

**WARREN N. DAVIS**  
DIRECT LINE: 202.383.0133  
E-mail: [warren.davis@sutherland.com](mailto:warren.davis@sutherland.com)

April 17, 2014

**VIA ELECTRONIC SUBMISSION**

Ms. Melissa Jurgens  
Secretary of the Commission  
Commodity Futures Trading Commission  
Three Lafayette Center  
1155 21st Street, N.W.  
Washington, DC 20581

**Re: Comments on CFTC Rule 1.35 in Response to the CFTC's Roundtable to Discuss Dodd-Frank End-User Issues**

Dear Ms. Jurgens:

On behalf of the twelve Federal Home Loan Banks (the "FHLBanks"), we appreciate the opportunity to submit this comment letter in response to the Commodity Futures Trading Commission's (the "CFTC" or "Commission") April 3, 2014 public roundtable to discuss certain end-user issues with respect to the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act").<sup>1</sup> Specifically, the FHLBanks provide these comments herein with respect to the recordkeeping requirements under CFTC Rule 1.35 ("Rule 1.35").<sup>2</sup> The following is an overview of the FHLBanks and the FHLBanks' concerns with respect to Rule 1.35.

---

<sup>1</sup> Press Release, CFTC Staff to Host Public Roundtable to Discuss Dodd-Frank End-User Issues (Apr. 3, 2014), *available* [here](#).

<sup>2</sup> 17 C.F.R. § 1.35 (2014) (requiring members of a swap execution facility (among others) to "keep full, complete, and systematic records, which include all pertinent data and memoranda, of all transactions relating to its business of dealing in commodity interests and related cash or forward transactions.").

## **I. The FHLBanks**

The FHLBanks are government-sponsored enterprises of the United States, organized under the authority of the Federal Home Loan Bank Act of 1932, as amended, and structured as cooperatives. Each FHLBank is independently chartered and managed, but the FHLBanks issue consolidated debt obligations for which each FHLBank is jointly and severally liable. The FHLBanks serve the general public interest by providing liquidity to approximately 7,000 members, including banks, thrifts, credit unions, insurance companies and community development financial institutions. In doing so, the FHLBanks help increase 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 funds to their members through loans referred to as “advances.”

The FHLBanks enter into swap transactions as end-users with swap dealers to facilitate their business objectives to safely and soundly provide liquidity to members, and to manage and mitigate their own financial risk, primarily interest rate risk. Notably, due to their unique statutory mission to provide liquidity to members, the FHLBanks use highly customized off-the-run interest rate swaps to manage the risks associated with both the advances they make to their membership and the debt issuance used to fund those advances. As of December 31, 2013, the aggregate notional amount of over-the-counter interest rate swaps held by the FHLBanks collectively was approximately \$539 billion.

At present, the FHLBanks are clearing a significant and growing percentage of their interest rate swap transactions, but the FHLBanks have executed only a small percentage of their swap transactions on or through a swap execution facility (“SEF”). The FHLBanks have not to date executed a large portion of their swap transactions on or through a SEF because of the highly customized nature of the FHLBanks’ swap transactions and the current scope of made-available-to-trade determinations. While it is impossible to predict the percentage of the FHLBanks’ swaps that will ultimately be subject to mandatory SEF execution or how soon this will occur, the FHLBanks expect that over time a significant percentage of the swaps they enter into will be subject to the mandatory clearing requirement and trade execution requirement.<sup>3</sup> As participants in the swaps market, the FHLBanks are subject to the recordkeeping obligations under CFTC Rule 45.2 (“Rule 45.2”).<sup>4</sup> In addition, with respect to executing certain swaps that are subject to the Trade Execution Requirement, the FHLBanks must either become a member of a SEF (and thus comply with Rule 1.35) or execute such swaps through an intermediary service.

---

<sup>3</sup> See Section 2(h) of the Commodity Exchange Act (“CEA”) (the “Clearing Requirement”) and Section 2(h)(8) of the CEA (the “Trade Execution Requirement”).

<sup>4</sup> 17 C.F.R. § 45.2 (2014) (swap recordkeeping).

