November 4, 2011

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

Re: Customer Clearing Documentation and Timing of Acceptance for Clearing (RIN 3038—AD51; Swap Transaction Compliance and Implementation Schedule: Trading Documentation and Margining Requirements under Section 4s of the CEA (RIN 3038-AC96; 3038AC-97); and, Transaction Compliance and Implementation Schedule: Clearing and Trade Execution Requirements under Section 2(h) of the CEA (RIN 3038-AD-60)

Dear Mr. Stawick,

The Association of Institutional INVESTORS (the "Association")[1] appreciates the opportunity to provide comments related to proposed rules on customer documentation, clearing and the related compliance implementation schedules promulgated under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act").[2]

On August 1, 2011, the Commodity Futures Trading Commission ("CFTC" or "Commission") published a proposed rule on customer clearing documentation and the timing of acceptance for clearing (the "Proposed Documentation Rule").[3] On September 20, 2011, the Commission published two rulemakings related to the Proposed Documentation Rules. These proposed rulemakings provide a compliance and implementation schedule for (i) the new trading documentation and margining requirements,[4] and (ii) the new trade execution and clearing requirements[5] (collectively referred to as the "Proposed Implementation Rules").

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[1] The Association of Institutional INVESTORS is an association of some of the oldest, largest, and most trusted investment advisers in the United States. Our clients are primarily institutional investment entities that serve the interests of individual investors through public and private pension plans, foundations, and registered investment companies. Collectively, our member firms manage ERISA pension, 401(k), mutual fund, and personal investments on behalf of more than 100 million American workers and retirees. Our clients rely on us to prudently manage participants' retirements, savings, and investments. This reliance is built, in part, upon the fiduciary duty owed to these organizations and individuals. We recognize the significance of this role, and our comments are intended to reflect not just the concerns of the Association, but also the concerns of the companies, labor unions, municipalities, families, and individuals we ultimately serve.

[2] *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111–203, 124 Stat. 1376 (2010).

[3] *See* Customer Clearing Documentation and Timing of Acceptance for Clearing, 76 Fed. Reg. 45,730 (Aug. 1, 2011).

[4] *See* Swap Transaction Compliance and Implementation Schedule: Trading Documentation and Margining Requirements under Section 4s of the CEA, 76 Fed. Reg. 58,176 (Sept. 20, 2011).

[5] *See* Transaction Compliance and Implementation Schedule: Clearing and Trade Execution Requirements under Section 2(h) of the CEA, 76 Fed. Reg. 58,186 (Sept. 20, 2011).

The Association recognizes the efforts undertaken by the Commission to implement these new requirements with minimal market disruption. Nonetheless, there are some common concerns regarding the Proposed Documentation Rule and the Proposed Implementation Rules shared by our members. As explained below, we support the principle-based approach found in the Proposed Documentation Rule, however we believe the Commission should enhance the Proposed Implementation Rules by providing a more concrete implementation schedule and clarifying the terms "active fund" and "third-party subaccounts."

I. PROPOSED DOCUMENTATION RULE

In the Proposed Documentation Rule, the Commission sets out general standards governing customer documentation together with a limited number of specific well-tailored limitations. In particular, the proposed rule would prevent certain Commission registrants (futures commission merchants (FCMs), swap dealers, and major swap participants) from entering into an arrangement with a customer that would disclose the identity of the customer's original executing counterparty. The proposed rule would also prevent these Commission registrants from (1) limiting the number of counterparties with whom a customer may enter into a trade; (2) restricting the size of the position a customer may take with any individual counterparty, apart from an overall credit limit for all positions held by the customer; (3) impairing a customer's access to execution of a trade on terms that have a reasonable relationship to the best terms available; and (4) preventing compliance with specified time frames for acceptance of trades into clearing.[6]

The Association supports the Commission's principles-based approach found in the Proposed Documentation Rule and believes these broad standards will encourage greater open access to clearing. More importantly, we believe the principles-based approach fosters open access in a manner that still allows market participants the ability to determine the terms most appropriate for their needs. It is essential that the final rule recognize that the details of these arrangements should be left to market participants to decide, ensuring that these transactions are crafted in the manner best suited for serving our clients' needs.

II. PROPOSED IMPLEMENTATION RULES

The Proposed Implementation Rules establish a phased-in compliance schedule setting effective dates for the Commission's clearing mandate, trade execution requirements, documentation standards, and margin requirements for uncleared swaps. Under the proposed schedules, depending on how the Commission categorizes the trading entity and corresponding counterparty to the trade, the trading entity must comply with the clearing mandate and related requirements either 90, 180, or 270 days after the effective date for the Proposed Implementation Rules (the "Phase-In Dates"). The Proposed Implementation Rules would not prohibit an entity from complying voluntarily with the clearing mandate and related requirements sooner than the proposed implementation schedule requires.[7]

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[6] *See* Customer Clearing Documentation and Timing of Acceptance for Clearing, 76 Fed. Reg. at 45,731.

