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**VIA ELECTRONIC SUBMISSION**

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

Elizabeth M. Murphy
Secretary
U.S. 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**

Dear Mr. Stawick and Ms. Murphy:

On behalf of the Federal Home Loan Banks (the "FHLBanks"), we appreciate this opportunity to comment on the above-referenced proposed rules (the "Proposed Rules") and accompanying interpretive guidance (the "Interpretive Guidance") issued jointly by the Commodity Futures Trading Commission (the "CFTC") and the Securities and Exchange Commission (the "SEC"; and together with the CFTC, the "Commissions"), which, *inter alia*, address the definition of "swap" under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"). The FHLBanks are specifically concerned that the Proposed Rules do not adequately address the overinclusivity of the definition of "swap" in Title VII of the Dodd-Frank Act. As a result, loans and advances made by the FHLBanks and certain other lenders could inadvertently be subject to regulation as swaps.

The FHLBanks previously commented on the overinclusive nature of the statutory definition of "swap" in their comment letter to the CFTC dated September 20, 2010, a copy of which is available at:

http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=26242&SearchText=warren (the "Original FHLBank Comment Letter"). At this time, the FHLBanks maintain their comments in the Original FHLBank Comment Letter, as supplemented by this comment letter.

## I. The FHLBanks

The 12 FHLBanks are government-sponsored enterprises ("GSEs") of the United States, organized under the authority of the Federal Home Loan Bank Act of 1932, as amended, and structured as cooperatives. Each is independently chartered and managed, but the FHLBanks issue consolidated debt obligations for which each is jointly and severally liable. The FHLBanks serve the general public interest by providing liquidity to approximately 8,000 member financial institutions, thereby increasing the availability of credit for residential mortgages, community investments, and other services for housing and community development. Specifically, the FHLBanks provide readily available, low-cost sources of funds to their member financial institutions through loans referred to as "advances."

FHLBank advances serve as an important low-cost funding source for a variety of conforming and nonconforming mortgage loans and thereby support the national housing market, including lending to targeted low- and moderate-income households. FHLBank advances are fully secured with high quality collateral and, in the 78-year history of the FHLBank System, no FHLBank has ever sustained a credit loss on an advance. The FHLBanks' member institutions use FHLBank advances to fund loans that they make and hold in their portfolios and as interim funding for loans that the member institutions sell in the secondary market. Accordingly, it is important that the FHLBanks continue to be able to price and structure their advances in a way that meets the liquidity and funding needs of their member institutions

## II. Definition of "Swap" in the Dodd-Frank Act

Subclause (A)(ii) of the definition of "swap" in §1a(47) of the Commodity Exchange Act (the "CEA") includes "any agreement contract or transaction…that provides for any purchase, sale, payment or delivery (other than a dividend on an equity security) that is dependent on the occurrence, nonoccurrence, or the extent of the occurrence of an event or contingency associated with a potential financial, economic, or commercial consequence." The foregoing language is so broad that it could inadvertently include loans and other advances made by financial entities such as the FHLBanks, an issue that the Commissions acknowledged in the preamble to the Proposed Rules.

The overinclusivity of the swap definition is not problematic for loans and other advances that are "identified banking products" (as defined in §402(b) of the Legal Certainty for Bank Products Act of 2000 (the "LCBPA")) because "identified banking

products" are excluded from the CFTC's jurisdiction pursuant to §403(a) of the LCBPA (as amended by §725(g)(2) of the Dodd-Frank Act).[1] However, FHLBank advances do not qualify as "identified banking products" because the FHLBanks are not "banks," as defined in §402(a) of the LCBPA. While the LCBPA's definition of "bank" includes insured depository institutions, certain foreign banks, credit unions, institutions regulated by the Federal Reserve and trust companies, it does not include the FHLBanks or other GSEs. Accordingly, loans and advances made by the FHLBanks and other GSEs could inadvertently be subject to CFTC regulation as swaps while similar loans and advances made by other financial institutions would not be subject to such regulation.

Notwithstanding the foregoing, it is understood that Congress did not intend for traditional loans such as FHLBank advances to be regulated as swaps and it is clear that the Dodd-Frank Act's new regulatory requirements for swap transactions were not meant to apply to FHLBank advances. As discussed in the Original FHLBank Comment Letter, FHLBank advances are already subject to comprehensive regulation by the Federal Housing Finance Agency (the "FHFA"), a "prudential regulator" under the Dodd-Frank Act. Additional regulation of such advances would not comport with the intent or objectives of the Dodd-Frank Act. In fact, certain provisions of the Dodd-Frank Act explicitly preserve the right of prudential regulators such as the FHFA to set prudential requirements (*e.g.,* capital and margin) for financial institutions subject to their jurisdiction, indicating the sensitivity of Congress to the prudential regulators' role as the primary regulators for such institutions.[2] The primary purpose of the FHLBanks is to provide liquidity to their member financial institutions through their advances. Not surprisingly, FHLBank advances represent the majority of the total assets of the FHLBanks and are the largest category of the FHLBanks' combined assets. Congress surely did not intend to make the CFTC the primary or exclusive regulator for the FHLBanks' primary business activities and largest asset category.

