HUNTON & WILLIAMS

HUNTON & WILLIAMS LLP
1900 K STREET, N.W.
WASHINGTON, D.C. 20006-1109

TEL 202 • 955 • 1500
FAX 202 • 778 • 2201

FILE NO: 76142.000002

January 24, 2011

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

VIA ELECTRONIC MAIL

Re: *Rulemaking Establishing the Duties of Swap Dealers and Major Swap Participants under Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act*

Dear Secretary Stawick:

On behalf of the Working Group of Commercial Energy Firms (the "Working Group"), Hunton & Williams LLP respectfully submits this letter in response to the Commodity Futures Trading Commission's (the "Commission") request for comment concerning the Commission's Notice of Proposed Rulemaking on Regulations Establishing and Governing the Duties of Swap Dealers and Major Swap Participants (the "Proposed Rules").[1]

The Working Group is a diverse group of commercial firms in the energy industry whose primary business activity is the physical delivery of one or more energy commodities to others, including industrial, commercial and residential consumers. Members of the Working Group are energy producers, marketers and utilities. The Working Group considers and responds to requests for public comment regarding legislative and regulatory developments with respect to the trading of energy commodities, including derivatives and other contracts that reference energy commodities.

Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Act") vests the Commission with new and expanded authority to regulate a wide array of participants in swap markets. These market participants will have a significant burden to develop measures to assure compliance with both substantive and procedural requirements under the Commission's new regulations set forth under the Act. Such regulations are the subject of several key proposed rulemakings, including the instant one.

[1] *Regulations Establishing and Governing the Duties of Swap Dealers and Major Swap Participants*, 75 Fed. Reg. 71,397 (Nov. 23, 2010).

I. COMMENTS OF THE WORKING GROUP.

A. GENERAL.

1. COMMISSION SHOULD AFFORD MORE DISCRETION TO FIRMS TO DESIGN AND IMPLEMENT COMPLIANCE MEASURES UNDER THE PROPOSED RULES.

The Working Group applauds the Commission's recognition in the release to the Proposed Rules that "an individual firm must have the flexibility to implement specific policies and procedures unique to its circumstances."[2] The Working Group also supports the Commission's observation that swap dealers and major swap participants have operations that vary in size and complexity.[3] The Commission characterizes the Proposed Rules as "general parameters for . . . a swap dealer's or major swap participant's risk management program."[4] The Commission left firms some discretion as to the details of designing and implementing risk management and compliance programs. However, the "general parameters" still retain a notable amount of requirements that are both granular and prescriptive.

Effective regulations must strike a balance between rigorous, detailed requirements and the flexibility necessary for firms to comply efficiently and effectively. We believe that the Commission has asked for a level of detail not provided for in Title VII of the Act regarding the requirements set forth by the Proposed Rules. Many elements of the Proposed Rules will not increase the effectiveness of risk management and compliance measures and will impose substantial costs on market participants.

The Proposed Rules should be revised to afford firms greater discretion in designing and implementing compliance measures. Firms are in the best position to craft risk management and compliance programs that are the most efficient and effective given the unique nature of their business. Accordingly, a set of generic and prescriptive "best practices" for risk management and compliance measures might not result in the most effective and efficient program for an individual firm, particularly where such "best practices" are imported from an unrelated industry.

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2 *Proposed Rules* at 71,399.

3 *Id.*

4 *Id.*

Many firms that may come within the definition of "swap dealer" or "major swap participant" already have robust compliance and risk management programs in place, particularly those in regulated industries such as energy. Certain firms, for example, already have compliance and risk management departments to address the current rules and regulations of the Commission as well as the rules and regulations of other regulators.[5] Any proposed rules addressing compliance or risk management issues should be flexible enough to allow firms to leverage their existing compliance and risk management measures. New regulations promulgated by the Commission under the Act should not cause firms to add entirely new compliance or risk management infrastructure. Instead, the Commission should establish principles that further the requirements of the Act, but allow firms flexibility in how they meet those objectives.[6]

2. STANDARDIZATION IN REPORTS TO BE DELIVERED TO THE COMMISSION.

Where the filing of reports with the Commission is required, the Working Group respectfully suggests that the Commission provide a standard form of report. Standardized reporting requirements mutually benefit the Commission and market participants. For the Commission, they facilitate the efficient review and evaluation of what might be thousands of reports. For market participants, they provide necessary guidance on how to prepare reports, which will inform certain aspects of compliance programs.[7]

It should be noted that a standardized set of reporting criteria still leaves a large amount of discretion to individual firms. Each firm must evaluate what data is responsive to the report's requirements. Firms also must make determinations as to what disclosure is material (and what information must be included to make disclosures not misleading).

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[5] Certain firms, for example, already have compliance and risk departments to address current rules and regulations of the Commission. Other firms have compliance and risk units as brokers or dealers under the Securities Exchange Act of 1934, as amended (the " '34 Act"), while other companies have robust compliance measures as they are regulated by banking authorities, insurance authorities, FERC, state agencies, and, in the electric industry, the North American Electric Reliability Corporation. Public reporting companies under the '34 Act have additional compliance measures in place to remain compliant with the Sarbanes-Oxley Act.

