

October 25, 2013

**SUBMITTED ELECTRONICALLY**

Ms. Melissa Jurgens  
Secretary of the Commission  
Office of the Secretariat  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1151 21st Street, NW  
Washington, DC 20581-0001

**RE: Petition for Exemptive Relief and Interim No-Action Relief for Bank Holding Companies of Banks Eligible for the End-User Exception for Mandatory Clearing of Swaps**

Dear Ms. Jurgens:

The American Bankers Association (ABA)<sup>1</sup> has previously informed the Commodity Futures Trading Commission (CFTC) of a myriad of concerns about the expense and operational difficulties that our members are facing in trying to establish the necessary infrastructure to clear swaps. We are writing again to provide additional information and petition for exemptive relief and interim no-action relief for bank and savings and loan holding companies (collectively, BHCs) of the banks and savings and loans (collectively, banks) that are eligible for the end-user clearing exception. Specifically, we request that the BHCs of the end-user banks be treated the same and also be eligible for the clearing exception.

Currently, banks that use swaps to hedge or mitigate risk qualify for an exception from clearing requirements if they have total assets of \$10 billion or less. However, BHCs of those banks are not eligible for the clearing exception.

Many BHCs use swaps to hedge or mitigate risk the same way as the banks that are eligible for the clearing exception. Most commonly, the BHCs periodically obtain financing and use swaps to hedge the interest rate or other business risk associated with that financing. Those BHCs should not be treated differently from the end-user banks.

Accordingly, ABA asks that the CFTC provide exemptive relief from clearing for BHCs of banks that are eligible for the clearing exception. Since we understand that it might take the

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<sup>1</sup> The American Bankers Association represents banks of all sizes and charters and is the voice for the nation's \$14 trillion banking industry and its 2 million employees. Learn more at [www.aba.com](http://www.aba.com).

Commission some time to grant permanent exemptive relief, we ask for interim no-action relief so that those BHCs can continue to use swaps to hedge or mitigate risk.

## **Background**

The Dodd-Frank Act required the CFTC to consider whether to treat some banks the same as other end users and exempt them from clearing requirements.<sup>2</sup> On July 10, 2012, the CFTC adopted a final rule exempting banks with total assets of \$10 billion or less from the Dodd-Frank Act's swaps clearing requirements.<sup>3</sup>

However, the bank clearing exception is available only to banks. Many community banks also use swaps at the BHC level to hedge their risk. Currently those BHCs are not eligible for the end-user clearing exception.<sup>4</sup> The ABA has no reason to believe that this was anything other than an unintentional oversight during the legislative process, so exemptive relief would be appropriate.

Most commonly, BHCs of end-user banks periodically obtain financing and use swaps to hedge the associated interest rate risk. They may be engaged in issuing debt securities or borrowing transactions. These BHCs generally use the proceeds to finance their subsidiary bank. In order to hedge against interest rate fluctuations, those BHCs may use swaps to lock in a fixed cost of capital. Furthermore, the swaps used to hedge financing risk must be done at the BHC level in order to gain hedge accounting treatment.

The swaps used to hedge risk from financing transactions for these BHCs of end-user banks tend to be smaller notional amounts, for example \$10 million or less. These financing transactions have also tended to be infrequent – some BHCs have only used swaps to hedge risk every five years. However, in the current low interest rate environment BHCs may seek to enter into swaps more frequently to hedge against rising interest rates.

Clearing requirements add significant costs to establish the clearing infrastructure with middleware trade affirmation platforms as well as recurring maintenance and transactional costs. These costs would be disproportionate to the limited number, and notional amount of swaps used by these BHCs. The BHCs of the end-user banks are using swaps in this limited way to hedge or mitigate risk associated with floating rate financing. This limited use does not pose a systemic risk and these BHCs should be allowed to have the same clearing exception as other end-users.

## **Petition for Exemptive Relief**

The CFTC has authority under Commodity Exchange Act (CEA) Section 4(c) to grant exemptions that would “promote responsible economic or financial innovation and fair competition.” Swaps have become an important risk management tool for banks. It is important

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<sup>2</sup> Commodity Exchange Act (CEA) Section 2(h)(7)(ii).

<sup>3</sup> End-User Exception to the Clearing Requirement for Swaps, 77 Fed. Reg. 42560 (July 19, 2012) (hereinafter End-User Clearing Exception).

