applicable fiscal quarter.²⁶ We believe that a leverage ratio²⁷ that would indicate an end user is “low-risk” would be to 4 to 1 or lower.

Because ERISA plans are highly credit worthy, minimally leveraged (if at all), heavily regulated, and prudently managed counterparties to CSEs, we strongly believe that ERISA plans should be completely excluded from any initial margin requirements. If, however, the Agencies do not exclude ERISA plans from such requirements, then we request that the definition of “low-risk financial end user” be modified to include ERISA plans as “low-risk financial end users” per se.

The Definition Of “Low-Risk Financial End Users” Should Be Expanded to Include ERISA Plans.

Alternatively, if the Agencies will not automatically consider ERISA plans “low-risk,” they should modify the definition of “low-risk” to accommodate ERISA plans. In this regard, we have the following suggestions:

²⁶ CFTC Proposed Rule 1.3(vv)(2) and SEC Proposed Rule § 240.3a67-6(b), 75 Fed. Reg. 80,174.

²⁷ Leverage ratio is the ratio with the numerator equal to the sum of the market values of physical assets plus the notional value (which is the implied market values of notionally equivalent physical assets as calculated from derivative instruments) and the denominator equal to the net asset value of the plan (or fund).

A. The “low-risk” definition should be clarified to include swaps entered into by an ERISA plan to hedge or mitigate risk associated with the operation of the plan.

The second prong of the definition of “low-risk financial end user” would require that the end user use swaps primarily for hedging “business activities” and “business risks.” We are concerned that the term “business activities” may be wrongly interpreted not to apply to ERISA plans as they are not operating company end users, but instead are end users in the business of providing retirement benefits to retirees.

Accordingly, we suggest that the second prong of the “low-risk financial end user” definition be clarified to include explicitly swaps entered into to hedge or mitigate the risks of operating a pension plan. We note that Congress excluded, for purposes of calculating whether an ERISA plan has a “substantial position in swaps,” those swaps entered into by a pension plan for “the primary purpose of hedging or mitigating any risk directly associated with the operation of the plan.”²⁸ We suggest that the same language be included in the second prong of “low-risk financial end user.”

B. The “low-risk” definition should not exclude highly creditworthy, low leveraged entities which are not subject to prudential regulator or insurance regulatory capital requirements.

The Proposed Rules would include as low-risk financial end users only entities subject to capital requirements set by a Prudential Regulator or state insurance regulator. The proposal states: “This distinction reflects the fact that financial end users that are subject to regulatory capital requirements are likely to pose less risk as counterparties (*e.g.*, because the requirements ensure that minimum amounts of capital will be available to absorb any losses on their derivatives transactions).”²⁹

Although ERISA plans are subject to funding requirements³⁰ which are comparable to capital requirements, we suggest that, with respect to ERISA plans, the “low-risk financial end user” definition not be based on whether an entity is subject to capital requirements established by a prudential regulator or insurance regulator but rather be based on the financial leverage of such counterparty which is a better measure of counterparty risk to the CSE.

²⁸ Dodd-Frank §§ 721(a)(16), adding new CEA § 1a(33), and 761(a)(5), adding new Exchange Act § 3(a)(67).

²⁹ Proposed Rules at 27,572.

³⁰ ERISA plans are subject to stringent funding requirements pursuant to the Pension Protection Act of 2006.

We do not believe that capital requirements are a reliable indicator of the financial soundness of a counterparty. As evidenced by the financial crisis of 2008, such requirements serve primarily to lessen the impact of an entity's financial failure but do not necessarily protect individual counterparties to such entity. Leverage is a more reliable indicator of a counterparty's creditworthiness. ERISA plans are highly creditworthy, minimally leveraged (if at all), and prudently managed counterparties which pose virtually no default risk to CSEs. Accordingly, we ask that ERISA plans not be excluded from the "low-risk financial end user" definition solely because they are not subject to prudential or insurance regulatory capital requirements.