[6] As the Commission's cost-estimates reflect incremental costs, the Commission appears to be assuming that firms will already leverage existing compliance and risk measures.

[7] Ultimately, the Commission and market participants will benefit from a reporting paradigm that is fully integrated. An integrated reporting system eliminates the unnecessary repetition of information (and the attendant data and physical storage issues). It also promotes a unified approach to reporting.

B. REQUIRED RISK MANAGEMENT PROGRAM.

1. PROVISION OF RISK MANAGEMENT POLICES TO THE COMMISSION.

The Commission solicits comments as to whether copies of risk management policies and procedures should be submitted to the Commission.[8] The Working Group respectfully recommends that they not be. In the alternative, firms might be asked to attest that such policies and procedures exist and that they meet the requirements of the Act and the Commission's regulations. The utility of the Commission having copies of such policies and procedures is uncertain. They should be made available upon request of the Commission or its staff, but having regulated firms provide them to the Commission does not appear to serve any utility given the high volume of reports the Commission is likely to receive. The Working Group requests that the Commission ensure that any policies and procedures provided to the Commission be kept confidential. The Working Group is concerned that certain information contained in reported policies and procedures might expose swap dealers and major swap participants to legal and reputational risk if made public and that certain information contained in the reports will constitute proprietary trade secrets.

2. RISK MANAGEMENT PROGRAMS SHOULD BE LIMITED TO SWAP TRADING ACTIVITIES.

The Proposed Rules provide that a swap dealer or major swap participant must establish a risk management program "reasonably designed to monitor and manage the risks associated with its business as a swap dealer or major swap participant."[9] However, the Proposed Rules also state that "business activities engaged in and risks faced by one affiliate may increase the risk exposure or alter the overall risk profile of another affiliate or the entity as a whole, and that, to be effective, a risk management program must protect against the risks resulting from the activities of interconnected or otherwise related entities."[10] Accordingly, each swap dealer and major swap participant is required to demonstrate "that, to the extent possible, it is taking an integrated approach to risk management at the consolidated entity level."[11]

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8 *Proposed Rules* at 71,400.

9 *Id.*.

10 *Id.* at 71,399.

11 *Id.*

The express language of certain proposed regulations does not limit their scope to a swap dealer or major swap participant's swaps activities. Proposed CFTC Rule 23.600(b)(1) states: "each swap dealer and major swap participant shall establish…a system of risk management policies and procedures designed to monitor and manage the risks associated with the business of the swap dealer or major swap participant." While Proposed CFTC Rule 23.600(c)(1) states: "the Risk Management Program should take into account market, credit, liquidity, foreign currency, legal, operational, settlement, and any other applicable risks together with a description of the risk tolerance limits set by the swap dealer or major swap participant." As drafted, both of these rules can be interpreted to mean that a firm's risk management program should cover any and all business conducted by a swap dealer or major swap participant, regardless of whether it is swaps related. While under certain circumstances, a broad approach to risk management across all business lines might be thought to be "best practices" for enterprise risk management, in many other instances, it might not be appropriate to impose the Proposed Rule's requirements on non-swaps activities.

The Proposed Rules also can be read to give the Commission authority over entities and activities covered by a commercial energy firm's enterprise-wide risk management program that it might not have the jurisdiction or the necessary expertise to regulate or oversee. Requiring an enterprise-wide risk management program as well as requiring such program to have certain characteristics will place obligations and limitations on activities that are unrelated to commodities markets and on entities that do not transact in commodities markets.[12] For example, as currently drafted, the Proposed Rules can be read to require a commercial energy firm to ensure that their exploration and production business is covered by the risk management program even though the activities of that line of business are outside the Commission's jurisdiction.

The Working Group requests that the Commission make clear that the Proposed Rules do not mandate an enterprise-wide risk management program. Given the complex legal and regulatory obligations imposed on many commercial energy firms, the determination of the scope of a comprehensive risk management program should be left to the individual company.[13]

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[12] The Proposed Rules should clarify that information on entities and activities outside the Commission's jurisdiction supplied to the Commission in connection with a risk management program is only required in order to provide an accurate accounting of the risk management program and that the provision of such information does not grant the Commission jurisdiction over such entities and activities.

[13] This is consistent with the Commission's statement that it recognizes that "an individual firm must have the flexibility to implement specific policies and procedures unique to its circumstances." *Proposed Rules* at 71,399.

Specifically, the Working Group recommends that proposed regulation 23.600(b)(1) be redrafted to read as follows:

> Each swap dealer and major swap participant shall establish, document, maintain and enforce a system of risk management policies and procedures designed to monitor and manage the risks associated with the swaps activities of such swap dealer or major swap participant.

Also, proposed regulation 23.600(c)(1)(ii) should be redrafted to read as follows:

> The Risk Management Program may take into account swaps-related risks posed by affiliates and take an integrated approach to risk management at the consolidated entity level to the extent the Chief Compliance Officer or other senior officer deem necessary to enable effective risk and compliance oversight of the business trading unit.