[7] *See* Swap Transaction Compliance and Implementation Schedule: Trading Documentation and Margining Requirements under Section 4s of the CEA, 76 Fed. Reg. at 58,185, and Transaction Compliance and Implementation Schedule: Clearing and Trade Execution Requirements under Section 2(h) of the CEA, 76 Fed. Reg. at 58,186.

The first group of participants, "Category 1" entities, has 90 days after the effective date to be compliant with the clearing mandate and related execution requirements. Category 1 entities include swap dealers, security-based swap dealers, major swap participants, major security-based swap participants, or active funds. The proposed definition of "active fund" would mean any private fund as defined in section 202(a) of the Investment Advisors Act of 1940, that is not a third-party subaccount and that executes 20 or more swaps per month based on a monthly average over 12 months.[8]

"Category 2" entities have 180 days to ensure compliance. Category 2 entities include commodity pools; private funds as defined in Section 202(a) of the Investment Advisors Act of 1940 other than active funds; employee benefit plans identified in paragraphs (3) and (32) of section 3 of the Employee Retirement Income and Security Act of 1974; or persons predominantly engaged in activities that are in the business of banking, or in activities that are financial in nature as defined in Section 4(k) of the Bank Holding Company Act of 1956, provided that the entity is not a third-party subaccount.[9]

Finally, "Category 3" entities encompass all other entities and transactions not covered by Categories 1 and 2, and includes transactions involving third-party subaccounts and those not excepted from the mandatory clearing requirement. Category 3 entities are provided 270 days to bring their transactions into compliance once the requirements are finalized.[10]

The Association supports the principles behind the Proposed Implementation Rules and its phase-in approach based on entity type. Nonetheless, there are concerns about the practical application of these proposals. Our chief concern is that the proposed Phase-In Dates do not provide adequate time for institutional investment advisers and their clients to complete the necessary client documentation to ensure compliance by the effective dates. Furthermore, the proposals are dependent upon too many varying factors, such as unfinished rulemakings and pending definitions, to provide our members with a reliable schedule, hindering efforts to prepare for the clearing mandate and related regulatory requirements. Finally, there are additional concerns regarding how these proposals have defined both "active funds" and the "third-party subaccounts." Each of these issues is discussed in further detail below.

1. Implementation Schedule

Unfortunately, the proposed Phase-In Dates do not provide sufficient time to complete the voluminous amount of documentation required between our member firms and their clients. The challenges of this undertaking are compounded by the fact that substantial portions of the documentation required cannot be completed until the Commission has finalized other aspects of their rulemaking agenda, such as product and entity definitions as well as standards for margin. The documentation requires negotiations and agreements be made across thousands of accounts with numerous counterparties, and be done in a concurrent manner. At the same time, our members will also be working to update their operations to comply with not only the CFTC's new regulations, but

[8] *Id.*
[9] *Id.*
[10] *Id.*

also the new regulatory mandates and registration requirements being issued by the Securities and Exchange Commission ("SEC"), the Department of Treasury, various self-regulatory organizations ("SROs"), the Department of Labor for ERISA accounts, and other financial regulatory authorities.

The Proposed Implementation Rules are also dependent on several yet-to-be completed rulemakings. As CFTC Commissioner Scott O'Malia has highlighted, the compliance schedule on clearing and trade execution cannot be triggered until the Commission finalizes at least five rulemakings, including: (i) entity definitions; (ii) the end-user exception; (iii) the protection of cleared swaps customer contracts and collateral; (iv) core principles for designated contract markets; and (v) core principles for swap execution facilities. Moreover, the proposals provide no indication as to when the Commission anticipates finalizing these rulemakings.[11]

The uncertainty regarding the phase-in timeline, and the application of the Proposed Implementation Rules in general, presents a substantial challenge for certain larger investment adviser firms that must make arrangements to meet all three of the Phase-In Dates because of the varying aspects of their business operations, and do so in a manner best suited for each individual client. For example, asset managers may have difficulty executing block trades for multiple clients who fall into varying entity categories. If a block trade is initiated before the final phase-in date, the asset manager will need to consider whether the entire trade must comply with the clearing requirement or if only those positions allocated with active funds must be cleared. Such a situation creates a substantial logistical challenge for the Association members.

An unnecessarily truncated compliance deadline also creates an imbalance in the negotiation efforts taking place between institutional investment advisers and the dealers. The major dealers that operate in these markets have indicated that there is a limit to how many entities can negotiate with them at a given time. As such, institutional investment advisers may become pressured to "rush" the documentation process or risk being shut out of the market once these rules become effective. This situation harms institutional investment advisers and their clients by limiting their ability to adequately evaluate and negotiate these agreements. Furthermore, once these terms are established, it is difficult to renegotiate these agreements. Ultimately, this could lead to terms more favorable for dealers that are a result of situational demands rather than our clients' needs.