Thresholds to Post Initial Margin for "Low-Risk Financial End Users" Such as ERISA Plans Should Be High

The Proposed Rules would set maximum limits on margin thresholds for low-risk financial end users at the lesser of a set dollar amount or a percentage of the CSE's regulatory capital. To our knowledge, no ERISA plan has ever failed to make a payment on a swap to a dealer; accordingly, the imposition of initial margin appears to address a risk that does not exist. We believe that any imposition of initial margin on uncleared swaps of an ERISA plan would only serve as a financial penalty on an ERISA plan for conducting activities that the plan fiduciary believes are "in the best interests" of the retirees of such plan. But if initial margins are nonetheless still imposed by the Agencies on ERISA plans, we believe that the initial margin thresholds for ERISA plans should be high in light of the low-risk nature of ERISA plans. Permitting high initial margin thresholds for ERISA plans would be consistent with the Agencies' intent that "firms that take significant risks through derivatives will face more stringent margin requirements with respect to non-cleared derivatives, while firms that take lower risks will face less stringent margin requirements."³¹ To the extent the Agencies impose maximum limits on margin thresholds for low-risk financial end users, we believe those limits should be in the \$100 million to \$150 million range.

It is worth noting that the Agencies have not proposed maximum limits on margin thresholds for non-financial end users, even though non-financial end users are eligible for thresholds irrespective of whether they use swaps primarily for hedging. We agree with the Agencies' approach. Presumably the Agencies believe unlimited thresholds for non-financial end users do not create systemic risk because thresholds depend on the use of credit approval processes and regulatory capital charges to protect against risks posed by uncleared swaps. The Agencies also assume that non-financial end users only use swaps primarily for hedging, even though there is no such limitation in the statute or Proposed Rules.³² We believe the same logic should apply to, and unlimited thresholds should be adopted for, ERISA plans. In other words, ERISA plans should be treated the

³¹ Proposed Rules at 27,567.

³² Proposed Rules at 27,569 (describing an entity in the non-financial end user category as a "commercial end user" (i.e., a non-financial counterparty that engages in derivatives activities to hedge commercial risk)).

same as “non-financial end users” are treated in the Proposed Rules. This is a logical approach because, if a plan sponsor is exempted from initial margin requirements, it would necessarily follow that its pension plan, which carries less risk than the plan sponsor and which utilizes swaps primarily for hedging purposes, would receive similar favorable treatment.

The Agencies Should Revise the Initial Margin Calculation Methodology

The Proposed Rules would permit CSEs to calculate initial margin using an approved internal initial margin model. Proposed Rule § __.8 prescribes detailed requirements for initial margin models and would require models to determine potential future exposure to be based upon a 99 percent confidence interval "over a holding period equal to the shorter of ten business days or the maturity of the swap."³³ This is in contrast to "a typical requirement of 3 to 5 business days used by derivatives [central clearing counterparties] CCPs."³⁴

The Agencies have not provided any explanation for requiring a 10-day liquidation period to calculate initial margin. The only rationale provided is that “non-cleared swaps are expected to be less liquid than cleared swaps,” so a longer time horizon is necessary for a CSE to offset or liquidate a position.³⁵ We believe a 10-day liquidation period substantially overstates the risk of many uncleared swaps and will create unnecessarily high initial margin requirements, particularly since models must use a 99% confidence interval and be calibrated to a period of financial stress.³⁶ We ask that the Agencies require a 3 to 5 day liquidation period in initial margin models.

ERISA Plans Should Be Able to Choose Whether Initial Margin is Calculated Using an Initial Margin Model or the Alternative Look-up Table

As an alternative to an initial margin model, the Agencies would permit CSEs to use a look-up table that determines initial margin as a percentage of the notional exposure of the swap. ERISA plans should be permitted to choose whether initial margin is calculated using an initial margin model or the look-up table. If the choice is left to CSEs, CSEs may be able to maximize the amount of margin by choosing one method over the other, irrespective of the risk posed by a particular swap. This is particularly true if the Agencies do not impose two-way margin requirements (discussed below). We ask that the Agencies permit ERISA plans to elect the method by which initial margin is calculated for a particular swap.

³³ Proposed Rules at 27,590.

³⁴ Proposed Rules at 27,579.

³⁵ Proposed Rules at 27,579.

³⁶ Proposed Rules §§ __.8(d)(1) and __.8(d)(11). Proposed Rules at 27,590 – 27,591.

Initial and Variation Margin Requirements for Uncleared Swaps Should Be Two-Way

The Proposed Rules would create a two-way initial and variation margin requirement for transactions between two CSEs. The Agencies believe that a two-way initial and variation margin requirement is appropriate for those transactions because the Agencies' objective is to protect CSEs and the only way to ensure that objective is to require two-way margin.³⁷ This requirement rests on the premise that CSEs pose counterparty risk to one another. CSEs pose systemic risk to the financial system.