Finally, the definition of "business trading unit" in proposed regulation 23.600(a)(2) should be redrafted as follows to limit its scope to the swaps activities of a swap dealer or major swap participant:

> This term means any department, division, group, or personnel of a swap dealer or major swap participant or any of its affiliates, whether or not identified as such, that performs or is involved in, with respect to swaps activities, any pricing, trading, sales, marketing, advertising, solicitation, structuring, or brokerage activities on behalf of a registrant.

The Working Group believes that this question of scope must be clarified as an initial matter. Otherwise, it will be impossible for firms to evaluate the feasibility of designing and implementing risk management policies and procedures within the time frames required under the Act and the Commission's regulations.

3. MARKET RISK MEASURES.

The Working Group is unsure of the value of any requirement that positions be recorded to a general ledger on a daily basis.[14] Enterprise-wide risk management and compliance measures must work together with other accounting and reporting requirements. Very few commercial firms, if any, consolidate the accounting ledger or other accounts of physical and financial positions on a daily basis. For some firms, such consolidation might happen only on a monthly basis. To the extent that valuations are tracked daily, that would ordinarily take place in the firm's trading or risk management system, not the general ledger system. The general ledger

[14] Proposed CFTC Rule 23.600(c)(4)(i)(C).

system would typically receive results from the trading or risk management system in the normal course of the accounting cycle – typically monthly.

Among the items identified in the release to the Proposed Rules as a component of market risk is the sensitivity of options. The release and the Proposed Rules suggest that all components of market risk should be measured daily.[15] The Working Group recommends that metrics for options, particularly the sensitivity for options, be measured on a frequency less than daily. Such metrics can require complex calculations, some of which must be done outside the trading or risk management system.[16]

The Proposed Rules also provide that a risk management unit should be able to provide reports to senior management or the firm's governing body immediately upon the detection of a material change in market risk.[17] The Working Group recommends that firms have discretion to determine what constitutes a material change in market risk, the form and content of such a report and the timing for the delivery of a report.

4. RISK MANAGEMENT PROGRAM AUDITS SHOULD BE CONDUCTED ANNUALLY.

The Working Group understands that the Commission's intention is to make certain that a risk management program addresses necessary issues, the company adheres to such program and that senior management is informed as to relevant risk management issues. However, the quarterly risk management program audit and review required by the Proposed Rules might not be the best means to ensure that those goals are accomplished.[18]

Requiring a quarterly audit and review of a risk management program, the results of which must be reported to an entity's senior management and governing body, is burdensome, costly and unnecessary. In the collective experience of members of the Working Group, when conducting a similar audit with a far more defined set of criteria than published in the Proposed

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[15] Proposed CFTC Rule 23.600(c)(4)(i)(A).

[16] The Working Group also notes that similar complexity can be present when haircuts are adjusted for purposes of valuing collateral, a suggested component of liquidity risk.

[17] Proposed CFTC Rule 23.600(c)(2)(i).

[18] Proposed CFTC Rule 23.600(e)(2).

Rules, the average firm commits well over 300 man-hours to such audit.[19] Under the Proposed Rules, valuable resources and staff who could otherwise be tasked with monitoring a commercial energy firm's compliance with a risk management program will be used on the frequent audits and the construction of reports with likely little resulting improvement in the performance of the risk management program.

The Working Group respectfully suggests that both the frequency and the scope of audits of the risk management program be left to the discretion of the firms, so long as such audits are effective and are conducted at least annually. This regime would provide the desired results without the unnecessary cost and administrative burden imposed by the Proposed Rules.

The Commission should clarify what the governing body or senior management is expected to do with any and all information and reports delivered under the Proposed Rules. To assure directors or management receive useful information, it is instructive to understand their responsibilities upon receiving such information.

5. RISK MANAGEMENT PROGRAM REPORTS SHOULD BE PRODUCED ANNUALLY AND PROVIDED TO THE COMMISSION UPON REQUEST.

As with a mandatory quarterly audit and review of a risk management program, requiring quarterly risk exposure reports to an entity's senior management and governing body is burdensome, costly and unnecessary. With proper compliance and risk management policies in place, an annual risk exposure report coupled with a requirement to provide such a report in the event of material change in market risk would serve to keep an entity's senior management and governing body adequately informed without the cost burden imposed by a quarterly report.

In addition, any risk exposure report should be supplied to the Commission upon request and not when provided to an entity's senior management and governing body. Given the high volume of reports the Commission is likely to receive, it is unlikely that it will have the resources or need to review each (or many) submission. Therefore, a frequent periodic submission requirement will only serve to drain the Commission's resources without providing any substantive benefit. Requiring risk exposure reports be made promptly available to the Commission upon request would provide the Commission with access to the necessary information without imposing the costs associated with a periodic submission requirement on both the Commission and market participants.

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[19] For a complete discussion of the Working Group's cost estimates regarding the Proposed Rules, see Section II.E. below, Schedule A attached hereto and the Working Group's comment letter regarding the estimated cost of the Proposed Rules, filed with the Commission on December 15, 2010.

