July 22, 2011

By Electronic Submission

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

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping (RIN 3038-AD46; SEC File No. S7-16-11; RIN 3235-AL14)

Dear Mr. Stawick and Ms. Murphy:

On behalf of its members, the Farm Credit Council is pleased to submit these comments on the product definition rules and interpretive guidance proposed by the Commodity Futures Trading Commission (the "CFTC") and the Securities and Exchange Commission (the "SEC" and, together with the CFTC, the "Commissions") under the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank").[1]

The Farm Credit Council is the national trade association for the Farm Credit System, a government instrumentality created "to accomplish the objective of improving the income and well-being of American farmers and ranchers by furnishing sound, adequate, and

[1] Pub. L. No. 111-203, 124 Stat. 1376 (2010). The proposed rules and interpretive guidance are set forth in Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping, 76 Fed. Reg. 29,818 (proposed May 23, 2011) (to be codified at 17 C.F.R. pts. 1 & 240) (hereinafter, "NOPR").

constructive credit and closely related services to them, their cooperatives, and to selected farm-related businesses necessary for efficient farm operations."[2] Today, the Farm Credit System comprises five banks and 87 associations, which together provide 40% of agricultural lending in the United States. Among the products offered by the Farm Credit System are variable rate loans and other structured loan products. Because we do not believe Congress intended these loan products or financing facilities to be treated as swaps or security-based swaps, we appreciate the opportunity to comment.[3]

I. Summary of Comments

On September 20, 2010, the Farm Credit Council submitted comments in response to the Commissions' advanced notice of proposed rulemaking. In that letter, we asked the Commissions to make clear in the final product definition rules that typical loan transactions, such as variable rate loans or other structured loans and unique financing relationships, would not be included in the definition of a swap. As we noted then, and as we continue to believe, these loans are not currently considered part of the over-the-counter derivatives market, and Congress did not intend Dodd-Frank to alter this understanding. Indeed, treating loan products as swaps simply because payments depend on interest rates would make loans more complex and would limit access to certain loan products to only those borrowers that qualify as eligible contract participants.

In light of these concerns, we commend the Commissions for providing guidance about which such agreements, contracts, or transactions will not be considered swaps or security-based swaps. We further commend the Commissions for providing guidance concerning the treatment of loan participations. With respect to these issues, we respectfully offer the following comments:

- We support the general considerations for determining that loans will not be treated as swaps. We respectfully request, however, that the Commissions clarify further that commercial loans and financing facilities with embedded options will not be considered swaps.

- We believe that consumer and commercial loans should not be considered swaps regardless of their treatment under the Legal Certainty for Bank Products Act of 2000.[4] To the extent the CFTC relies on that Act to provide

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[2] 12 U.S.C. § 2001(a).

[3] This letter uses the term "swap" to refer collectively to swaps and security-based swaps.

[4] 7 U.S.C. §§ 27 *et seq.*

legal certainty for identified banking products, it should interpret Farm Credit System institutions as "banks" and loans made by Farm Credit System institutions as "identified banking products."

- We support the Commissions' determination that "true" loan participations, in which the participant acquires a beneficial ownership interest in the underlying loans, will not be considered swaps.

II. The Interpretive Guidance for Consumer and Commercial Agreements, Contracts, or Transactions Should Clarify that Commercial Loans With Embedded Interest Rate Options Are Not Swaps

The Farm Credit Council supports the factors identified by the Commissions to distinguish customary consumer and commercial agreements, contracts, or transactions, on the one hand, from swaps, on the other hand. All loan agreements and financing facilities offered by the Farm Credit System satisfy the "key components" identified by the Commission. Namely, the payment provisions in the loan agreements are not severable from the agreement, and the agreements are not traded on an organized market or over the counter.[5] Further, customary loan agreements serve an independent business purpose of providing funding to, for example, an affiliated association or commercial customer. They are not executory contracts that are used for speculative, hedging, or investment purposes. All interest rate caps or locks on the interest rate are embedded in the loan, and the benefit of the cap or lock is realized only if the loan is made to the consumer or commercial customer. No loans offer two-way settlements whereby the borrower would be able to receive a settlement payment that is based on a market yield or rate. Finally, no Farm Credit System loan products or financing facilities contain payment obligations that are severable from the loan contract. As a result, customers cannot cash-out the value of the embedded cap, prepayment option, or rate lock feature at any time, and all of these features are conditioned upon the customer borrowing the funds in a loan. Similarly, the financing facilities that Farm Credit System banks have with their affiliated lending associations, including wholesale advances from banks to associations, satisfy the criteria for the type of agreement that

[5] *See* NOPR, 76 Fed. Reg. at 29,833. We understand this guidance to refer to the loan agreement at the time it is initiated. In other words, if a consumer or commercial customer does not enter into a loan through trading on an organized market or over-the-counter, then the loan should not be considered a swap. Farm Credit System institutions do buy and sell loans in the secondary market. But, as discussed in Section IV *infra*, these transactions are "true" loan participations involving the transfer of a current or future direct or indirect ownership interest in the related loan. As such, consistent with the Commissions' proposed guidance, these secondary market transactions should also not be considered swaps.

should not be included in the swap definition.[6] Accordingly, we believe that none of the Farm Credit System's loan products should be treated as swaps.

