

KfW Bankengruppe, Postfach 111141, 60046 Frankfurt am Main

## Via Agency Web Site

Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21st Street, NW  
Washington, DC 20581

Jochen Leubner  
Our ref.: Lbn  
Phone: +49 69 7431-2569  
Fax: +49 69 7431-4324  
E-mail: jochen.leubner@kfw.de  
Date: 09-07-2012

Attention: David A. Stawick  
Secretary, Commodity Futures  
Trading Commission

**Re: CFTC; Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants (RIN 3038-AC97)**

Dear Mr. Stawick:

We are submitting this comment letter in response to the April 28, 2011 Notice of Proposed Rulemaking on Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 76 Fed. Reg. 23,732 (April 28, 2011), issued by the Commodity Futures Trading Commission (the "CFTC"), and the CFTC's extension of the comment period on that release, 77 Fed. Reg. 41,109 (July 12, 2012). We appreciate the opportunity to comment on the proposed requirements set forth in the Notice of Proposed Rulemaking, pursuant to Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank").

This comment letter is submitted on behalf of KfW, and the views expressed herein are those of KfW only. For the reasons described herein, we believe that the use of Swaps, as defined under Dodd-Frank, by KfW, which, as explained below, is a foreign government-linked entity owned by the Federal Republic of Germany (the "Federal Republic") and the German federal states and the obligations of which are backed by the full faith and credit of the Federal Republic due to a statutory guarantee, should not be subject to the regulatory scheme imposed by Dodd-Frank. Accordingly, we respectfully request that the CFTC use the authority provided by Dodd-Frank to exclude any agreement, contract or transaction a counterparty of which is KfW from the requirement to post initial and variation margin.

## I. Background on KfW

### *Legal Status, Ownership and Statutory Guarantee*

KfW is a German public law institution (*Anstalt des öffentlichen Rechts*) organized under the Law Concerning KfW (*Gesetz über die Kreditanstalt für Wiederaufbau*, or "KfW Law"). The Federal Republic holds 80% of KfW's equity capital and the German federal states hold the remaining 20%.



The KfW Law expressly provides that the Federal Republic guarantees all existing and future obligations of KfW in respect of money borrowed, bonds and notes issued and derivative transactions entered into by KfW (KfW Law, Article 1a). Under this statutory guarantee (the "Guarantee of the Federal Republic"), if KfW fails to make any payment of principal or interest or any other amount required to be paid with respect to any of KfW's obligations mentioned in the preceding sentence, the Federal Republic will be liable at all times for that payment as and when it becomes due and payable. The Federal Republic's obligation under the Guarantee of the Federal Republic ranks equally, without any preference, with all of its other present and future unsecured and unsubordinated indebtedness. Creditors who have a claim against KfW resulting from one of the obligations mentioned in the first sentence of this paragraph may enforce this obligation directly against the Federal Republic without first having to take legal action against KfW. Against this background, these obligations of KfW, both financially and in terms of legal recourse, are viewed as sovereign credits and KfW, like the Federal Republic, enjoys a triple A credit rating.

Furthermore, as a public law institution, KfW benefits from the German administrative law principle of *Anstaltslast*, according to which the Federal Republic, as the constituting body of KfW, has an obligation to safeguard KfW's economic basis. Under *Anstaltslast*, the Federal Republic must keep KfW in a position to pursue its operations and enable it, in the event of financial difficulties, through the allocation of funds or in some other appropriate manner, to meet its obligations when due. Although *Anstaltslast* is not a formal guarantee of KfW's obligations by the Federal Republic, the effect of this legal principle is that KfW's obligations are fully backed by the credit of the Federal Republic on this basis as well, in addition to the Guarantee of the Federal Republic referred to above.