Given that risk exposure reports will likely not be considered confidential information protected from Freedom of Information Act requests, the Working Group is concerned that certain of the required information fields might expose swap dealers and major swap participants to legal and reputational risk if made public.[20] Moreover, the report may force firms to make disclosures prior to having remedial actions put into place to address market risks. The Working Group requests that the Commission take steps to ensure that the information contained in such reports remains confidential when they are submitted to the Commission.

6. LIMITS: MONITORING; POSITION LIMITS PROCEDURE TEST AND REPORTS.

The Proposed Rules provide that firms must "monitor each trader throughout the trading day to prevent the trader from exceeding any limit to which the trader is subject."[21] Compliance with any internal trading limits set by a firm is best monitored at a desk level. Generally, individual trading desks are responsible for trading a certain class or certain classes of instruments. Accordingly, the proper level at which to monitor compliance with internal limits on positions held in any one product or class of products would be at the desk level and not the trader level. Monitoring compliance with limits at the trader level would be overly burdensome and would not provide the proper perspective on compliance with internal trading limits.

In addition, position limits are applied at the entity or possibly enterprise level, not at the trader or desk level. It is not possible to determine whether transactions that individual traders enter into violate position limits without placing the transactions in the context of an entire portfolio and any relevant hedge exemptions. Accordingly, swap dealers and major swap participants should monitor compliance with position limits in the context of their aggregate swaps and futures portfolio not on a trader-by-trader basis.

Under the Proposed Rules, swap dealers and major swap participants are required to report any detected violations of applicable position limits to an entity's governing body and the Commission.[22] Without limiting the duty to report violations of position limits to material violations, this requirement would place an undue burden on market participants and the

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[20] The information contained in the annual report does not appear to fit within the of types of confidential information listed in CFTC Rule 145.5.

[21] Proposed CFTC Rule 23.600(d)(4).

[22] Proposed CFTC Rule 23.601(e).

Commission. For example, a minor and inadvertent one-time violation of position limits is not a material event, and market participants are frequently informed of any such violation by a Designated Contract Market ("DCM") days after it occurs.[23] As such a violation is not material, reporting it to a board of directors would only serve to divert a governing body's focus and resources from consequential matters. Only when a violation might result in material regulatory action should a governing body be advised. The utility of alerting a governing body of non-material violations of position limits is unclear at best.

In addition, the reporting of on-exchange violations of position limits to the Commission is already done by DCMs and will likely be the responsibility of swap execution facilities as well. Thus, requiring swap dealers and major swap participants to report on-exchange violations will only serve to inundate the Commission with redundant information, placing an additional burden on the Commission with no recognizable benefit.[24]

The Proposed Rules also require swap dealers and major swap participants to provide quarterly reports to the entity's senior management and governing body on compliance with applicable position limits.[25] Swap dealers and major swap participants must also conduct monthly tests of their position limit procedures.[26] Like with the required quarterly risk exposure reports and quarterly risk program audits, the frequency of the position limits compliance reports and audits would impose a substantial burden on swap dealers and major swap participants by diverting valuable risk management resources, while likely providing little to no improvement in a swap dealer or major swap participant's compliance with applicable position limits.

The Working Group respectfully suggests that the Commission require (i) annual reports to the entity's senior management and governing body on compliance with applicable position limits and (ii) tests of position limit procedures on a semi-annual basis (or on a more frequent basis as the firm might determine to be effective).

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[23] In addition, it is common practice in futures markets to allow market participants to file for a hedge exemption days after exceeding a position limit to rectify a violation of positions limits.

[24] The Working Group acknowledges that if position limit rules require the aggregation of exchange-traded swaps and over-the-counter swaps, that swap dealers and major swap participants should be required to report position limit violations that occur because of over-the-counter swaps.

[25] Proposed CFTC Rule 23.601.

[26] *Id.*

The Commission solicits comments in the release to the Proposed Rules about the amount of time required for firms to design and implement procedures to monitor compliance with position limits. Without resolution on the various proposals for position limits, this is not a question for which a definitive answer can be supplied. However, the Working Group submits the observation that, as more complex requirements are included in position limit rules, such as the requirement to convert bespoke bilateral transactions into futures-equivalents, substantially more time will be required.

7. SEPARATION OF RISK MANAGEMENT AND BUSINESS STAFF.

The Proposed Rules require swap dealers and major swap participants to separate "personnel in the business trading unit from personnel in the risk management unit."[27] The Working Group requests clarification as to whether such separation requires separate and independent oversight of business unit and risk management unit personnel or actual physical separation of such personnel. Separate oversight of business and risk management personnel would comport with industry best practice. It would avoid potential conflicts of interest and help engender a culture of compliance. However, requiring actual physical separation of risk management and business unit personnel would contradict industry best practice, and would severely limit risk management personnel's ability to properly implement a risk management program. In order to ensure a culture of compliance, risk management personnel need a functional working relationship with and the ability to interact with their business unit counterparts. Requiring physical separation will silo risk management and business units making it next to impossible to conduct effective risk management.