Because of their fiduciary responsibilities, funding obligations, and the importance of their mission, ERISA plans are particularly sensitive to counterparty risk. CSEs pose significantly more counterparty risk to ERISA plans than ERISA plans do to CSEs. We believe that CSE capital requirements do not provide sufficient protection for ERISA plans from the counterparty risk of a CSE because ERISA plans have no input in and cannot monitor a CSE's compliance with its capital requirements. Further, capital requirements are designed primarily to prevent or at least limit the impact of an entity's failure, not to protect individual creditors with regard to specific transactions. To the extent that ERISA plans are required post initial margin, we ask that the Agencies require CSEs to post equivalent initial margin if requested by their counterparty.

Most ERISA plans design their swap relationships in a manner that provides two-way collateral requirements and many require that collateral be segregated with third party custodians. ERISA plans should be able to continue these protective arrangements. We note that Sections 724 and 764 of the Dodd-Frank Act explicitly require SDs and MSPs to notify their counterparties of the right to have initial margin segregated with an independent, third-party custodian. We ask that the Agencies explicitly permit a counterparty to a CSE the right to elect to require a CSE to segregate variation margin with a third party custodian and with no ability to rehypothecate the collateral.

With respect to variation margin, CSEs currently pay variation margin to ERISA plans, and vice versa, with respect to derivatives transactions. ERISA plans' current use of variation margin is risk-based; ERISA plans require dealers to post daily variation margin to protect against counterparty risk posed by dealers. We believe that, in general, it is prudent for plans to both collect variation margin with respect to derivatives transactions (and, in turn, plans are agreeable to posting variation margin to dealers) and expect to continue this practice. We ask the Agencies to continue this sound practice by requiring CSEs to post, as well as collect, equivalent variation margin for uncleared swaps between CSEs and ERISA plans.

The Definition of "Eligible Collateral" Should Be Expanded To Include Other High Quality Instruments

Dodd-Frank requires that the Agencies "permit the use of noncash collateral" as the Agencies determine "to be consistent with (i) preserving the financial integrity of

³⁷ Proposed Rules at 27,567.

markets trading swaps; and (ii) preserving the stability of the United States financial system.”³⁸ The Agencies propose to permit only cash, US Treasuries, and, for initial margin only, senior debt obligations of certain government-sponsored entities (“GSEs”). The proposed definition of “eligible collateral” is too narrow.

Pension plans, by the nature of their size and investment philosophies, as well as the ERISA requirement to be prudently diversified, invest in myriad security types across markets, geographies, and asset classes. Furthermore, plans typically hold cash balances only to the extent necessary to pay pensioners and make other required distributions. Additional cash lowers expected investment returns, which in turn leads to greater funding risk. Restricting non-cash collateral to US Treasuries and senior GSE debt necessarily forces plans to hold a greater percentage of such instruments than might otherwise be prudent. Accordingly, this proposed requirement ultimately will decrease diversification in ERISA plans’ investment portfolios and may serve to increase overall funding risks.

Dodd-Frank expressly gives the Agencies discretion to permit parties to use non-cash collateral as margin. Other types of non-cash collateral (beyond just US Treasuries and GSEs) would not increase risk to the CSE in a way that jeopardizes the financial integrity of swap markets or the US financial system. For example, assets such as hypothetical high-quality debt securities described in the Agencies’ Question 64(a) in the preamble should be permitted.³⁹ Requiring ERISA plans (or other financial entities) to post only cash or US government obligations as margin may require plans to liquidate other investments, creating opportunity costs by forcing plans to turn income producing investments into non-productive cash or low-yielding investments. The Agencies should adopt a more flexible definition of “eligible collateral” that would permit parties to agree to accept other types of high quality collateral and appropriate haircuts.⁴⁰ Such additional forms of collateral may include high quality municipal securities, certificates of deposit, commercial paper, corporate bonds, and interests in money market mutual funds either (i) to be posted by all parties to a swap or (ii) to be posted by highly creditworthy, low leveraged counterparties such as ERISA plans, in each case as the parties agree. It is important to note that if CSEs are also required to post initial and variation margin, as we propose above, both parties to a swap are incentivized only to accept high quality collateral.

³⁸ Dodd-Frank §§ 731(e)(3)(C), adding new CEA § 4s(e)(3)(C) and 764(e)(3)(C), adding new Exchange Act § 15F(e)(3)(C).