## **II. Comments of the FHLBanks Regarding Rule 1.35**

### **A. Rule 1.35 Recordkeeping Obligations – General Comment**

As noted above, the FHLBanks, like many market participants, are clearing their swap transactions and are subject to the recordkeeping obligations under Rule 45.2. Further, the recordkeeping requirements under Rule 1.35 are substantially encompassed in the recordkeeping requirements under Rule 45.2. It is unclear why market participants subject to Rule 45.2 and not otherwise required to be registered with the CFTC must also be subject to additional recordkeeping requirements under Rule 1.35 solely because such market participants are required to register as members of a SEF to comply with the Trade Execution Requirement for certain of their swaps. We note that the FHLBank system is highly regulated by the Federal Housing Finance Agency, which also monitors, examines and regulates the FHLBanks' swaps activity. As such, the FHLBanks recommend that any additional recordkeeping obligations under Rule 1.35 be subject to a careful review and cost-benefit analysis against Rule 45.2 to avoid duplicative recordkeeping measures, redundant regulator reviews, and regulatory inconsistency and uncertainty.

### **B. Definition of “Member” Under CFTC Regulations**

#### *1. Traditional Exchange Membership*

The FHLBanks request that the CFTC provide further clarification with respect to the definition of “member” of an exchange. Under the CEA, a “member” of an exchange is a person who has “trading privileges” on that exchange. Traditionally, a key characteristic of exchange “membership” has been serving in a fiduciary capacity for customers by an entity that is required to be registered with the CFTC (e.g., introducing broker, futures commission merchant).<sup>5</sup> However, CFTC Rule 1.35 seems to expand the traditional concept of member of an exchange by applying Rule 1.35 to buy-side entities who are members of a SEF or designated contract market (“DCM”) and not otherwise serving in a fiduciary capacity or required to register with the CFTC. Accordingly, the FHLBanks respectfully request that the CFTC reconsider whether buy-side entities, such as the FHLBanks, that are subject to the recordkeeping obligations under Rule 45.2, that do not serve in a fiduciary capacity, and that are not otherwise required to register with the CFTC, should be subject to Rule 1.35.

---

<sup>5</sup> We note that the CFTC’s Division of Market Oversight has issued guidance clarifying that “trading privileges” is “generally understood to mean the rights granted to a person by a SEF to directly, or through an independent software vendor, effect transactions on the SEF.” See CFTC Division of Market Oversight, Guidance on Application of Certain Commission Regulations to Swap Execution Facilities (Sept. 30, 2013), available [here](#).

## 2. *Intermediary Trade Execution Services*

Even if it is determined that direct membership in a SEF or DCM subjects a buy-side customer to the requirements of Rule 1.35, we note that various intermediary trade execution alternatives have evolved that provide market participants access to, and an ability to execute trades on, an exchange as a customer of that intermediary and not as direct members of a SEF or DCM. The FHLBanks request that the CFTC confirm that, for purposes of Rule 1.35, the definition of “member” does not encompass entities that act in a traditional customer capacity utilizing such an intermediary.

### **C. Uncertainty With Respect to Certain Aspects of Rule 1.35**

#### 1. *Scope of Rule 1.35*

*Scope of Commodity Interest Transactions.* Rule 1.35 applies to market participants that are members of a SEF or DCM, among others. On its face, Rule 1.35 is not limited to commodity interest transactions executed on or through a SEF or DCM in which a market participant is a member. Rather, a broad reading of Rule 1.35 would apply to all commodity interest transactions of such SEF or DCM member. We believe that this expansive application of the Rule 1.35 recordkeeping obligations to all commodity interest transactions of a SEF or DCM member is overly broad and unduly burdensome. Accordingly, we request that the CFTC clarify that the scope of Rule 1.35, for purposes of members of a SEF or DCM, is limited to trades that such member conducts on a SEF or DCM.