The release for the Proposed Rules mentions that the personnel responsible for recording transactions in the books of a firm cannot be the same as those responsible for executing transactions.[28] However, the Proposed Rules do not include this specific requirement. It appears to be covered by the general requirement that risk management be independent from the business trading unit. If the reference to recording transactions in the books of a firm is intended to refer to entries into the general ledger system, then the Working Group agrees that this process should be subject to the usual segregation of duties requirements that protect the general ledger system throughout.[29] However, there is no reason to prohibit individuals who execute transactions from entering the information regarding such transactions into a firm's trading or risk management

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[27] Proposed CFTC Rule 23.600(d)(10).

[28] *Proposed Rule* at 71,399 and 71,400.

[29] *Id.* at 71,399.

system. The Working Group requests the Commission clarify the personnel requirements for transaction entry, if any. If the Commission elects to impose any such requirements, the Working Group respectfully requests that the requirements allow an ample degree of flexibility to allow swap dealers and major swap participants to account for the new "real-time" reporting requirements imposed under the Act, the proposed swap confirmation rules[30] and the variety of ways in which swaps are executed.

8. NEW PRODUCT POLICY.

Under the Proposed Rules, swap dealers and major swap participants must adopt a new product policy which, among other things, requires (i) an analysis of the risks associated with any new product to such entity and its affiliates and (ii) an analysis of any changes to the risk management policy required if such new product is offered."[31] This requirement raises many difficult interpretative questions. For example, at what point do small changes to an existing product constitute the creation of a new product? When does a novel trade, which may be traded infrequently, constitute a new product? Does a "new" product need to be offered to multiple counterparties? How does this rule apply to bespoke swaps?

To address the potential ambiguity raised by this requirement, the Working Group respectfully requests that the Commission make an affirmative statement that the determination of what constitutes a new product and the determination of the appropriate approval process for such product is left to the discretion of the swap dealer or major swap participant. This approach is consistent with the Commission's traditional principles-based approach to regulation.

With regard to the recommended approach, the Working Group respectfully suggests that the Commission's regulations mandate that (i) before a swap dealer or major swap participant may offer a new product, they must conduct due diligence that is commensurate with the risks associated with such product and (ii) the decision to offer the product be approved by appropriate risk management and business unit personnel. In addition, the Commission might provide that the determination as to whether a product is "new" should be left to the swap dealer or major swap participant, who should consider factors such as whether the product contains structural or pricing variations from existing products, whether the product is targeted at a new class of

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30 *Confirmation, Portfolio Reconciliation, and Portfolio Compression Requirements for Swap Dealers and Major Swap Participants*, 75 Fed. Reg. 81,519 (Dec. 28, 2010).

31 Proposed CFTC Rule 23.600(c)(3). This proposed rule does not limit the scope of the new product policy to swaps. The Working Group respectfully requests that the Commission clarify that new products that are not swaps would not be subject to this rule.

customers, whether it is designed to address a new need of customers, whether it raises significant new legal, compliance or regulatory issues, and whether it, or the manner in which it would be offered, would materially deviate from standard market practices.[32]

This approach to the approval of new products is consistent with existing regulatory guidance regarding the approval of new complex structured financial transactions. Interagency guidance issued by the Securities Exchange Commission and banking regulators sets forth a similar principles-based regime.[33] And, though the Working Group would generally caution the Commission against transposing regulatory requirements created for financial entities onto commercial firms, the Working Group believes that the existing interagency guidance is flexible enough to be appropriate for application to commercial firms that are deemed swap dealers or major swap participants.

9. TECHNICAL COMMENTS REGARDING THE PROPOSED RULES.

Proposed Rule	Description of Requirement	Comment
23.600(c)(1)(i)	Risk tolerance limits reviewed by senior management (quarterly) and by governing body (annually).	Risk tolerance limits should be reviewed no more frequently than semi-annually by senior management and need not be reviewed by the governing body at all. The responsibility of risk limits should reside with management of the trading unit. Companies should not be restricted in their ability to delegate the responsibility to set and monitor internal risk tolerance limits. Following such proper delegation, further review by the upper levels of the organization is not necessary.
23.600(c)(2)	Risk exposure report to senior management (quarterly) and to governing body (quarterly)- immediately upon material change; furnished to the Commission within five business days.	See comments of the Working Group at Section I.B.5 addressing the unnecessary frequency and delivery to the Commission.

[32] The determination of what constitutes "market practices" should also be left to a firm to decide.

[33] *Interagency Statement on Sound Practices Concerning Elevated Risk Complex Structured Finance Activities*, 72 Fed. Reg. 1372 (January 11, 2007).