In addition, as noted in the Original FHLBank Comment Letter, it is unclear how many of the Dodd-Frank Act's new requirements for swap transactions would even apply to FHLBank advances. For example, FHLBank advances are not suitable for platform execution, clearing or daily valuations and are already subject to capital, recordkeeping, documentation and collateral requirements imposed by the FHFA. The Dodd-Frank Act's new documentation and collateral requirements for swaps would not only be unworkable for FHLBank advances, but such requirements would also conflict with regulations promulgated by FHFA for the specific purpose of regulating FHLBank

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[1] The FHLBanks do not enter into security-based swaps or security-based swap agreements and therefore this comment letter does not address such products. However, the FHLBanks note that the Section 403(a) of the LCBPA, as amended by Section 725(g)(2) of the Dodd-Frank Act also excludes identified banking products from the definitions of security-based swap and security-based swap agreement.

[2] *See* §731 of the Dodd-Frank Act (§4s(d)(2)(A) of the CEA) ("The Commission may not prescribe rules imposing prudential requirements on swap dealers or major swap participants for which there is a prudential regulator.").

advances.[3] Furthermore, with respect to collateral requirements, FHLBank advances may be secured by mortgage loans, privately issued securities or certain other qualifying real estate-related collateral.[4] The ability of the FHLBanks' member institutions to obtain FHLBank advances and make mortgage loans is, in many cases, dependent on the member institutions' ability to pledge such mortgage loans and related collateral as security for their FHLBank advances. If FHLBank advances were deemed swaps, mortgage loans and other real estate-related collateral would not qualify as eligible collateral and the FHLBanks would consequently not be able to fulfill their statutory duties of providing liquidity to their member institutions.

## III. The Proposed Rules and Interpretive Guidance

### A. FHLBank advances are not swaps.

The Commissions have sought to address the overinclusive nature of the definition of swap in the Dodd-Frank Act through the Interpretive Guidance. In addition to listing certain products and instruments that the Commissions do not consider to be swaps, the Interpretive Guidance contains general "catch-all" language indicating that certain commercial agreements, contracts and transactions other than those specifically listed should not be deemed swaps. According to the general "catch-all" language in the Interpretive Guidance, such commercial agreements, contracts and transactions (1) do not contain severable payment obligations (whether or not contingent); (2) are not traded on an organized market or over-the-counter; and (3) are entered into by commercial or non-profit entities as principals (or by their agents) to serve an independent commercial, business or non-profit purpose, other than speculation, hedging or investment. All FHLBank advances satisfy each of the foregoing criteria and thus should not be deemed to be swaps regulated by the Commissions. Although the FHLBanks believe that they should be able to rely on these "catch-all" provisions as authority that their advances are not swaps, in order to provide clarity and legal certainty, the FHLBanks request that the lists of "non-swaps" in the Interpretive Guidance be revised to explicitly indicate that loans and advances satisfying the above criteria are not swaps.

### B. The Interpretive Guidance's List of "Non-Swaps" Should Be Revised to Treat FHLBank Advances in the same Manner as Loans with Identical Terms Made by Other Banks.

In order to document the full intent of Congress and the Commissions, the FHLBanks believe that certain provisions of the Interpretive Guidance pertaining to loans should be revised to clarify that FHLBank advances are the types of loans that are not considered "swaps" under the Dodd-Frank Act. **Specifically, the FHLBanks believe**

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[3] *See* FHFA Regs. §950.2 (documentation) and §§950.7-.10 (collateral requirements).

[4] FHFA Reg. §950.7.

**that the Interpretive Guidance should indicate that all loans made by lenders that are not "banks" as defined in Section 402(a) of the LCBPA would not be considered swaps for purposes of the Dodd-Frank Act.** Alternatively, the Interpretive Guidance could indicate that all such loans are not swaps if they are made by lenders subject to the jurisdiction of a prudential regulator and/or that all such loans are not swaps if they satisfy the Interpretive Guidance's "catch-all" criteria discussed above.

*1.* *Definition of non-bank.* The exclusion from the CEA for identified banking products is meant to address the fact that such products are already subject to comprehensive regulation by prudential regulators and should not be subject to duplicative and/or conflicting regulation by the CFTC. As noted above, the Dodd-Frank Act itself recognizes the role of such prudential regulators as the primary regulators for the financial institutions within their respective jurisdictions. However, in order to effectuate the full intent of such exclusion for identified banking products, the definition of "bank" must be broadened to include lenders such as the FHLBanks. The Commissions have sought to achieve that effect by indicating in the Interpretive Guidance that fixed or variable rate commercial loans entered into by non-banks would not be considered swaps. However, the Interpretive Guidance does not define or reference a definition of "non-bank."