³⁹ Question 64(a) asks whether “fixed income securities issued by a well-known seasoned issuer that has a high credit standing, are unsubordinated, historically display low volatility, are traded in highly liquid markets, and have valuations that are readily calculated be added to the list of eligible collateral for initial margin? . . . If so, how should the concept of ‘high credit standing’ be defined in a way that does not reference credit ratings?” Proposed Rules at 27,578. We believe that “high credit standing” is a sufficiently precise description for CSEs to apply using their own credit evaluation processes.

⁴⁰ An appropriate metric for determining whether a debt instrument is “high quality” could be the option-adjusted spread.

Clarify That Pre-enactment Swaps Should Not Be Included In Initial Margin Calculated on a Portfolio Basis Unless Agreed To By the CSE and Its Counterparty

The Proposed Rules may be read to permit a CSE to include pre-enactment swaps in initial margin calculations for swap portfolios. Although we understand that Agencies may not have intended that CSEs have unilateral authority to include pre-enactment swaps, the Proposed Rule and statements in the preamble may provide a basis for CSEs to assert that they have such unilateral authority.

Under the proposal, a customer could be required by a CSE to post initial margin for all pre-enactment swaps in a portfolio that is in the same risk category as a post-enactment swap at the time it enters into its first post-enactment swap in that risk category. If a customer has a large pre-existing swap portfolio with a CSE and did not previously post initial margin, including those swaps in the initial margin calculation could result in an exorbitant margin call. This is significant for our members because no initial margin is currently posted for the vast majority of our members' current swaps positions.

Furthermore, any decision by a CSE counterparty to exit such transactions prior to final settlement date in order to avoid a surprise initial margin payment could be quite costly. This is because the vast majority of swaps have no contractual settlement formula for early terminations absent a default-based event and, accordingly, the CSE counterparty must agree to unwind existing transactions and the CSE may choose to do so only at unfavorable prices to the CSE counterparty.

In contrast to the Proposed Rules, the CFTC has correctly proposed not to permit CSEs that it regulates to include pre-enactment swaps in initial margin calculations. The CFTC "believes that the pricing of existing swaps reflects the credit arrangements under which they were executed and that it would be unfair to the parties and disruptive to markets to require that new margin rules apply to those positions."⁴¹

We agree with the CFTC. It is hard to imagine why a CSE would choose *not* to collect additional margin when given a unilateral option. As discussed above, under the Proposed Rules, ERISA plans will lose the bargaining power they currently have with CSEs. If the final rules provide CSEs a right to include pre-enactment swaps, ERISA plans would likely not be able to require a CSE, by contract, only to include post-enactment swaps in initial margin calculations for swap portfolios. The large after-the-fact margin calls that would be caused by allowing inclusion of pre-enactment swaps could require dramatic shifts in ERISA plans' asset allocations to meet those calls. This shift in asset allocation may cause some ERISA plans to unwind or otherwise offset a large number of positions in a very short time and, given that the consent of the CSE may be required, at unfavorable prices.

⁴¹ Preamble to CFTC Proposed Rules, 76 Fed. Reg. 23,734.

Our members (as well as other financial end users) have relied in good faith on these pre-existing transactions in implementing their hedging strategies and allocating their assets. Importantly, plans did not contemplate these proposed margin costs when entering into these pre-enactment transactions. Therefore we advocate that the Agencies only permit inclusion of pre-enactment swaps in initial margin calculations if both parties agree.

We therefore suggest modifying the language in Proposed Rule § __.8(b)⁴² to read as follows:

. . . . To the extent that a qualifying master netting agreement between a covered swap entity and its counterparty governs swaps or security-based swaps that were entered into before, on, and after the effective date, the covered swap entity may use its initial margin model to calculate the amount of initial margin required to be collected pursuant to section __.3 either—

- (1) With respect to only those swaps and/or security-based swaps transactions entered into on and after the effective date; or
- (2) With respect to those pre-enactment ~~all~~ swaps and/or security-based swaps transactions for which the parties agree, governed by such qualifying master netting agreement, regardless of whether they were entered into before, on, or after the effective date⁴³

The Rules Should Require Covered Swap Entities to Return Variation Margin to ERISA Plans Where the Mark-to-Market Results in a Reduction

Although the proposed definition of “variation margin amount” appears to contemplate that variation margin can be returned, the Proposed Rule does not explicitly address the return of any amounts based upon the periodic adjustments. As the Agencies themselves have stated, “variation margin is generally used to offset the current exposure arising from actual changes in the market value of the derivative position.”⁴⁴ It follows that where current exposures decrease based on actual changes in market value, variation margin should be returned based upon that decrease.