Proposed Rule	Description of Requirement	Comment
23.600(c)(4)(i)(B)	Pricing models have been validated by independent persons.	The Working Group respectfully requests that this rule be clarified to permit a group independent of the relevant trading group, though not external to the company, such as risk management, to review pricing models.
23.600(c)(4)(i)(C)	Reconciliation to general ledger daily.	See comments of the Working Group at Section I.B.7. addressing the unnecessary frequency of reconciliation.
23.600(c)(4)(iv)(A)	Daily measurement of capital exposed to fluctuations in foreign currency.	The frequency of measurement of capital exposed to fluctuations in foreign currency should be left to individual firms to determine based on their circumstances.
23.600(c)(4)(vi)(C)	Reconciliation of operating and information systems.	Further explanation is needed. Information is reconciled, but systems might not be.
23.600(c)(5)(iii)	Investigation into the adequacy of financial resources and risk management procedures of any central counterparty.	If central counterparties are regulated as derivatives clearing organizations, these items should be monitored by the Commission. This requirement should be unnecessary.
23.600(c)(6)	Compliance with capital and margin requirements.	This item is superfluous, but otherwise not objectionable. If the Commission wants to cross-reference other regulatory requirements, it should do so consistently.
23.600(d)(1)	Governing body approves all trading policies.	A governing body should be required to approve general macro-level policies that allow the delegation of authority to develop specific policies to others. For example, the development of risk management policies should be permitted to be delegated to a risk management committee. Delegation allows firms to place responsibility with individuals who have the requisite expertise.
23.600(d)(2)	Traders can only execute trades with counterparties for whom credit limits have been established.	The Commission should allow swap dealers and major swap participants the discretion to make exceptions to this requirement for certain limited risk transactions.

Proposed Rule	Description of Requirement	Comment
23.600(d)(4)	Continual monitoring of compliance with all limits.	While internal trading limits are monitored with some frequency throughout the day in the normal course, the Commission might clarify that "continual" does not mean every second of the trading day. Requiring every trader be continuously monitored with regards to every internal trading limit would not result in drastically improved compliance performance, especially given that it would be prohibitively costly to comply with.
23.600(d)(4)	Continual monitoring of traders to prevent traders from incurring undue risk.	The determination of whether a risk is appropriate and the degree of monitoring for such risk is best left to individual firms based on their unique circumstances.
23.600(d)(7)	Trade discrepancies are brought to the immediate attention of management of the business unit.	Please further define "trade discrepancy" and provide criteria to understand what constitutes "immediate attention." Also, there should be some materiality qualifier so that technical errors can be resolved below the management level.
23.600(d)(8)	Risk management review of broker statements, reconciliation of actual charges to estimates, review of commissions, initiation of payments to brokers.	These functions are not traditionally performed by a risk management group and nor should they be. The review of broker statements, reconciliation of actual charges to estimates, review of commissions, and initiation of payments to brokers have no direct relation to risk mitigation.
23.600(e)(1)	Review and testing of risk management program - quarterly or upon material change in business.	The Commission should provide more criteria to establish what "testing" meets the requirements of this proposed rule. It is possible that the "review" sufficiently meets the aim of this provision.
23.600(e)(2)	Analysis of adherence to and effectiveness of risk management program, recommendations for modifications - quarterly. Testing done by independent auditor (can be internal). Review of quarterly review by CCO, senior management and governing body.	Please see the comments of the Working Group at Section I.B.4. -5. about the selected frequency and need for review by senior management and the governing body.

Proposed Rule	Description of Requirement	Comment
23.601(e)	Implementation of "early warning system" on violation of position limits. Violations reported to governing body and Commission. Record keeping for "early warning system."	Only material violations of position limits should required to be reported to the Commission. Minor violations of position limits are best handled at the exchange or company level. In addition, firms should be given the discretion to self correct any violation of a position limit prior to reporting it to the Commission.
23.601(f)	Test adequacy of position limit system - monthly. Record keeping for tests.	Please see the comments of the Working Group at Section I.B.7. addressing the unnecessary frequency and related costs for such testing.
23.601(g)	Report on compliance with position limits - provided to CCO, senior management and governing body - quarterly.	Please see the comments of the Working Group at Section I.B.7. addressing the unnecessary review by senior management and the governing body and related costs for such review.
23.601(h)	Audit of Position Limit Procedures.	See comments of the Working Group at Section I.B.6. addressing the unnecessary frequency of such audits.
23.602(b)(1)	Designation of individual as responsible for supervision.	The responsibility for supervision is best not placed in a single individual, but rather a reporting line. The Working Group questions this approach given that the existing duty to supervise under CFTC Rule 166.3 has never been specific to an individual.
23.603(b)(5)	Maintenance of back-up facilities, systems, infrastructure and personnel.	As drafted, the Proposed Rule appears to require additional personnel be hired to staff back-up facilities. This requirement would require firms to hire two people for the same job. The Working Group suggests that the Proposed Rule be clarified to not require separate personnel to staff back-up facilities.
23.603(g)	Testing of business continuity and disaster plan - annual. Testing done by independent auditors.	The requirement for annual testing by independent auditors is costly. While disaster planning should be reviewed and tested, the expense of an audit is unnecessary.