Although we agree with the general factors proposed for identifying agreements, contracts, or transactions that are not swaps, we think the market, and our members, would benefit from additional clarity with respect to particular transactions. Most importantly, we request that the final interpretive guidance specify that commercial loans and financing facilities with embedded interest rate options should not be considered swaps. The final interpretive guidance should further specify that products that will not be treated as swaps include loans that provide for rates to change upon certain events related to the commercial borrower, such as a higher rate of interest following a default.

This clarification would be consistent with the guidance that the Commissions have already provided for consumer loan products.[7] Although the Commissions did specify that consumer loans with embedded options were not swaps, the Commissions did not so specify with respect to commercial agreements, contracts, or transactions. We recognize that the Commissions provided that they would not treat as swaps "commercial agreements, contracts, and transactions (including, but not limited to, leases, service contracts, and employment agreements) containing escalation clauses linked to an underlying commodity such as an interest rate or consumer price index."[8] Because this provision does not specifically identify loan products, however, we think the market would benefit from greater clarity.

Accordingly, although none of the loan products offered by the Farm Credit System should be treated as swaps under the proposed interpretive guidance, we respectfully request that the Commissions clarify that commercial loans with embedded options will not be considered swaps.

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[6] Based on the unique cooperative structure of the Farm Credit System, most lending relationships between Farm Credit System banks and associations use a match funded concept where the loan to the borrower is matched to a specific advance from the bank to the association on a dollar-for-dollar basis.

[7] *See id.* (stating that products that will not be considered swaps include "[c]onsumer loans or mortgages with variable rates of interest or embedded interest rate options, including such loans with provisions for the rates to change upon certain events related to the consumer, such as a higher rate of interest following a default").

[8] *Id.*

III. Consumer and Commercial Loans Should Not Be Considered Swaps Regardless of their Treatment Under the Legal Certainty for Bank Products Act

As noted above, the Farm Credit Council generally supports the Commissions' interpretation that a loan will not be considered to be a swap if the payment provisions are not severable, and the agreement is not traded on an organized market or over-the-counter. In this regard, the Farm Credit Council further supports the Commissions' decision to provide interpretive guidance that is independent from the Legal Certainty for Bank Products Act. As the Commissions note, that Act provides that, under certain circumstances, the Commodity Exchange Act does not apply, and the CFTC may not exercise regulatory authority over, identified banking products. That Act is limited, however, to certain transactions that generally involve banks. We think it is important that the interpretive guidance providing that the definition of swap does not cover certain consumer and commercial agreements, contracts, or transactions not historically considered swaps, including loans, should apply equally to banks and non-banks that make such loans or participate in such non-swap transactions.

To the extent that the CFTC does rely on the Legal Certainty for Bank Products Act, we request that it interpret that Act to exempt from the CFTC's jurisdiction loans made by Farm Credit System institutions. This is necessary because Dodd-Frank introduces ambiguity into the definitions of "bank" and "identified banking product" under the Legal Certainty for Bank Products Act. As enacted in 2000, that Act defines an "identified banking product," which is excluded from the CFTC's jurisdiction, to include, among other things, "a letter of credit issued or loan made by a bank."[9] The Act states, in turn, that in applying the definition of "identified banking product," the word "bank" means a depository institution, a foreign bank or foreign bank branch, a credit union, a corporation organized under Section 25A of the Federal Reserve Act, a corporation operating under Section 25 of the Federal Reserve Act, a trust company, or a subsidiary of any of the above.[10] This section does not reference institutions of the Farm Credit System.

Dodd-Frank amends the Legal Certainty for Bank Products Act to provide that "[a]n appropriate Federal banking agency may except an identified banking product of a bank under its regulatory jurisdiction from the exclusion" for identified banking products subject to certain procedures and determinations.[11] Dodd-Frank further provides that, for Farm Credit

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[9] 7 U.S.C. § 27(b) (providing, among other things, that "the term 'identified banking product' shall have the same meaning as in paragraphs (1) through (5) of section 206(a) of the Gramm-Leach-Bliley Act"); Gramm-Leach Bliley Act, Pub. L. No. 106-102, § 206(a)(3), 113 Stat. 1338, 1393 (1999).

[10] 7 U.S.C. § 27(a)-(b).

[11] Dodd-Frank § 725 (amending Section 403 of the Legal Certainty for Bank Products Act).