In order to fully bridge the gap between the definition of "identified banking product" and the Interpretive Guidance's exclusion for certain commercial loans, the FHLBanks believe that the Commissions should clarify that "non-bank" means "any lender that is not a bank as defined in Section 402(a) of the LCBPA." Otherwise, certain financial institutions such as the FHLBanks could be lost in a definitional "no-man's land." Loans and advances made by "banks," as defined in Section 402(a) of the LCBPA, would be excluded from all regulation under the CEA and loans made by entities not generally considered to be "banks" would be excluded from the definition of swap as loans made by "non-banks." However, loans and advances made by financial institutions, such as the FHLBanks, that are generally considered to be "banks" but that are excluded from the LCBPA's definition thereof, could be regulated as swaps. At the very least, the Interpretive Guidance should be revised to indicate that loans entered into by "lenders subject to regulation by a prudential regulator" would not be considered swaps.

*2.* *Loans made by non-banks.* As noted above, the Interpretive Guidance indicates that fixed or variable rate commercial loans entered into by non-banks would not be considered swaps. However, the definition of "identified banking product" in the LCBPA covers, *inter alia*, all loans made by a bank. Accordingly, the FHLBanks believe that the exclusion from the definition of swap in the Interpretive Guidance should similarly apply to all loans and not just fixed or variable rate commercial loans.

The FHLBanks make fixed and variable rate advances, some of which may include features such as interest rate caps or floors and prepayment terms that may include a prepayment fee. Although the FHLBanks believe that all such advances should

be considered "fixed or variable rate commercial loans," the Interpretive Guidance does not clarify this point, resulting in undesirable uncertainty. If loans or advances with such embedded features were to be made by a "bank" under the LCBPA, they would be entirely excluded from the CFTC's jurisdiction as "identified banking products." The FHLBanks do not believe such products should be regulated differently merely because they are not made by a "bank" under the LCBPA. This is particularly true with respect to loans and advances made by institutions such as the FHLBanks, which are highly regulated by a prudential regulator but nevertheless are not "banks" under the LCBPA.

If the Commissions choose not to indicate that all loans made by lenders that are not "banks" under the LCBPA are not swaps, the Commissions could indicate that such loans are not swaps if they (1) are made by institutions subject to the jurisdiction of a prudential regulator and/or (2) satisfy the Interpretive Guidance's "catch-all" criteria discussed above.

## IV. The Commissions' Anti-Evasion Authority

As noted in the preamble to the Proposed Rules, Section 725(g) of the Dodd-Frank Act amends the LCBPA to provide that, although identified banking products generally are excluded from the CEA, that exclusion shall not apply to an identified banking product (1) made by a bank that is not under the jurisdiction of an appropriate Federal banking agency, (2) that meets the definition of "swap" or "security-based swap" and (3) that has been *structured as an identified banking product for the purpose of evading* the provisions of the, the Securities Act of 1933 or the Securities Exchange Act of 1934. In addition, the CFTC's portion of the Proposed Rules provides that those transactions that are willfully structured to evade the provisions of Title VII governing the regulation of swaps will be deemed to be swaps.[5] Thus, the Commissions may revise the Interpretive Guidance as discussed above in order to provide clarity and legal certainty for bona fide lenders without worrying about whether such revisions would become a "loophole" from the Dodd-Frank Act's new regulatory regime for swap transactions. If any lenders, whether regulated by an appropriate Federal banking agency, a prudential regulator or neither, intentionally structure their swaps as loans or identified banking products in order to avoid regulation, the CFTC would nonetheless have regulatory jurisdiction over such swaps.

## V. Conclusion

For the reasons discussed above, the FHLBanks believe that the Commissions should clarify that FHLBank advances should not be deemed swaps under the Dodd-Frank Act. Such a determination would be consistent with the intent and purposes of Title VII of the Dodd-Frank Act and consistent with the steps already taken by the Commissions to clarify that similar loans and commercial products would not be

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[5] Proposed CFTC Reg. §1.3(xxx)(6).

considered swaps. While the FHLBanks maintain that none of their advances should be regulated as swaps regardless of whether the Commissions include such a clarification in their final rules and/or interpretive guidance on the definition of swap, the FHLBanks believe that such a clarification is necessary and desirable to provide legal certainty.

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The FHLBanks appreciate the opportunity to comment. Please contact Warren Davis at (202) 383-0133 or warren.davis@sutherland.com with any questions you may have.

Respectfully submitted,

Warren Davis/AMB

Warren Davis, Of Counsel
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cc: FHLBank Presidents
FHLBank General Counsel