The lack of clear deadlines and their ambiguous application frustrates efforts by investment advisers to plan for and execute the necessary arrangements to ensure compliance once these rules are finalized and effective. The cumulative effect of these circumstances means that our members must meet a moving target, and do so with limited resources that are under unprecedented strain while simultaneously coordinating efforts with thousands of clients and counterparties who are in the same precarious situation. Additionally, the uncertainty around these issues has the potential to effect the institutional adviser's requirement to fairly allocate trading decisions irrespective of the size of a particular client account. Thus, without further clarity the Proposed Implementation Rules risks being an obstacle rather than a solution that actually delays the overall implementation efforts.

The Association recommends that the Commission first finalize other rulemakings, (i.e. margin requirements, definitions, etc.) before setting an effective date for clearing. Once these rules are

[11] Comments of CFTC Commissioner Scott O'Malia, *available at:* http://www.cftc.gov/PressRoom/Events/ssLINK/omaliastatement090811.

finalized the Commission should then finalize the clearing requirement, and provide all entities with 18 months or more to bring their operations into compliance in a manner utilizing the entity categories as proposed in the Proposed Implementation Rules. This would provide investment advisers and their clients the necessary time to complete the necessary documentation, and to do so in a fair manner.

2. Entity Categories

The Association has concerns about the Proposed Implementation Rules regarding how the Commission has defined the terms "active funds" and "third-party subaccounts."

a. Active Funds

The term "active funds" is arbitrary and too ambiguous as currently provided for in the Proposed Implementation Rules. If the rule is intended to be limited to only 20 individual swaps a month, this limit appears to be an arbitrary ceiling that lacks supporting data. The Association believes a more appropriate standard can be established after the definitions are finalized and the Commission has a chance to collect additional market data. After collecting and analyzing this data as well as consulting with market participants, the Commission is likely to find that a much higher limit is more appropriate and better reflects current industry practices.

In addition, the Commission should further clarify how the term "swap" is used in the context of its definitional phrase "…that executes 20 or more *swaps* per month." It is unclear whether this encompasses all swap activity in general, including hedge transactions and step-out transactions through a novation or assignment, or only transactions in particular asset classes or products. The Association believes in particular swaps entered into for hedging purposes should be excluded in this calculation, or otherwise accounted for when establishing this definitional limit. Once again, the Association believes the CFTC may more appropriately determine which swaps should be included in the limit after collecting and analyzing additional market data.

b. Subaccounts

The Proposed Implementation Rules designates what the Commission calls "third-party subaccounts" as Category 3 entities, which are provided 270 days to bring their operations into compliance.[12] The Proposed Implementation Rules define a third-party subaccount as "a managed account that requires specific approval by the beneficial owner of the account to execute documentation necessary for executing, confirming, margining, or clearing swaps."[13] As institutional investment advisers, this definition has important implications for our member firms and their clients, particularly with regard to what are commonly known as "institutional separate accounts," or just simply "separate accounts." The Commission's proposed definition is inconsistent with current industry standards, as these separate accounts do not uniformly require advisers to have document execution authority. Thus, the proposed definition of "third-party subaccounts" is overly narrow,

[12] *See* Swap Transaction Compliance and Implementation Schedule: Trading Documentation and Margining Requirements under Section 4s of the CEA, 76 Fed. Reg. at 58,185, and Transaction Compliance and Implementation Schedule: Clearing and Trade Execution Requirements under Section 2(h) of the CEA, 76 Fed. Reg. at 58,186.
[13] *Id.*

and risk excluding numerous accounts that are widely recognized by market participants as separate accounts.

Document execution authority is not a defining trait of third-party subaccounts. While advisers may not have authority to sign these agreements, they are primarily responsible for all of the work behind the accounts, and thus the "authority to sign" distinction is an inappropriate manner to distinguish as to what is and is not a sub-account. Moreover, if the Commission retains the document execution authority as the distinguishing factor, it is possible that this may increase the amount of documentation required and further lengthen the implementation process. Therefore, we request that the Commission define "third-party subaccounts" to include all separate accounts, irrespective of the manager's authority to sign.

III. CONCLUSION

The Association recognizes the challenges the CFTC faces in implementing these new requirements and appreciates the Commission's consideration of our concerns. The Association thanks the Commissions for the opportunity to comment on these proposed rules. Please feel free to contact me with any questions you may have on our comments at jgidman@loomissayles.com or (617) 748-1748.

On behalf of the Association of
Institutional INVESTORS,

John R. Gidman

cc: Honorable Gary Gensler, Chairman
Honorable Bart Chilton, Commissioner
Honorable Mark Wetjen, Commissioner
Honorable Scott O'Malia Commissioner
Honorable Jill Sommers, Commissioner
Commodity Futures Trading Commission