#### *Purpose*

KfW was established in 1948 by the Administration of the Combined Economic Area, the immediate predecessor of the Federal Republic. Originally, KfW's purpose was to distribute and lend funds of the European Recovery Program (the "ERP"), which is also known as the Marshall Plan. Even today, several of KfW's programs to promote the German and European economies are supported using funds for subsidizing interest rates from the so-called "ERP Special Fund". Over the past decades, KfW has expanded and internationalized its operations. Today, KfW serves domestic and international public policy objectives of the German federal government, primarily by engaging in various promotional lending activities.<sup>1</sup>

As a government-sponsored bank, KfW does not seek to maximize profits and is prohibited from distributing profits, which are instead allocated to statutory and special reserves. KfW is also prohibited from taking deposits, conducting current account business or dealing in securities for the account of others.

---

<sup>1</sup> KfW's lending activities include: domestic financing, primarily made through commercial banks, including loans to small and medium-sized enterprises, housing-related loans, grants and financings to individuals for educational purposes, financing for infrastructure projects and global funding instruments for promotional institutes of the German federal states (*Landesförderinstitute*); export and project finance through its wholly-owned subsidiary KfW IPEX-Bank GmbH ("KfW IPEX-Bank"); and development finance for developing and transition countries, including private-sector investments in developing countries through its wholly-owned subsidiary DEG—Deutsche Investitions- und Entwicklungsgesellschaft mbH ("DEG").



### *Governance and Supervision*

KfW is governed by an Executive Board (*Vorstand*) and a Board of Supervisory Directors (*Verwaltungsrat*). The Executive Board is responsible for the day-to-day conduct of KfW's business and the administration of its assets. The Board of Supervisory Directors, which, among others, consists of seven Federal ministers<sup>2</sup>, supervises the overall conduct of KfW's business and the administration of its assets.

Under the KfW Law, the Federal Ministry of Finance, in consultation with the Federal Ministry of Economics and Technology, supervises KfW and has the power to adopt all measures necessary to safeguard the compliance of KfW's business operations with applicable laws, KfW's by-laws and other regulations.

In addition to the annual audit of its financial statements, KfW, as a government-owned entity, is subject to an audit that meets the requirements of the German Budgeting and Accounting Act (*Haushaltsgrundsätze-gesetz*). One of the specific aspects to be covered by this audit and the related reporting is the proper conduct of KfW's business by its management.

### *Funding Activities and Derivatives Transactions*

KfW finances the majority of its lending activities from funds raised by it in the international financial markets. KfW issues debt instruments in various currencies, primarily the Euro and the U.S. dollar (which accounted for 50% and 29% of KfW's new capital-market funding in 2011, respectively). As of December 31, 2011 KfW's total outstanding funded debt amounted to EUR 365.0 billion. On the basis of a no-action letter issued by the SEC on September 21, 1987, KfW, in connection with global debt offerings in an aggregate amount equivalent to close to EUR 350 billion, has registered debt securities with the SEC under Schedule B of the Securities Act of 1933, which is applicable to foreign governments or political subdivisions thereof, and more than 50% of KfW's funded debt outstanding on December 31, 2011 consisted of debt securities sold in these global debt offerings.

KfW enters into derivatives transactions in order to manage the risks incurred by it and its wholly-owned subsidiaries KfW IPEX-Bank and DEG in connection with its financing and funding activities. Such risks are almost entirely associated with changes in interest rates and foreign exchange rates. As U.S. dollar bonds make up a significant portion of KfW's financing and funding activities, KfW generally has large over-the-counter ("OTC") positions in derivatives hedging changes in the Euro/U.S. dollar exchange rate. Many of KfW's counterparties are dealers based in the United States. As of December 31, 2010, the total

---

<sup>2</sup> Generally, the Supervisory Board has 37 members and consists of the Federal Minister of Finance; the Federal Minister of Economics and Technology; the Federal Minister of Foreign Affairs; the Federal Minister of Food, Agriculture and Consumer Protection; the Federal Minister of Transport, Building and Urban Affairs; the Federal Minister for Economic Cooperation and Development; the Federal Minister for the Environment, Nature Conservation and Nuclear Safety; seven members appointed by the *Bundesrat*; seven members appointed by the *Bundestag*; five representatives of commercial banks; two representatives of industry; one representative each of the local municipalities, agriculture, crafts, trade and the housing industry; and four representatives of the trade unions. The representatives of the commercial banks, industry, the local municipalities, agriculture, crafts, trade, the housing industry and the trade unions are appointed by the German Federal government after consultation with their constituencies.