<sup>4</sup> See ABA Comment Letter on June 10, 2013 Clearing Deadline for Category 2 Entities dated June 8, 2013.

to maintain competition in the market and allow BHCs of end-user banks to hedge their capital costs economically.

Providing a clearing exemption for BHCs of community banks will enable them to finance their bank subsidiaries. The banks use this capital to support lending in their communities, including long-term fixed rate loans to small and middle market businesses. Thus, the exemption would also help maintain the longstanding U.S. tradition of an economy built on banking institutions of a variety of sizes.

Understanding the CFTC's concerns regarding continued fidelity to the purpose of the statutory provision, it would not be unreasonable to make the exemptive relief conditional. For example, the end-user clearing exception for banks is limited to swaps that are used to hedge or mitigate risk. There are also reporting requirements applicable to all end-users that elect the clearing exception. We anticipate that these same conditions would apply to a clearing exemption for the BHCs of the end-user banks.

### **Cost-Benefit Analysis**

Banks commonly operate under a holding company structure. In fact, 79% of all banks have holding companies.<sup>5</sup> As of June 30, 2013, there were 399 bank holding companies of banks with total assets less than \$10 billion that reported swaps.<sup>6</sup> Of those banks, 147 reported swaps only at the holding company level.<sup>7</sup> If those BHCs wanted to enter into new swaps to hedge interest rate risk for the future, they would have to clear those transactions. The costs to establish and maintain the clearing infrastructure coupled with the limited volume of swap transactions would make it uneconomical for these BHCs to use swaps to hedge.

Many other banks are also considering using swaps as a risk management tool. If the BHCs of community banks are not exempt from the clearing requirements, then they may leave floating-rate financing costs unhedged. This result would not be optimal from a business or regulatory perspective.

Swaps have become a useful tool for prudent risk management. The BHCs of end-user banks are also already subject to comprehensive supervision and regulation. Furthermore, their swaps transactions are a de minimis part of the swaps market. Failing to exempt them from the mandatory clearing requirement would subject them to significant costs that would outweigh any potential regulatory benefit.

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<sup>5</sup> Federal Financial Institutions Examination Council, Consolidated Reports of Condition and Income (Call Report), June 2013.

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

<sup>7</sup> Board of Governors of the Federal Reserve System, Consolidated Financial Statements for Holding Companies (FR Y-9C), June 2013.

## **Interim No-Action Relief**

Understanding that it may take an extended period of time to issue a formal exemption, ABA also asks the Commission to issue interim no action relief for BHCs of end-user banks during the time necessary to evaluate and take formal action on a permanent exemption.

The BHCs of banks that are eligible for the clearing exception are currently required to clear swaps. Since clearing makes the cost prohibitive for the limited number and size of their transactions, those BHCs have been essentially forced to stop using swaps to hedge their risk.

ABA has heard from many banks with BHCs that are interested in entering into swaps to hedge risks at the BHC level. Some correspondent banks have informed us, however, that they are finding it difficult to engage in swaps with BHCs of end-user banks and BHCs have told us that they are not engaging in swaps unless the CFTC provides relief. These institutions account for a truly de minimis amount of the bank swaps market and would not present market risk while the CFTC considers a formal exemption.

Providing interim no-action relief would enable regulators and market participants to pursue their common interest in a smooth transition to implement the new regulatory framework for swaps. Since the end-user clearing exception is limited to banks with total assets of \$10 billion or less, it might be appropriate to limit the exemption to BHCs that have bank subsidiaries with total combined assets of \$10 billion or less during this transition period.

## **Conclusion**

ABA continues to believe that a risk-based measurement would be the most appropriate measurement for the clearing exception. However, if the CFTC considers itself bound by an asset threshold, then bank holding companies of banks that have a clearing exception should be treated the same as their banks. Accordingly, ABA asks that the CFTC provide exemptive relief from clearing requirements for BHCs of banks that are eligible for the end-user clearing exception.

Please let me know if you have any questions or need additional information.

Regards,

Diana L. Preston  
Vice President and Senior Counsel  
Center for Securities, Trust & Investments  
American Bankers Association

cc:

CFTC Chairman Gensler  
CFTC Commissioner Chilton  
CFTC Commissioner O'Malia  
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