*Scope of Records Required.* Rule 1.35 requires retention of “all . . . written communications provided or received concerning quotes, solicitations, bids, offers, instructions, trading, and prices that lead to the execution of a transaction in a commodity interest and related cash or forward transactions.” (Emphasis added.) We request that the CFTC provide clarification on the following points with respect to trades that may be executed on a SEF using the request for quote (“RFQ”) trade execution method:

- (a) if a market participant obtains several quotes from different dealers and executes a trade with one of those dealers, please confirm that such market participant would be required to maintain only records/information required by Rule 1.35 in connection with the successful quote that results in an executed trade and not other quotes that may have been obtained; and
- (b) please confirm our understanding that if a market participant obtains quotes for a particular transaction, but none of the quotes results in an executed swap transaction, such market participant is not required to maintain records of such quotes.

## 2. *Original Source Documents*

Rule 1.35 imposes an affirmative obligation to retain all documents on which trade information is originally recorded, whether or not such documents must be prepared pursuant to CFTC regulations or the rules or regulations of the relevant SEF. CFTC Regulation 45.2 does not impose this requirement. The FHLBanks request guidance regarding what documentation qualifies as original source documents for electronic trading, and in particular, that a Portable Document Format (“PDF”) of certain documents qualifies as an original source document.

## 3. *Related Cash or Forward Transactions and Searchability*

Rule 1.35 requires that market participants retain records for a swap transaction as well as any “related cash or forward transaction” in a “form and manner identifiable and searchable by transaction.” Rule 1.35 defines the term “related cash or forward transaction” as “a purchase or sale for immediate or deferred physical shipment or delivery of an asset related to a commodity interest transaction where the commodity interest transaction and the related cash or forward transaction are used to hedge, mitigate the risk of, or offset one another.” (Emphasis added.) While we think this requirement is relevant to related physical transactions, it is not clear to us why there is any value in requiring such recordkeeping for related financial transactions. Accordingly, we believe the scope of “related cash or forward transactions” should not include financial transactions that the FHLBanks may enter into in connection with a swap, such as an advance to a member or bond issuance transaction (which do not, in our view, involve “physical shipment or delivery”). Clarification of this point would be very helpful. Further, it is unclear what requirements must be met for records of such related transactions to be sufficiently tied to the swap transaction and “searchable” in compliance with Rule 1.35.<sup>6</sup>

Consequently, the FHLBanks seek the following:

- (a) the CFTC’s determination that the scope of Rule 1.35 is limited to related cash or forward transactions in physical commodities requiring physical shipment or delivery, and that Rule 1.35 does not also cover related financial transactions, such as the FHLBanks’ advances and bond issuance transactions, among others; and
- (b) if Rule 1.35 is determined to also cover related financial transactions, then the FHLBanks seek the CFTC’s guidance regarding how the “searchability” requirement of Rule 1.35 applies to such related cash or forward transactions. We note that the FHLBanks already

---

<sup>6</sup> According to the CFTC, an entity would be in compliance with the recordkeeping standard under Regulation 1.35 if a record-keeper can readily access and identify records pertaining to a transaction or counterparty by running a search of raw data. *See* Adaptation of Regulations to Incorporate Swaps – Records of Transactions, 77 Fed. Reg. 75,523, 75,531 (Dec. 21, 2012).

Ms. Melissa Jurgens  
April 17, 2014  
Page 6

maintain records of transactions that are related to, or executed in connection with, their swap transactions. However, the FHLBanks are concerned with whether such records meet the searchability requirement; namely, whether such related records are sufficiently linked to the records of the FHLBanks' swap transactions. We also note that the FHLBanks' recordkeeping systems for member advances is highly customized and would require costly modifications to make such member advance records "searchable" in connection with any related swap transactions.

\* \* \*

Again, we urge the Commission to undertake a cost-benefit analysis with respect to each of the issues raised in this letter. We appreciate the opportunity to comment. Please contact Warren Davis at (202) 383-0133 or [warren.davis@sutherland.com](mailto:warren.davis@sutherland.com) with any questions you may have.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Warren Davis". The signature is fluid and cursive, with a large initial "W" and "D".

Warren Davis, Of Counsel  
Sutherland Asbill & Brennan LLP

cc: FHLBank Presidents  
FHLBank General Counsel