Under the Proposed Rules, “variation margin amount” would be defined as the cumulative mark-to-market change in value “less the value of all variation margin

⁴² Proposed Rules at 27,590.

⁴³ The Agencies note that the proposed rule is intended to prevent a CSE from selectively incorporating only certain pre-enactment swaps in portfolio margin calculations. Proposed Rules at 27,569, n. 34. We believe that permitting inclusion of some, but not necessarily all, pre-enactment swaps based upon the agreement of the parties alleviates the concern that a CSE might cherry-pick certain pre-enactment swaps.

⁴⁴ Proposed Rules at 27,578, n. 72 (explaining why there is no segregation requirement for variation margin).

previously collected but not returned.”⁴⁵ The use of the word “returned” suggests that variation margin can be returned, and the Proposed Rules do not prohibit such a return. In contrast, the CFTC proposal points parties to their credit support agreements, which almost universally provide for the return of variation margin.

It is common and widespread industry practice, both for futures contracts cleared by derivatives clearing organizations and for over-the-counter swaps and other derivatives, for parties to return variation margin where the required margin decreases. Moreover, as plans are subject to ERISA considerations in determining the amount of excess margin that can be kept at a futures commission merchant,⁴⁶ it can be expected that plans will be subject to similar constraints for swaps margins. Accordingly, the Agencies should clarify that variation margin should be returned where the mark-to-market reduces the variation margin amount.

Parties Should Be Permitted a Commercially Reasonable Time After Executing a Swap Before Posting Initial and Variation Margin

The Proposed Rules would require CSEs to collect initial margin “on or before the date it enters into” a swap and collect variation margin on the date it enters into the swap.⁴⁷ Parties need a commercially reasonable time to operationally move money to a new counterparty or a new third party custodian. Under the Proposed Rules, an ERISA plan may have to establish new arrangements with new counterparties or custodians and set aside collateral several days before the plan even knows with certainty that the swap will be executed. This will hurt ERISA plans and tie up funds that otherwise could be used to generate income for retirees. We therefore ask that the Agencies permit a commercially reasonable time of two days after entering into a swap before requiring initial or variation margin to be posted.

Initial Margin Models Utilized By CSEs Should Be Submitted For Public Comment

The proposed rules would require that a CSE’s prudential regulator approve its internal initial margin model. Although we support the requirement that a prudential regulator must approve each initial margin model, it is critical that market participants who will have to post initial margin in accordance with those models be permitted to comment on the models, or at least on the formulas in those models that will be used to calculate the initial margin. We believe it is important that initial margin models can be replicated by independent third parties, which necessarily implies that such models not be proprietary if being proprietary would prevent independent third parties from utilizing

⁴⁵ Proposed Rule § __.2(aa). Proposed Rules at 27,588.

⁴⁶ See DOL Advisory Opinion 82-49A and Letter from Department of Labor to Futures Industry Association, Inc. dated August 15, 1985.

⁴⁷ Proposed Rules §§ __.3(b) and __.4(a). Proposed Rules at 27,588, 27,289.

those models. Permitting public comment would provide transparency consistent with the intent of Title VII of Dodd-Frank, which is titled “Wall Street *Transparency And Accountability*” (emphasis added). Further, the Agencies and market participants will benefit from the knowledge and expertise that industry participants can bring to bear through the public comment process. We ask that the Agencies provide at least a 30 day public comment period for each model.

Uncleared Swap Margin Requirements Should Only Take Effect After The Clearing System Is In Place and After Initial Margin Models Have Been Approved

The Proposed Rules will create higher initial margin requirements than those applicable for cleared swaps, particularly where initial margin is not calculated using an initial margin model. It will take some time for the clearing requirements to be implemented. If uncleared swap margin requirements take effect before the clearing infrastructure is in place, ERISA plans that would like to use cleared swaps will have no option but to pay the higher margin requirements under the uncleared swap rules until cleared swaps are available. Similarly, if the uncleared swap margin rules take effect before initial margin models are approved, which timeframe is highly uncertain given the Agencies’ resource constraints, ERISA plans will be forced to post initial margin in accordance with the look-up table (which is expected to impose higher requirements than initial margin models).

We ask that the Agencies delay implementation of the uncleared swap margin rules to coordinate with the clearing system and the approval of internal margin models. We also ask that the Agencies phase in the uncleared swap margin rules to permit market participants to time to put in place the necessary arrangements once the rules are final.

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We appreciate your consideration of our views.

Committee on Investment of Employee Benefit Assets American Benefits Council

cc: Commodity Futures Trading Commission