System institutions, the Farm Credit Administration is an "appropriate Federal banking agency."[12] Thus, under the Legal Certainty for Bank Products Act, as amended by Dodd-Frank, the Farm Credit Administration may include in the CFTC's jurisdiction an otherwise excluded identified banking product offered by a Farm Credit System institution. This provision cannot be reconciled with the definition of "bank" described above. If the Farm Credit Administration must make a determination to *include* products within the CFTC's jurisdiction, then loans made by Farm Credit System institutions must be identified banking products that are already *excluded* from the CFTC's jurisdiction. In short, this provision presupposes that Farm Credit System institutions are "banks," and should be interpreted as such, for purposes of applying the identified banking product exclusion. There is no relevant difference between loans made by Farm Credit System banks and loans made by other banks that may more clearly fall within the Legal Certainty for Bank Products Act. Loans made by Farm Credit System banks are, in fact, loans made by banks, and should be treated as such.

We further request clarification about the status of Farm Credit System loans. The Commissions proposed interpretive guidance providing that "[f]ixed or variable interest rate commercial loans *entered into by non-banks*" will not be treated as swaps, and then alluded to a separate exclusion for identified banking products effectively providing that commercial loans entered into by banks could not be treated as swaps because they were outside the CFTC's jurisdiction.[13] If Farm Credit System institutions are not banks for purposes of the Legal Certainty for Bank Products Act, then they should not be treated as banks for purposes of the interpretive guidance, such that, consistent with the proposed guidance, a loan entered into by a Farm Credit System institution would not be treated as a swap. If, however, the Commissions interpret Farm Credit System institutions as banks, and loans made by Farm Credit System institutions as identified banking products, then these products would already be excluded from the CFTC's jurisdiction, and interpretive guidance would simply provide additional clarity. Either way, we think the Commissions would reach the correct result that loan products not historically considered to be swaps would not become subject to regulation under Title VII of Dodd-Frank. But we respectfully request that the Commissions clarify that loans made by Farm Credit System institutions will not be swaps either under the Commissions' interpretive guidance, or the Legal Certainty for Bank Products Act, or both.

In sum, the Commissions, and particularly the CFTC, can address or resolve this ambiguity in at least two ways. First, as recommended above, the Commissions should simply clarify that commercial loan products with embedded options are not swaps. Second, the CFTC should further clarify that, given Dodd-Frank's amendment of the Legal Certainty for Bank

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[12] *Id.* § 721(a)(2) (CEA § 1a(2)).

[13] NOPR, 76 Fed. Reg. at 29,833 & n.107 (emphasis added).

Products Act, it is more consistent with current congressional intent to consider Farm Credit System institutions "banks" for purposes of the exclusion for identified banking products.

IV. Loan Participations Should Not Be Considered Swaps Where the Participant Acquires a Beneficial Ownership Interest in the Underlying Loans

The Farm Credit Council further supports the Commissions' guidance with respect to loan participations. As we understand it, this guidance distinguishes between loan participations in which the purchaser is acquiring a current or future direct or indirect ownership interest in the related loan, which the Commissions call "true participations," and loan participations that are "synthetic" transactions. The Commissions would not treat "true participations" as swaps.[14] True participations include both LSTA-style participations, which are intended to effect a true sale, and LMA-style participations, under which a future ownership interest is conveyed.[15] Our members are involved in only LSTA-style participations. Because, as the Commissions noted, these are "true" participations, we agree with the Commissions that they should not be considered swaps. Accordingly, we support the Commissions proposed interpretive guidance, which would not treat LSTA-style participations as swaps.

V. Conclusion

The Farm Credit Council appreciates the opportunity to comment on the Commissions' proposed product definition rules and interpretive guidance. We commend the Commissions for clarifying that consumer and commercial loans and financing facilities offered by Farm Credit System institutions will not be considered swaps because the payment provisions in the loan agreements are not severable from the agreement, and the agreements are not traded on an organized market or over the counter. To provide additional clarity for market participants, however, we respectfully request that the Commissions specify that commercial loans with embedded options will not be considered swaps. Further, to the extent that the Commissions rely on the Legal Certainty for Bank Products Act to exclude certain loan products, we urge the CFTC to interpret Farm Credit System institutions as "banks" and loans made by Farm Credit System institutions as "identified banking products" that qualify for this exclusion. Finally, we support the Commissions' proposed interpretive guidance that it will not treat as swaps "true" loan participations in which the participant acquires a current or future direct or indirect ownership interest in the related loan and the loan participations.

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[14] *See id.* at 29,834.

[15] *See id.*

The Farm Credit Council appreciates the opportunity to comment. If you have any questions or we can provide other information, please do not hesitate to contact us. We would welcome the opportunity to work with the Commissions in developing final rules and interpretive guidance.

Sincerely,

Robbie Boone
Vice President, Government Affairs
Farm Credit Council

cc: Honorable Gary Gensler, Chairman
Honorable Michael Dunn, Commissioner
Honorable Jill E. Sommers, Commissioner
Honorable Bart Chilton, Commissioner
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