notional amount of derivatives outstanding amounted to EUR 713 billion equivalent (on a consolidated basis), of which close to 25% (by notional amount) were executed with U.S. counterparties (including non-U.S. affiliates of U.S. counterparties). KfW enters into these transactions solely for purposes of hedging risks incurred by it and its wholly-owned subsidiaries KfW IPEX-Bank and DEG, and KfW does not and, in accordance with Article 2 paragraph 3 of the KfW Law, may not, engage in proprietary or speculative trading. Further, KfW does not accommodate demand for swaps from other parties nor enter into swaps in response to interest expressed by other parties in the manner a dealer would customarily do, except that, in the context of centralizing and aggregating market-facing hedging activities within the group at the parent level, KfW accommodates demand for swaps by its wholly-owned subsidiaries KfW IPEX-Bank and DEG for their hedging activities. KfW therefore considers itself as an end-user customer of derivatives.

All of KfW's OTC derivatives transactions are concluded under appropriate derivatives master agreements (such as the ISDA Master Agreement and the German Master Agreement for Financial Derivatives Transactions). As part of KfW's risk policy, KfW's exposures under such derivatives master agreements generally are to be collateralized by KfW's counterparties. While KfW receives collateral from its counterparties under credit support annexes pertaining to the respective derivatives master agreement, it generally does not provide collateral itself for purposes of mitigating credit risk, because, as mentioned above, its obligations are backed by the Guarantee of the Federal Republic. Internal guidelines require that no transaction is executed outside such (collateralized) derivatives master agreements.

## **II. Treatment of Foreign Governments and KfW under certain Final Rules issued by the CFTC under Title VII of Dodd-Frank**

In the CFTC's release of the final rules regarding the further definition of "Swap Dealer," "Major Swap Participant," and other matters, the CFTC stated that foreign governments, foreign central banks and international financial institutions should not be required to register as SDs or MSPs and it clarified that it considers KfW a foreign government for this purpose.<sup>3</sup> Furthermore, in its release of the final rules regarding the end-user exception to clearing requirements for Swaps, the CFTC similarly stated that foreign governments, foreign central banks and international financial institutions will not be subject to the requirement under Dodd-Frank that Swap transactions be cleared through a derivatives clearing organization and it also clarified that it considers KfW a foreign government for this purpose.<sup>4</sup>

The CFTC has therefore recognized that foreign sovereign entities in particular should be distinguished from other non-U.S. persons and excluded from certain of the most significant regulatory requirements and that KfW should be treated as a sovereign for these purposes. In so doing, the CFTC acknowledged that "[t]here is nothing in the text or history of the swap-related provisions of Title VII to establish that Congress intended to deviate from the

---

<sup>3</sup> See CFTC and the Securities and Exchange Commission, Further Definition of "Swap Dealer," "Security-Based Swap Dealer," "Major Swap Participant," "Major Security-Based Swap Participant" and "Eligible Contract Participant," 77 Fed. Reg., 30,596, 30,692-93 (May 23, 2012).

<sup>4</sup> See CFTC, "End-User Exception to the Clearing Requirement for Swaps," 77 Fed. Reg. 42,560 (July 19, 2012).



traditions of the international system by including foreign governments, foreign central banks and international financial institutions within the definitions of the terms "swap dealer" or "major swap participant," thereby requiring that they affirmatively register as swap dealers or major swap participants with the CFTC and be regulated as such."

We respectfully submit that it would be completely inconsistent, in light of these statements, to subject KfW to regulatory margin requirements under the CFTC's rules. Conversely, excluding KfW from these requirements is the logical extension of the actions the CFTC has taken with respect to KfW in these other instances. We believe that the provisions in the margin rules, taken together with the CFTC's statements and reasoning in the releases accompanying the final definitions of SDs and MSPs and the rules applicable to end-users, similarly warrant excluding foreign governments (including KfW) from the requirement to post initial and variation margin. Accordingly, we respectfully request that the CFTC confirm the exclusion of foreign governments (including KfW) from the requirement to post initial and variation margin in its finalization of the proposed rules.