Proposed Rule	Description of Requirement	Comment
23.606(a)(1)	Commission access to information about regulated entities swap portfolio.	Please clarify what is intended by requiring a firm to maintain records and documents for purposes of "disclosure" to the Commission. Firms easily understand making documents and information available for "inspection." Does the Commission intend for something different? If not, then perhaps the reference to disclosure should be omitted.
23.606(b)(1)	Information systems must capture and be able to produce "all information necessary to satisfy [a firm's] duties under the CEA and the Commission's regulations."	Under this requirement, each individual rule promulgated by the Commission requires that a covered entity have the systems in place to comply with such rule. As styled, this provision would require swap dealers and major swap participants to have information systems designed for each and every potentially applicable requirement under the CEA and the Commission's regulations. This would be wasteful and unnecessarily costly, as the process to determine compliance with this requirement would be extensive and many requirements do not require tailored systems to ensure compliance.

C. DILIGENT SUPERVISION REQUIREMENT.

The Proposed Rules require each swap dealer and major swap participant to diligently supervise its conduct as a swap dealer and major swap participant. Each swap dealer and major swap participant is required to "designat[e]… a person with authority to carry out the supervisory responsibilities of the swap dealer or major swap participant for all activities relating to its business as a swap dealer or major swap participant."[34] The Working Group respectfully requests that the Commission clarify that the "person with authority to carry out the supervisory responsibilities" is permitted to delegate such authority to ensure that the supervisory responsibilities are properly carried out.

The Proposed Rules also require a swap dealer or major swap participant to "use reasonable efforts to determine that all supervisors are qualified and meet such standards of training, experience, competence, and such other qualification standards as the Commission finds necessary or appropriate."[35] The Working Group respectfully suggests that the Commission

[34] Proposed CFTC Rule 23.602.

[35] *Id.*

allow firms to make reasonable determinations as to what constitutes "sufficient authority" and "qualified" given their individual business and corporate structure.

D. DISASTER RECOVERY PLANS.

The Working Group respectfully suggests that requiring all firms that might be deemed swap dealers and major swap participants to be capable of resuming operations in one-business day is overly ambitious. The Working Group recognizes that it might be crucial for market stability for certain systemically important swap dealers and major swap participants to be subject to a one-business day requirement.[36] However, requiring smaller, non-systemically important firms to have one-day preparedness for every foreseeable disaster comes with an enormous price tag when weighed against the corresponding benefit. Non-systemically important swap dealers and major swap participants should be permitted to determine the appropriate period for resuming their business operations based on their individual circumstances. The proper standard for swap dealers and major swap participants that are not crucial to market integrity should be the resumption of core operations within a reasonably prompt period of time.

E. THE COMMISSION'S COST ESTIMATE.

The Working Group filed a letter with the Commission on December 15, 2010 to separately address the Commission's estimates of the costs associated with the Proposed Rules. In general, the Working Group believes that the Commission is significantly underestimating the costs that market participants will incur in complying with the Proposed Rules.

In the release to the Proposed Rules, the Commission provides certain estimated burdens imposed by complying with the Proposed Rules.[37] Schedule A sets out itemized estimates by the Working Group of the burdens that a mid-sized commercial energy firm might incur to comply with the Proposed Rules.[38] As seen in Schedule A, the Working Group believes that the

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[36] The Working Group suggests that the Financial Stability Oversight Council might also offer guidance on disaster recovery requirements for systemically important swap dealers and major swap participants.

[37] *Proposed Rules* at 71,402.

[38] The audit estimates contained in Schedule A are based on the time needed to comply with an audit required by the Federal Energy Regulatory Commission ("FERC"). The FERC audit is narrower in scope and its requirements are more defined. The Working Group estimate reflects an assumption that the audits in the Proposed Rules will require 50% more time to complete than the FERC audit. This estimate represents the Working Group's most conservative estimate. The real cost could be substantially higher. The Working Group notes that the audit estimates contained in this comment letter are higher than the corresponding estimates in our earlier cost letter

Commission's estimated burden is quite understated. The Commission estimates, for the purposes of the Paperwork Reduction Act,[39] that the burden imposed by the Proposed Rules is $20,450. The Working Group Estimates that, at a minimum, complying with the Proposed Rules would cost at least $418,440, or over 20 times the Commission's estimate.[40] The Working Group respectfully suggests that the Commission, among other cost-saving measures, reduce the burden imposed by the Proposed Rules by reducing the frequency of the required audits and promoting delegation by the governing body to management and staff members with the requisite expertise. By doing so, the Proposed Rules would accomplish the regulatory goals of the Commission and would comply with President Obama's recent executive order which directs regulators to "select, in choosing among alternative regulatory approaches, those approaches that maximize net benefits."[41]

F. APPROPRIATE EFFECTIVE DATES.

The Commission has requested comments as to the appropriate effective date for the Proposed Rules. The Working Group respectfully recommends that the proposed regulations become effective 2 years after the later of (i) the effective date of regulations regarding the definitions of "swap dealer" and "major swap participant," and (ii) the effective date of the regulations regarding the definition of "swap." Market participants must know their status with respect to such definitions before determining their need to comply with the ultimate regulations based on those contained in the Proposed Rules.

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referenced above. The Working Group's current estimate represents a more complete review of all of the costs imposed by the proposed audits.