### **III. Exception from the Proposed Margin Requirements for Entities Such as KfW**

If the CFTC's regulations requiring initial and variation margin posting for Swaps not cleared through a derivatives clearing organization are adopted as currently proposed, KfW could be required to post margin in connection with its Swaps transactions if its counterparties are registered SDs or MSPs, notwithstanding KfW's limited purpose in entering into Swaps as outlined under I. above and despite the fact that it is backed by the full faith and credit of the Federal Republic. We do not believe that this result is warranted or appropriate, or that it will operate to reduce systemic risk or to protect market participants. To the contrary, it will serve only to increase the cost, and reduce the efficiency, of necessary hedging transactions entered into by KfW, and perhaps force it to transact primarily or exclusively with non-U.S. counterparties.

In light of the significant losses occurred during the financial crisis, particularly in connection with uncleared Swaps, Dodd-Frank amended the Commodity Exchange Act (the "CEA") to account for the need to address the added risk posed by Swaps that are not cleared through a clearing house. CEA Section 6(s)(e)(3)(A) addresses the need to offset the greater risk from uncleared Swaps posed to SDs and MSPs, and the financial system more broadly, and directs the CFTC to adopt requirements that (i) "help ensure the safety and soundness of the swap dealer or major swap participant" and (ii) "be appropriate for the risk associated with the non-cleared swaps held as a swap dealer or major swap participant."

While we support the CFTC's measures to enhance the safety and soundness of, and reduce systemic risk to, the overall financial system, the proposed establishment of margin requirements for uncleared Swaps was prompted by the failure of profit-maximizing commercial institutions. As a not-for-profit public entity which serves domestic and international public policy objectives of the German federal government, primarily by engaging in various promotional lending activities, and which is backed by the full faith and credit of the Federal Republic, KfW does not pose the type of risk to counterparties, both U.S. and non-U.S., and the wider financial system that the proposed margin requirements seek to rectify.

The Dodd-Frank amendments to the CEA required that the regulations adopted by the CFTC to address the risk caused by uncleared Swaps be "appropriate" for the actual risk posed. Requiring entities such as KfW to post margin on their Swap transactions would neither

be “appropriate” nor be necessary to mitigate the type of risk that the proposed margin requirements seek to rectify. An exemption from posting margin requirements on uncleared Swaps would not be inconsistent with the principles guiding the CFTC’s rulemaking and would avoid placing an unnecessary burden on KfW.

Therefore, we respectfully submit that entities such as KfW, which are not-for-profit public entities backed by the full faith and credit of a sovereign, should not be required to post initial or variation margin on Swaps transactions not cleared through a clearing house.

#### **IV. Basel Commission on Banking Supervision (“BCBS”) and International Organization of Securities Commissions (“IOSCO”) Working Group on Margin Requirements (the “WGMR”) and Request for Relief**

The CFTC reopened the comment period for the proposed rules on margin in order to provide interested parties an opportunity to comment concurrently on the WGMR Consultive Document on Margin Requirements for Non-Centrally-Cleared Derivatives (the “WGMR Paper”) issued in July 2012 and on the proposed rules. In this regard, we note that the WGMR Paper provides that “BCBS and IOSCO broadly supported not applying the margin requirements in a way that would require sovereigns or central banks to either collect or post margin. Both of these views are reflected by the effective exclusion of such transactions from the scope of the margin requirements proposed in this consultative paper.”<sup>5</sup> Based on these statements, we expect the WGMR to exclude sovereigns and sovereign-linked entities from the scope of the margin requirements in their final recommendations.