[39] The Paperwork Reduction Act defines burden as "the time, effort, or financial resources expended by persons ..., including the resources expended for-- reviewing instructions; acquiring, installing, and utilizing technology and systems; adjusting the existing ways to comply with any previously applicable instructions and requirements; searching data sources; completing and reviewing the collection of information; and transmitting, or otherwise disclosing the information." 44 U.S.C § 3502(b)(2) (2010).

[40] This estimate is based solely on the activities included in the Commission's estimate. As stated in the Working Group's December 15, 2010 letter, implementing a "comprehensive risk management program" that "protect[s] against the risks resulting from the activities of interconnected or otherwise related entities… [that] take[s] an integrated approach to risk management at the consolidated entity level" and provides "diligent supervision reasonably designed to achieve compliance with the CEA and Commission regulations" would cost at least $1,080,000 annually. (*Proposed Rules* at 71,399-400).

[41] Exec. Order No. 13563, 76 Fed. Reg. 3821 (January 18, 2011). The Working Group acknowledges, that as an independent agency, the Commission is not subject to the executive order. However, the Working Group encourages the Commission to adhere to President Obama's intent.

To give effect to the Commission's recognition that firms that might become regulated entities have varied business models,[42] the Commission should provide an extended transition period for firms that have not been prudentially regulated by a financial regulator and might require substantial corporate restructuring. This approach will allow firms to concentrate resources and attention to individual aspects of designing and implementing new risk management and compliance measures. It will also allow firms to spread costs out over time. For some firms, the new risk management and compliance requirements under the Act and the Commission's rules may be incremental and minor. However, for commercial firms, even "minor" requirements could require substantial investment. An extended transition period for such firms will also allow some time for the development of technologies to support the various information gathering, processing and reporting requirements under various new regulations proposed by the Commission.[43]

G. OPEN COMMENT PERIOD.

Given the complexity and interconnectedness of all of the rulemakings under Title VII of the Act, and given that the Act and the rules promulgated thereunder entirely restructure over-the-counter derivatives markets, the Working Group respectfully requests that the Commission hold open the comment period on all rules promulgated under Title VII of the Act until such time as each and every rule required to be promulgated has been proposed. Market participants will be able to consider the entire new market structure and the interconnection between all proposed rules when drafting comments on proposed rules. The resulting comprehensive comments will allow the Commission to better understand how their proposed rules will impact Swap markets.

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[42] *Proposed Rules* at 71, 399.

[43] For a full discussion of the Working Group's recommendation for proper transition periods for swap dealers and major swap participants please see the Working Group's comment letter on the Proposed Rules for Registration of Swap Dealers and Major Swap Participants filed with the Commission on January 24, 2011.

II. CONCLUSION.

The Working Group supports tailored regulation that brings transparency and stability to the Swap markets in the United States. We appreciate the balance the Commission must strike between effective regulation and not hindering the uncleared energy-based Swap markets. The Working Group offers its advice and experience to assist the Commission in implementing the Act. Please let us know if you have any questions or would like additional information.

Respectfully submitted,

/s/ David T. McIndoe
David T. McIndoe
Mark W. Menezes
R. Michael Sweeney, Jr.

Counsel for the
Working Group of Commercial Energy Firms

Schedule A

CFTC Estimates

Item	Burden per report (hrs)	Reports per year	Total est hours	Working Group Comment
Drafting etc. Risk Management Program	160	1	160	One-time filing, annual distribution, update as needed.
Quarterly risk exposure reports	8	4	32	
Qrtly doc. of Risk Management Testing	1	4	4	Requires quarterly audit. Required time grossly understated.
Doc. of Annual Position Limit Compliance Training and Audit	2	1	2	Requires actual training --1/2hour X # of trainees and time to develop training.
Qrtly doc. Position Limit Compliance	0.5	4	2	Requires quarterly audit. Required time grossly understated.
Documentation of Position Limit Violations	0.5	1	1	Effort per violation grossly understated.
Filing Emer. Contact info; annual doc Bus Continuity Testing	1	1	1	
Doc. Risk Assessment of New Products	3	1	3	Requirement not well defined. Incremental time could be grossly understated.
Estimated total hours			205	
Assumed cost per hour			$ 100	
Assumed cost per respondent			$ 20,450	

Working Group Estimates

Item	Revised est per report (hrs)	Reports	Revised est Total hours	Internal Audit Hours	Risk & Compliance Hours	IT	Management
Drafting etc. Risk Management Program			160				
Quarterly risk exposure reports			32				
Qrtly doc. of Risk Management Testing	388	4	1,552	300	28	40	20
Doc. of Annual Position Limit Compliance Training and Audit	15	1	15		15		
Qrtly doc. Position Limit Compliance	388	4	1,552	300	28	40	20
Documentation of Position Limit Violations	4	2	8		4		
Filing Emer. Contact info; annual doc Bus Continuity Testing	2	1	2		2		
Doc. Risk Assessment of New Products	6	1	6		6		
Estimated total hours			3,327				
Assumed cost per hour			**$ 120**	*The hourly cost estimate was developed for the Working Group's December 15, 2010 cost focused comment letter on this Proposed Rule. Management hours are assumed to cost $240.*			
Estimated cost per respondent			**$ 418,440**				