Also, the WGMR Paper in Key Principle 7 provides that “[r]egulatory regimes should interact so as to result in sufficiently consistent and non-duplicative regulatory margin requirements for non-centrally cleared derivatives across jurisdictions.”<sup>6</sup> In this context, we note that Article 1 Paragraph 4 and 5 of the so-called European Market Infrastructure Regulation (“EMIR”)<sup>7</sup> provides for both an exemption from the clearing obligation for standardized derivatives in accordance with Article 4 of EMIR and from certain risk mitigation techniques (including but not limited to “exchanging collateral”, i.e. posting and collecting margin) in accordance with Article 11 of EMIR for sovereigns, central banks, multilateral development banks and government-guaranteed public sector entities. KfW is a public sector entity within the meaning of Article 1 Paragraph 5b) of EMIR, and is thus not subject to the clearing obligation nor the margin requirements under EMIR.

We believe that excluding entities such as KfW from the requirement to post initial and variation margin is in line with the approach taken in the WGMR Paper with respect to margin requirements for non-centrally cleared derivatives. Further, taking into consideration the

---

<sup>5</sup> See Basel Committee on Banking Supervision, Board of the International Organization of Securities Commissions, Consultative Document, Margin Requirements for Non-Centrally-Cleared Derivatives, at 9 (July 2012) <http://www.bis.org/publ/bcbs226.pdf>.

<sup>6</sup> *Id.* at 29.

<sup>7</sup> See 2012 O.J. (L 201), Regulation (EU) No 648/2012 of the European Parliament and the Council of July 4, 2012 on OTC Derivatives, Central Counterparties and Trade Repositories, available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:201:0001:0059:EN:PDF>.

exception for government-guaranteed public sector entities from the margin requirements under EMIR, such exclusion would also be in line with Key Principle 7 of the WGMR paper calling for consistent regulatory margin requirements for non-centrally cleared derivatives across jurisdictions and be responsive to Section 752(a) of Dodd-Frank that requires the CFTC to “consult and coordinate with foreign regulatory authorities on the establishment of consistent international standards with respect to the regulation ... of swaps ...” Accordingly, we respectfully request that the CFTC confirm the exclusion of government entities (including KfW) also for the reasons presented in this section in its finalization of the proposed rules.

**V. Conclusion**

There is no evidence suggesting that Congress intended government-owned entities like KfW to be subject to Title VII of Dodd-Frank. KfW’s derivatives transactions did not contribute to the recent financial crisis that resulted in the adoption of Dodd-Frank. Subjecting KfW and its derivative transactions to the margin requirements of Dodd-Frank could have serious adverse effects on its ability to cost-efficiently hedge the risks to which it is exposed, thereby increasing costs to its borrowers, and thus may force it to direct hedging transactions currently still concluded with U.S. counterparties to non-U.S. counterparties in the future. Moreover, imposing the margin requirements of Dodd-Frank on KfW and its derivative transactions is unnecessary for the protection of counterparties and the financial system. Finally, an exclusion for KfW from the requirement to post initial and variation margin would be in line with KfW’s treatment in respect of margin requirements under EMIR, be consistent with the expected scope of the WGMR paper and adequately take into account the objective to achieve consistent international regulatory requirements in accordance with Key Principle 7 of the WGMR paper and Section 752(a) of Dodd-Frank.

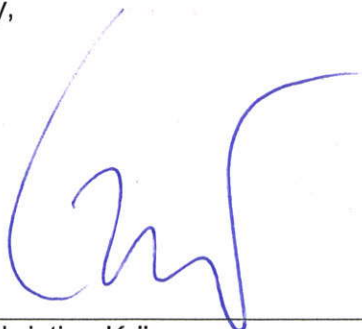
Accordingly, for the reasons set forth above, KfW should not be subject to the Commissions’ proposed margin regulations and, we respectfully submit, should be eligible for the relief described above.

\* \* \*

Thank you for your consideration of our comments and please do not hesitate to contact David J. Gilberg of Sullivan & Cromwell LLP at 212-558-4000 or gilbergd@sullcrom.com if you have questions or would find further background helpful. We have sent a copy of this letter to the Federal Ministry of Finance of Germany in its capacity as KfW’s supervisory authority.

Sincerely,

KfW



Name: Christian Krämer  
Title: First Vice President



Name: Dr. Frank Czichowski  
Title: Senior Vice President and Treasurer